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A Global Approach to Insolvency within Multinational Groups of Companies

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Irit Ronen-Mevorach

Abstract

This work attempts to tackle the complex case of insolvencies within multinational corporate groups ("MCGs"), an issue currently poorly dealt with under contemporary international insolvency models. In its core lies the question of whether there is justification to 'link' between affiliates in their insolvencies either for procedural or substantive purposes in spite of them being separate legal entities, which are located in different countries. In addition, what sort of mechanisms could serve this end? Indeed, the thesis asserts that 'linking' is essential in many occasions, though various scenarios should be considered. Moreover, 'one size fits all' sort of approach will be deemed unfit. Thus, in order to solve this issue a universalist view is adopted, essentially looking at such cases with a worldwide perspective, accepting a certain degree of interference with the corporate form (a view termed here as 'a global approach'). The merits and reasons for embracing such mode of thought are demonstrated via examining the main 'insolvency goals' (of a system regulating international insolvencies) and asking whether a global approach is apt in dealing with them compared with a 'separable' territorial approach. This investigation reveals the advantages of a global approach to insolvencies within MCGs while proposing ways to overcome its potential flaws, so that eventually it will be able to offer a suitable comprehensive solution. It concludes by asserting that the 'battle' between the needs to link between affiliates and to maintain the corporate form can be reconciled by exercising a prudent and flexible global approach that will match the needs of the specific case. Finally, a set of propositions extracted from the discussion of the various insolvency goals are offered as guidance for future reforms of cross-border insolvency models.

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Some elements of this thesis, while still work in progress, were embodied into papers accepted for publication in Journal of Business Law (based mainly on part of chapter 5) and International Insolvency Institute (elements of chapters 4, 5 and 7).

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The contents of the thesis are based on my understanding of the law as at the end of June 2006.

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Introduction

Purpose and scope of work

This work is aimed at construing the specific case of insolvency[1] within a multinational corporate group (hereinafter: MCG[2]) and its realization under different possible corporate structures and scenarios. Thus far, the issue was somewhat neglected in major contemporary international approaches to cross-border insolvency. This work will attempt to fill this gap, and consider ways to link between the MCG's components in the event of insolvency. Though, it will bear in mind the critical question: namely, to what extent and in which way insolvency courts should or should not 'lift the veil' of the MCG's constituents or apply enterprise principles[3]. We will examine whether these actions facilitate the insolvency proceedings and help achieve fair results in the course of the MCG insolvency. We will also ask ourselves how this could be achieved where the enterprise is spread amongst different states. Our discussion will be directed towards attempting to construct pragmatic mechanisms for use as structured guidelines in such cases, while maintaining their correspondence to a variety of MCG failure situations, accurately reflecting their economic reality. In this regard we will address issues such as the advantages and disadvantages in imposing joint administration upon transnational insolvency proceedings, the problems of handling MCGs insolvencies whose affairs were commingled as well as issues such as the possibility to justly address issues of group liability and inter- company debts on the international level.

Background

Recent years have exhibited a growing number of multinational insolvency incidents resulting from the increase of internationally integrated businesses and globalization. These special cases posed new demands on the legal and economic systems yielding novel doctrines and models for addressing these special complex problems.

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[1] I will use the terms insolvency and bankruptcy interchangeably as they hold the same meaning.

[2] Although the term multinational enterprises ('MNE') is often used in the literature also with regard to corporate group this work will make use of the term 'MCG' since it avoids any confusion with enterprises or corporations that operate worldwide without incorporating separate entities. It is thought that 'MCG' better expresses the fact that two or more separate corporations are involved in these cases. For the discussion on the different forms of MCGs see *infra* chapter 1.

[3] Evaluating corporate groups according to the economic inter- relations within the group, regarding it as a single entity in various legal matters (see also note 5 *infra* chapter 3).

The multinational business failure may take many shapes: an insolvent company with an international network of branches, a company holding assets around the world or simply a company employing foreign employees or dealing with foreign creditors. These examples all involve a single debtor having worldwide operations or relations. However, the international insolvency scenario may take a more complex form: that of a failure within an MCG. In fact, the corporate group is the most typical structure of modern international enterprises[4]. The issue then no longer concerns only one debtor but rather a bundle of affiliated companies. These debtors, although legally separated, can in fact be tied together in various ways, including mutual transactions and cross guarantees or even through a single control directing all the companies as a united business. This form of insolvency elicits a whole set of complex legal issues that need to be resolved, which typically were not handled within the cross-border insolvency arena.

All insolvency cases (whether locally or internationally operated) share the fundamental goal of reducing the overall damage this unwelcome situation brings forth and enforcing the principle of equality between creditors. Another objective, occurring in some cases, is reorganization of the debtor or achievement of a scheme of arrangement between the debtor and its creditors. Therefore, the insolvency situation demands a collective and centralized treatment for all creditors' claims and other parties' interests. This need is augmented in the case of a multinational insolvency event in which realization of the above mentioned objectives becomes contingent upon cooperation on a broader scale – that of different countries and different jurisdictions.

Several approaches for handling multinational insolvency situations have been developed during the years. On the national level, a significant number of countries have recently introduced rules and procedures regarding aspects of cross-border insolvency, international co-operation and assistance. Naturally however, even the most modern local approaches are limited to their boundaries and depend on other jurisdiction laws and policies. Thus, a local initiative will always be limited in creating a truly systematic and harmonized international method for handling

[4] See note 24 *infra* chapter 1, and accompanying text.

multinational cases[5]. Although an ideal (yet improbable) solution such as an international treaty or even an international court applying single bankruptcy law is not within reach, several significant initiatives emerged on the international level, trying to bridge the universality and territoriality theories[6]. The three main initiatives are the EU Regulation on Insolvency Proceedings, which is a regional rather comprehensive regime for cross-border insolvencies[7]; The UNCITRAL Model Law on Cross-Border Insolvency, which is the broadest global framework currently at hand, though more limited in substance[8], and the ALI Principles of cooperation in transnational insolvency cases among the members of the North American Free Trade Agreement, which is a set of unofficial best-practice recommendations encouraging close coordination and cooperation[9].

These models principally embrace a modified univesalism approach, with the ultimate goal of achieving maximum cooperation for the international insolvency case[10]. Nonetheless, in the attempts to reconcile territorial interests and the differences among national laws, this goal may prove to be a tough one[11]. In addition, these models fail to adequately or comprehensively deal with the case of MCGs[12].

In the lack of any applicable model upon relevant parties (or when otherwise appropriate), ad-hoc solutions can also be applied. These tools usually take the form of either international agreement drafted and concluded to the specific case, appointment of 'examiners', foreign representatives or direct judicial communication[13]. However, such mechanisms propose limited solutions especially when provided as stand alone tools, without general orderly guidelines[14] . In addition, they cannot provide all the required mechanisms for treating corporate groups in their variety of circumstances and scenarios[15].

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[5] See *infra* chapter 2 section 2.4.1.
[6] See *infra* chapter 2.
[7] *Id.*, section 2.4.3.
[8] *Id.*, section 2.4.4.
[9] *Id.*, section 2.4.5.
[10] *Id.*, sections 2.4.3, 2.4.4 and 2.4.5.
[11] *Id.*
[12] *Id.*
[13] See *infra* chapter 2 section 2.4.2.
[14] *Id.*
[15] *Id.*

Consequently, contemporary or future courts applying some of the main existing international cross border insolvency models to cases of corporate groups (specifically the EU Regulation and the Model Law) will lack a clear guidance for international cooperation in such cases. In the absence of any specific communication initiative (e.g., designing adequate Protocols for the specific case) the "member state" court or "Model Law" one, might base its decision regarding the relevant company at hand as entirely separate entity although it is in fact a part of a group. For instance, in the basic matters of jurisdiction and recognition, the court will most likely apply the rules of "centre of main interests" (COMI) and "establishment" (adopted within the EU Regulation[16] and the Model Law[17]) upon the specific company[18]. Thus, the court may not give any effect to possible implications of the fact that it might be in reality a case of a financial collapse of a single multinational business consisting of several companies or that the company at issue might be closely connected to other entities relevant to the matter. In addition, this court might decline requests of representatives or office holders of other companies from the same collapsing enterprise, who do not represent the single debtor the court is dealing with. However, these different companies might be closely connected and therefore it is a matter for consideration whether there is a need to handle those companies together or with active cooperation between the different proceedings.

The lack of a comprehensive orderly model in major international approaches for treating MCGs may result from various reasons. Primarily, this issue may affect the well-seated notions of a separate entity and the company's limited liability[19]. These concepts are known to be extremely important in terms of business developing, risk-taking and encouraging investments[20]. Evidently, the specific case of MCG presents difficulties in adhering to these basic concepts[21]. Thus, any suggested attempt to address the multinational enterprise, comprised of several entities, as a single body or as being connected in some way, can directly intervene with these concepts. In this

[16] See *infra* chapter 2 sections 2.4.3.
[17] See *infra* chapter 2 sections 2.4.4.
[18] See *infra* chapter 2 sections 2.4.3 and 2.4.4.
[19] See *infra* chapter 3 section 3.2.
[20] *Id.*
[21] *Id.*

respect, domestic laws themselves still lack a clear approach within the insolvency field[22].

In addition, there is an inherent difficulty in devising a model that enables international cooperation whilst refraining from creditors' prejudice and at the same time remains clear and predictable and is apt to deal with possible manipulations. This difficulty is mainly attributed to the complexity of the multiple debtor scenarios in which case there may be a spread of assets and debts among entities and large diversification of interests. Furthermore, the proper jurisdiction to handle the group insolvency case is presumably difficult to ascertain since different entities may have been incorporated or operated in different countries.

Indeed, it has been argued, that international models for cross-border insolvencies would be impractical in cases of MCGs, and that the MCG case demonstrates the uncertainty and unpredictability of a universalist approach as it involves different companies that may have different centres of gravity[23]. The conclusion, according to this approach, is that international insolvency cases, particularly those involving corporate groups will be better solved according to a territorial approach. It was further claimed that a territorial solution is in accordance with the contemporary MCG's tendency to keep their operations in various countries separate. The idea of this approach is thus to treat each of the MCG's companies separately, conducting their insolvency proceedings where their assets are located and enabling cooperation only according to the different countries' voluntary interests and willingness[24].

However, MCGs would not always keep the separateness between the entities comprising them. Even if they have maintained the separate entities, linking between the affiliates in their insolvency could sometimes be crucial. The multinational enterprise, which operates with a number of subsidiaries, may altogether form a coherent business, and/or it may manage its activities with significant close linkage between the different affiliates situated in a number of states. In certain cases the activities of the companies are deeply integrated leading to a de facto intermingling of assets and obligations[25]. This also contributes to a "domino" effect culminating in the

[22] *Id.*
[23] See notes 53-54 *infra* chapter 2, and accompanying text.
[24] See *infra* chapter 2 sections 2.2 and 2.3.
[25] See *infra* chapter 1 section 1.5.2 and *infra* chapter 4.

collapse of the whole group[26]. Additionally, there are scenarios where control over companies is exercised in an abusive manner. In all these different types of cases conducting separate insolvency proceedings for each subsidiary, with no sufficient linkage and no adequate means of international cooperation, may be a significant disadvantage. It may result with a considerable loss to the parties involved, a decrease of the feasibility of reorganization of the debtors and difficulties in ascertaining liabilities and controlling debtors' manipulations[27].

In summary it is evident that there is a range of possible situations for an MCG's business structure and mode of operation. The specific insolvency scenario may also vary from case to case and may be one of a whole enterprise failure conducted simultaneously or rather a specific division of the enterprise facing financial difficulties, or alternatively only the parent or only one of its subsidiaries may be facing insolvency[28]. Accordingly, any solution has to take into account this variety of situations. Referring solely to the case of completely separate operating affiliates is thus at best inconclusive. Furthermore, a comprehensive approach to the MCG insolvency situation needs to address both the problems of administering such proceedings, and other substantive issues related to the MCG insolvency cases, such as group liability.

As much as it is enormously complicated to untangle the case of a collapse of MCG, an international approach to these cases seems to be essential. It is the aim of this work to devise a global yet feasible model for the problem that could be relevant to a large number of states. Such a mechanism will be hereafter referred to as 'a global approach' or 'a global model', and it will mean an international approach to insolvencies within MCGs that both takes on a worldwide perspective and may disregard the corporate form in relevant circumstances. Since it will be apparent that it is difficult to create a specific strict model to be applied to all variety of MCG cases a more workable solution will focus on designing a variable and flexible mechanism yet systematically applicable in specific cases, reducing unpredictability. This mechanism will take into account the specific circumstances and relevant factors pertaining to the companies at issue.

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[26] See *infra* chapter 4 section 4.2.3.1.
[27] See *infra* chapters 4-6.
[28] See *infra* chapter 1 section 1.5.1.

The theme of the work

The first chapter will introduce us to the phenomenon of MCG and to the event of a failure within an MCG, aiming at providing the needed foundation for the formulation of a suitable approach for insolvencies within MCGs. The chapter will provide a general background on the phenomenon of corporate groups, including the question of which legal structures should be regarded as an MCG. Consequently, we will identify typical scenarios of insolvencies within MCGs that will serve as a reference point for the proposed global approach. These Prototypes will be designed using key factors that will be deemed most relevant for constructing a workable solution to these cases.

The second chapter will delineate the main approaches to international insolvencies both on the theoretical and practical levels. It will outline the main features of the 'universalist' theory confronting it with the 'territorialistic' view and will then review the major models for cross-border insolvency. This will enable to appreciate the main goals of existing regimes and initiatives as well as the tools currently available for coordinating international insolvencies. It will also be evident that existing models lack sufficient and effective means to deal with the phenomenon of insolvency within an MCG.

The third chapter will present the basic conflict between the need for a global approach to MCGs and its benefits on one hand and the importance of preserving the corporate separate personality on the other hand (the latter being emphasized in a cross border case, in which the separate entity operates within the borders of a different state than that of its affiliate). It will then set forth the key factors pertaining to the administration of MCG's insolvency, in light of which it will be subsequently considered whether unified proceedings for related companies would be advantageous and whether there would be circumstances in which the corporate form should be ignored in the context of the insolvency proceedings.

The main corpus of this study will discuss in detail the underlying aims and rationales for applying a global approach (therefore, presumably disrupting the entity doctrine and intervening with countries' sovereignty). It will explore the influence and effect such an approach has on promoting or otherwise withholding insolvency goals, and the possibility to overcome any major flaws it entails. It will include examples and reference to actual cases in order to accurately illustrate the strengths and potential

weaknesses a global approach possesses. In addition, mechanisms for treating corporate groups in insolvency, currently available in certain legal regimes will be discussed to appreciate their compatibility and availability for the international scenario. We will put focus on three insolvency regimes- the United States', United Kingdom's and New Zealand's laws– which represent different approaches to the relevant matters. On the one hand, the UK regime adheres relatively strictly to the notions of corporate personality and limited liability. On the other hand, the US bankruptcy regime and the New Zealand's law present a more liberal approach with regard to these concepts in the context of insolvency of corporate groups and propose modern mechanisms to deal with the particular challenges these cases present.

Chapter 4 will thus discuss the goal of promoting an economic efficient insolvency system and reorganizations, which basically means making the most of the companies' value while decreasing the costs occurring during the insolvency process. Chapter 5 will focus on the goal of enhancing fairness and the integrity of the insolvency system. Chapter 6 will deal with three additional goals: the aim of preventing manipulation of the forum ('forum shopping'), a goal particularly relevant in international cases; the need to provide clear and predicable rules; and the need to deal with inconsistencies between an international approach and domestic regimes, respecting state sovereignty while promoting suitable solutions for the MCG in insolvency that have the potential to be accepted by a large number of countries.

Chapter 7 will deal particularly with the issue which is fundamental to an attempt to promote a global solution to insolvencies within MCGs, and that is the ability to identify the 'home country' of the MCG for the purpose of handling the insolvency process. The designated forum to handle groups' insolvency or to supervise the proceedings will be proposed alongside the criteria for identifying this potential locus. Those scenarios where a single venue for the MCG insolvency can not be located will also be discussed.

As we will go along deliberating these issues, the essential characteristics of an optimal approach will emerge. Thus, we will be able to propose for each of the relevant goals, the characteristics and traits an adequate approach should display. Essentially, these characteristics will suggest the 'right' ways of 'piercing the veil' in

the MCG insolvency cases and linking between related entities in the course of their insolvency.

Finally, this study will conclude by suggesting that a comprehensive international model for insolvencies within MCGs is both essential and feasible. Such model should rely on the accumulative experience and should reflect as accurate an image as possible of the MCG at hand while appreciating the negative outcomes its application may bring about. This way, it will be possible to reconcile between the need to respect the corporate separate personality and the need to unify between affiliates in their insolvencies. Finally, a set of propositions extracted from the discussion of the various insolvency goals are offered as guidance for future reforms of cross-border insolvency models.

Chapter 1

The phenomenon of the MCG in the context of financial distress

1.1 Introduction

The phenomenon of the corporate group in general and the multinational corporate group in particular was already a subject for a significant number of publications. Our goal in this chapter is by no means to provide a comprehensive review of the corporate group concept and implication but rather to set the scene of the event of collapse within an MCG. At the outset it is important to appreciate the economic significance and considerable power of MCGs in the modern world. Indeed, the amount of public attention allocated to recent large scale insolvency cases in itself can give evidence for that. Moreover, the diversified scene of MCGs in distress need to be analysed to reveal the infrastructure of the MCG's operation and collapse hence paving the way for our later discussion regarding the validity of a global approach to insolvency within MCG's.

Accordingly, the chapter will begin by briefly reviewing the historical background of the multinational enterprise and the use of the corporate group device in this regard. It will describe the various reasons for the emergence of the MCG and its growth into what now became a significant phenomenon in world business. It will point out the way MCGs are expanding their businesses across borders using affiliates to achieve their economic goals, and the international legal framework within which they operate.

The chapter will then proceed to establish the proper definition of an MCG for the purpose of a global approach, delineating the various legal patterns such enterprises may use when they embark on a multinational venture. The spectrum will then be narrowed to focus on the specific factors pertaining to insolvencies within MCGs. Most notably, the organizational patterns coupled with the insolvency scenarios that will be most relevant and have crucial effect on the compatibility and efficacy with which global tools may be applied. While appreciating the diversity in the insolvency situations within a variety of MCG legal forms, the chapter will conclude with an

attempt to classify certain Prototypes of MCG along the relevant factors that will be suggested. These in turn, will facilitate our discussion in later stages of this work as well as provide a crucial groundwork for the formulation of a proper global approach.

1.2 Roots and reasons for the rise of MCGs

Multinational enterprises operating through group structures are essentially enterprises comprising of more than one company that operate in a transnational perspective[1]. Hence, when describing the roots and reasons for the growth of MCGs we ought to consider the developments at the two core axes of the phenomenon- the rise of the multinational enterprise and the emergence of the corporate group organizational pattern. As will be shown here, at some point these two axes coincided in that the multinational enterprise adopted the corporate group structure as a major form for its operation, thus placing the MCG as a major force in world business.

In the evolutionary process corporate groups represent an advanced stage of development building upon the now established concept of 'limited liability'[2]. Thus, they exploit the idea of a company's distinct personality which is detached from the identity of its shareholding members and the benefit of limiting the holding company's liability for the subsidiaries' debts to the amount it has paid or have agreed to pay to the company for its shares[3]. It appears that corporate groups first surfaced in the US. It was not until 1889-1893 when states within the US began enacting statutes granting powers to corporations to acquire and hold shares of other corporations[4]. Before that, such an action as purchasing stock of another corporation was seen as an improper expansion of the restricted corporate purpose. There was also a general anti corporate feeling in the US during the nineteenth century, stemming from the antagonism to monopolies, particularly where the purchase represented not merely an investment, but an attempt to gain control of the other corporation and perhaps to

[1] The specific definition of an MCG that should be adopted for the purpose of a global approach and the various possible structures of MCGs will be discussed in section 1.3 below.
[2] In the UK limited liability became generally available in 1855 (the Limited Liability Act 1855). The principles of the corporate entity and the limited liability were then firmly settled at the end of the 19th century in the Salomon case ([1897] AC 22) (see L.C.B. Gower, P.L. Davies, *Gower and Davies' principles of modern company law* (6th ed, 1997), p. 40-46).
[3] See *infra* chapter 3 section 3.2.
[4] See Blumberg, Phillip I. Blumberg, *The Multinational Challenge to Corporation Law: the search for a new corporate personality* (1993) [hereinafter: Blumberg, The Multinational Challenge], chap. 3.

achieve monopoly power over the market as well[5]. With the new rules that gradually dropped all restrictions on acquiring the shares of other companies, corporate groups soon grew to occupy a commanding role in American industry[6]. It is more difficult to track the entry of corporate groups onto the English scene, since there was not an equivalent rule in English law regarding ownership by companies[7]. However, the period of the 1920s and the 1930s has been indicated as the point of entry for groups into the conscious jurisprudence of UK company law[8].

It can be argued that the multinational enterprise should be tracked back to several hundred years earlier, however not in its modern form, when a genuine international division of production by firms was presented[9]. This phenomenon of control over the production of goods and services in foreign countries originated with the establishment in the sixteenth century of the great European colonial trading companies[10]. Initially, this worldwide business was achieved via trade relations. In time, big companies exerted a growing degree of control through foreign independent agencies. Finally, multinational enterprises in their modern sense began to appear in the nineteenth century with the growth of world trade and industrial production and the simultaneously growing importance of technological know-how[11]. The pressure to find affiliates increased, due to the need to open up new attractive markets and to secure access to raw materials. Independent agents still played a major role in this regard, but as they were often unreliable they were replaced more and more by directly controlled affiliates[12].

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[5] *Id.*
[6] *Id.*
[7] See D. Milman, "Groups of Companies: The Path towards Discrete Regulation" in *Regulating Enterprise* 218, 220 (D. Milman, ed., 1999).
[8] T. Hadden, "Inside Corporate Groups" [1984] 12 Int. J. of Soc. Of Law 271.
[9] See P.T. Muchlinski, *Multinational Enterprises and the Law* (1999) [hereinafter: Muchlinski, Multinational Enterprises], p. 19-20. Multinational enterprises (or transnational corporations) can be defined as decision- making centres owning income-generating assets in at least two countries. Such enterprises represent organizations designed for capital accumulation on a world scale (J.H. Dunning, *International Production and the Multinational Enterprise* (London, 1981), chap. 1. See also V. Bornschier and H. Stamm, "Transnational Corporations" in S. Wheeler (ed.), *The Law of the Business Enterprise*, (1994) p. 333).
[10] See I. Wallerstein, *The Modern World-system*, (New York, 1974, 1980) vol i and ii. See also V. Bornschier and H. Stamm, "Transnational Corporations" in S. Wheeler (ed.), *The Law of the Business Enterprise*, (1994) p. 340.
[11] M. Wilkins, *The Emergence of Multinational Enterprises: American Business Abroad from the Colonial Era to 1914* (Harvard, 1970), part two.
[12] See *Id.* See also V. Bornschier and H. Stamm, "Transnational Corporations" in S. Wheeler (ed.), *The Law of the Business Enterprise*, (1994) p. 340.

In fact, various theoretical explanations and historic views regarding the establishment and continued growth of the multinational enterprise were suggested over time. Initially it was suggested that ownership advantages were the driving force behind multinational enterprises. According to this view enterprises expanded beyond their national seat of operations primarily to be able to expand market power[13]. Later on another explanation linked the expansion of firms abroad to the development sequence of their products, offering that enterprises use foreign markets to seek new opportunities for profit and to remain competitive[14]. Yet another view explained the motivation for expansion into foreign markets as derived from minimizing transaction costs. According to this theory, internalization of activities (that is, the vertical and horizontal integration of operations) increases efficiency[15]. Yet another approach concentrated on location advantages. Namely, that the choice of the enterprise to expand to foreign markets depends on the advantages that host countries may or may not offer, such as the market size or local protective measures. This approach is closely related to the classical theory of trade[16]. Conclusively, the development of the multinational enterprise is explained as an integration of those different approaches into an 'eclectic paradigm', which combines ownership, location and internalization factors[17].

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[13] The 'monopolistic' approach illustrated in the work of Hymer (see, for example, S. Hymer, *The International Operations of National Firms: Study of Foreign Direct Investment* (1976); Hymer and Rawthorn, "Multinational Corporations and International Oligopoly: The Non-American Challenge" in Kindleberger (ed.), *The International Corporation* (1970), p. 57). See also S. Wheeler, "The Business Enterprise: A Socio-Legal Introduction" in S. Wheeler (ed.), *The Law of the Business Enterprise* (1994) p. 36-37; V. Bornschier and H. Stamm, "Transnational Corporations" in S. Wheeler (ed.), *The Law of the Business Enterprise* (1994), p. 334-335.

[14] Known as the 'product cycle' model developed by Professor Vernon (see R. Vernon, *Sovereignty at Bay: The Multinational Spread of U.S. Enterprises* (1971); R. Vernon, *The Economic and Political Consequences of Multinational Enterprise* (second ed., 1973)). The model lost its relevance since the mid-70, especially it did not thought to work as an explanation for the behaviour of established multinational enterprises or the expansion of non-US enterprises abroad (see in the writings of Professor Vernon himself (R. Vernon, "The product cycle hypothesis in a new international environment" [1979] 41 Oxford Bull. Econ. Stat. 255)).

[15] See, for example, P.I. Buckley and M. Casson, *The Future of Multinational Enterprise* (1976), revised 2nd edn, 1991, p. 2.

[16] See, for example, J.H. Dunning, *Explaining International Production* (1988), p. 22-23.

[17] See J.H. Dunning, *Industrial Production and the Multinational Enterprise* (1981); J. Black and J.H.Dunning (eds.), *International Capital Movements* (1982). Dunning's contribution is viewed as a combination of previous theories (see S. Wheeler, "The Business Enterprise: A Socio-Legal Introduction" in S. Wheeler (ed.), *The Law of the Business Enterprise* (1994), p. 38-39; V. Bornschier and H. Stamm, "Transnational Corporations" in S. Wheeler (ed.), *The Law of the Business Enterprise* (1994), p. 338).

Economic historians pointed out the vertical integration and the formation of multidivisional structure among the leading business firms as the roots for the growth of firms[18]. It was suggested that over time, with the growing number of affiliates the establishment of an administrative supervising organization became necessary. This was then developed into more complex structures of multinational enterprises- the polycentric systems- where the affiliates themselves had certain autonomy which allowed them to begin expansion, leading to the emergence of the conglomerate entangled structure[19].

Indeed, the corporate group form helps to achieve some of the goals pertaining to the expansion of firms across borders (as were briefly summarized above), such as ownership advantages, minimization of transaction costs and location advantages. Thus, the limited liability company and its expansion to the notion of the holding company (as mentioned above) were significant instruments to the growth of the multinational business[20]. This structure emerges either through the process of corporate acquisition, or via strategic planning of the enterprise's structure[21]. Particularly, this structure enables to take advantage of fragmenting the business enterprise into a collection of distinct entities[22], to ring-fence risks and isolate potential liabilities. It should also be noted that, though the integrated multinational enterprise structure helps businesses to achieve market power, companies may also be motivated to invest in foreign subsidiaries merely for the purpose of diversifying investment[23]. Consequently, as of today, the device of the corporate group is a key player in the international business scene depicting the efficient modern business actor[24]. The impact of the MCG in world business is even greater considering

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[18] See, for example, O. E. Williamson, "The Modern Corporation: Origins, Evolution, and Attributes" [1981] 19 J. Econ. Lit. 1537; M. Wilkins, *The Maturing of Multinational Enterprise: American Business Abroad from 1914 to 1970* (1974).

[19] See *Id.*; See also V. Bornschier and H. Stamm, "Transnational Corporations" in S. Wheeler (ed.), *The Law of the Business Enterprise* (1994), p. 339-340.

[20] See Muchlinski, Multinational Enterprises (note 9 above), p. 40-41.

[21] See O. E. Williamson, "Organization Form, Residual Claimants and Corporate Control" [1983] 26 J. Econ. 351, 362; O. E. Williamson, "The Modern Corporation: Origins, Evolution, and Attributes" [1981] 19 J. Econ. Lit. 1537. See also William W. Bratton Jr, "The New Economic Theory of the Firm: Critical Perspectives from History" in S. Wheeler (ed.), *The Law of the Business Enterprise* (1994), p. 153.

[22] Such as tax advantages (see D. Milman, "Groups of Companies: The Path towards Discrete Regulation" in D. Milman (ed.), *Regulating Enterprise* (1999), p. 221.

[23] See Kopits, "Multinational conglomerate diversification" [1979] 32 Econ. Int. 99.

[24] See K. Hofstetter, "Multinational Enterprise Parent Liability: Efficient Legal Regimes in a World Market Environment" [1990] 15 N.C.J. Int'l L. & Com. Reg. 299, 301-302; D. Milman, "Groups of

operations taking place using various legal forms, other than the conventional hierarchical structures and the full ownerships of affiliates. In fact, it was observed that there is a tendency towards majority or minority participations in foreign companies, joint ventures and licence agreements[25].

Other legal factors (apart from the corporate group legal device) influence multinational enterprises' expansion to foreign markets[26]. For instance, the variety of national regulations and investment incentives offered by domestic legal regimes[27] may attract multinational enterprises. Nation states may be driven to induce investment, in order to enhance domestic welfare, and therefore will tend to deregulate multinationals' economic activities[28].

All in all, the international arena offers the multinational enterprise a variety of legal frameworks within which to operate. Together with the use of the corporate group device (in its broad sense[29]) it enables the enterprise to ring-fence risk and to isolate activities 'twice'- within the subsidiaries' 'veil' (corporate or contractual[30]) and within national borders.

Nonetheless, it has been observed, that a rather chaotic platform supports the operation of corporate groups (domestic and multinationals)[31]. At present, most domestic or international legal regimes do not provide a fully developed law specifically tailored to corporate groups (distinguished from single companies)[32],

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Companies: The Path towards Discrete Regulation" in D. Milman (ed.), *Regulating Enterprise* (1999), p. 235-236.

[25] United Nations (1978), Transnational Corporations in Development: a Re- examination. New York: UNCTNC, p. 229; United Nations (1983), Transnational Corporations in World Development, 3rd Survey. New York: UNCTNC, p. 40-46; OECD (1981), "International Investment and Multinational Enterprises: Recent International Direct Investment Trends", p. 31-35. See also V. Bornschier and H. Stamm, "Transnational Corporations" in S. Wheeler (ed.), *The Law of the Business Enterprise* (1994), p. 334. See further on the various forms of corporate groups in section 1.3 below.

[26] See in Muchlinski, Multinational Enterprises (note 9 above), p. 38-47 an analysis of the contribution of legal factors to the growth of multinational enterprises.

[27] *Id.*, p. 42-45 (these factors are identified by Muchlinski as 'location factors').

[28] *Id.*, p. 45. The implications of states' approaches to foreign investment on the feasibility of applying a global model to insolvencies within MCGs will be discussed in *infra* chapter 6 section 6.3.

[29] See text preceding note 25 above.

[30] As will be later on elaborated (see *infra* chapter 5 section 5.2.4).

[31] See C. Schmitthoff, "Introduction" in Schmitthoff C.M. and Wooldridge F. (Eds.), *Groups of Companies* (1991), p. xiv-xv.

[32] Certain legal regimes have adopted a statutory solution and developed 'a law of corporate groups', most notably is the German Stock Corporation Act 1965 (*Aktiengesetz*) (reproduced in English in K.J. Hopt (ed.), *Groups of Companies in European Laws, Legal and Economic Analyses on Multinational Enterprises*, Vol. II (1982), p. 265-295), though this have been criticized as capable of improvement

although the growth of the multinational enterprises increased the call for regulating their activities[33]. Coupled with the diversity in the way legal systems' deal with corporate groups, this situation creates uncertainty with regard to the legal consequences in various aspects of MCGs' operations[34].

In the context of insolvency, the MCG phenomenon received great focus as a result of the collapse of large sized MCGs in the last decade. Insolvency cases such as Maxwell[35], *BCCI*[36] and *Polly Peck*[37] and more recently those of *Enron*[38], *Worldcom*[39]

(see K.J. Hopt, "Legal Elements and Policy Decisions in Regulating Groups of Companies" in C.M. Schmitthoff and F. Wooldridge (eds.), *Groups of Companies* (1991), p. 81; see also H. Weidemann, "The German Experience with the Law of Affiliated Enterprise" in K.J. Hopt (ed.), *Groups of Companies in European Laws, Legal and Economic Analyses on Multinational Enterprises*, Vol. II (1982), p. 21). The English Company Law Review (CLR, Completing the Structure, URN 00/1335, November 2000 [hereinafter: CLR, Completing], chap. 10) proposed something which was in part similar to the German model with regard to the issue of group liability, however the proposal was not proceeded with (Company Law Review (CLR), Final Report, Volume I, URN 01/943, July 2001[hereinafter: CLR, Final Report I], paras 8.23-8.28). See further on current legal approaches to the corporate group phenomenon specifically in the context of insolvency in *infra* chapter 2 section 2.4.5.3, *infra* chapter 3 section 3.2, *infra* chapter 4 sections 4.1.3.3 and 4.3.4 and *infra* chapter 5 sections 5.2.2.5, 5.2.3.2 and 5.2.4.4.

[33] The EC draft 9th Directive on groups of companies (Council Directive on the harmonisation of company law (9th Directive)), which is based on the German model (see in note 32 above.), provides for a legal structure for unified management of a public limited company and any other undertaking which has a controlling interest in it (see J.H. Farrar, et al., Company Law (4rd ed. 1998) [hereinafter: Farrar, Company Law], p. 536). However, the current position of the European Commission is that there is no need to revive the directive since the enactment of an autonomous body of law specifically dealing with groups does not appear necessary, but that particular problems should be addressed through specific provisions (see Final Report of the High Level Group of Company Law Experts on a Modern Regulatory Framework of Company Law in Europe, Brussels, November 4, 2003; Commission of the European Communities "Communication from the Commission to the Council and the European Parliament - Modernising Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward", May 21, 2003 (COM/2003/0284 final); see also P.L. Davies, *Gower and Davies' principles of modern company law* (7th ed, 2003) [hereinafter: Davies, Gower Company Law], p. 112-114; Muchlinski, Multinational Enterprises (note 9 above), p. 328-331; Farrar, Company Law, p. 12; G. Teubner "Unitas multiplex: corporate Governance in group enterprises" in *Regulating Corporate Groups in Europe* 67 (D. Sugarman and G. Teubner eds, Nomos, 1990), p. 92-93). Other initiatives derived from the OECD and from international banks. The OECD guidelines provide principles and standards of good practice consistent with applicable laws. These are recommendations jointly addressed by governments to multinational enterprises. Observance of the guidelines by enterprises is voluntary and not legally enforceable (OECD Guidelines for Multinational Enterprises 27 June 2000 (http://www.oecd.org/dataoecd/56/36/1922428.pdf) [hereinafter: OECD Guidelines], "preface", p. 15, para 1). The World Bank Guidelines on the Treatment of Foreign Direct Investment are aimed to set down emerging rather than settled standards, and, in the process, to emphasize what the World Bank Group sees as desirable practice in the field of direct foreign investments (Legal Framework for the Treatment of Foreign Investment (Volume II, Guidelines) (World Bank, 1992), reproduced 31 ILM 1363 (1992)). On these and on other initiatives see Muchlinski, Multinational enterprises (note 9 above), chap. 16.

[34] See C. Schmitthoff, "Introduction" in Schmitthoff C.M. and Wooldridge F. (Eds.), *Groups of Companies* (1991), p. xiv-xv; J. Keir, "Legal Problems in the Management of a Group of Companies" in Schmitthoff C.M. and Wooldridge F. (Eds.), *Groups of Companies* (1991), p. 53.

[35] *Re* Maxwell Communications Corp., [1993] 1 W.L.R. 1402 (Ch. 1993); 170 B.R. 800 (Bankr. S.D.N.Y. 1994).

and *Parmalat*[40] placed the 'group issue' in the centre of public attention. These events, having impact on creditors on a very large scale, emphasized the predominant role of the MCG in international economic affairs, and the difficulties in answering the legal issues that arise in the course of its operation and its default[41].

1.3 What will constitute an MCG as a subject of a global approach?

We have seen that the MCG is a major feature of worldwide economy. The enterprise may divide its business among nations, using complex structures and differences in national laws. In the context of insolvency this will raise questions of how to best deal with the event of a default within the MCG. An effective and fair handling of the issues pertaining to the MCG insolvency may demand global means and a sort of unified approach to the MCG as a whole, as will be demonstrated later on in this work. However, a basic issue to establish before considering any global approach is how we define an MCG for the purpose of such a model. It has been already indicated that foreign investment and operations via affiliates may take various legal forms[42]. It is hence worth considering in greater length the various options of corporate group forms, and substantiate whether these structures will be included under the term MCG and consequently be put under the scope of a proposed global model.

The basic straight-forward structure of a group of companies is where a parent owns a subsidiary, or where a common controlling shareholder owns two or more affiliated corporations[43]. However, the corporate group may appear in more complex multi-tier structure[44]. In all these structures, ownership is the vital link, which constitutes the 'group'. However, as was indicated above, there are other possible structures for

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[36] See note 155 *infra* chapter 4.
[37] Re A Company No. 009296 of 1990, 1992 BCC 510 (Ch. 1992).
[38] *In re* Enron, Chapter 11 No. 01-16034 (AJG) (Bankr. S.D.N.Y.).
[39] *In re* Worldcom, Chapter 11 No. 02-13533 (AJG) (Bankr. S.D.N.Y.).
[40] Note 51 *infra* chapter 4.
[41] See D. Milman, "Groups of Companies: The Path towards Discrete Regulation" in D. Milman (ed.), Regulating *Enterprise* (1999), p. 221.
[42] See text preceding note 25 above.
[43] See Phillip I. Blumberg, *The Law of Corporate Groups: Bankruptcy Law* (1985, Supp 1992) [hereinafter: Blumberg, Bankruptcy], p. 14.
[44] Corporate groups may evolve into intricate networks of sub-holding companies (see A. Muscat, The liability of the holding company for the debts of its insolvent subsidiaries [hereinafter: Muscat, The Liability], p. 8; Tom Hadden, "Inside Corporate Groups" [1984] 12 Int. J. of Soc. Of Law 271, 273; Farrar, Company Law (note 33 above), p. 46).

separate entities operating internationally in a coordinated way. In fact, economic globalization introduces us with great diversification of corporate holdings both in terms of commodity portfolios and geographical spheres of operation. Multinational corporations today are able to co-ordinate their businesses by virtue of sophisticated communications networks and strategic alliances. This is facilitated by the development of systems of 'electronic funds transfer' and 'e-commerce'[45].

Indeed economists have suggested that transnational businesses may be linked by contract rather than equity and may be organized with a high degree of decentralization. The vital link can thus be control (as well as common ownership) or coordination even when it is exerted over autonomous action centres[46]. The OECD Guidelines[47] provide a broad definition to multinational enterprises (while observing that they usually consist of separate entities established in a number of countries). It puts focus on coordination rather than control as the possible manifestation of linkage between separate entities, and suggests that the amount of influence and control over

[45] A. Bell, *Forum Shopping and Venue in Transnational Litigation* (2003 [hereinafter: Bell, Forum Shopping], p. 3; Farrar, Company Law (note 33 above), p. 12-13.

[46] See J.H.Dunning, *Multinational Enterprises and the Global Economy* (Wokingham, Addison-Wesley Publishing Co, 1993) [hereinafter: Dunning, Multinational Enterprises], p. 3; N. Hood and S. Young, *The Economics of Multinational Enterprise* (London, Longman, 1979), p. 3; R. Caves, *Multinational Enterprises and Economic Analysis* (Cambridge University Press, 2nd ed, 1996), p. 1; G. Teubner, "The many-headed Hydra: networks as higher order collective actors" in J. McCahery, S. Picciotto and C. Scott (Eds.), *Corporate Control and Accountability* (Clarendon Press, 1993) p. 41; G. Teubner "Unitas multiplex: corporate Governance in group enterprises" in D. Sugarman and G. Teubner (Eds.), *Regulating Corporate Groups in Europe* (Nomos, 1990), p. 87-92; G. Teubner *Law as an Autopoietic System* (Oxford, Blackwell Publishers, 1993), chap. 7; Muchlinski, Multinational Enterprises (note 9 above), chap. 3 and chap. 9, p. 327, 330. See also P.T.Muchlinski, "Corporations in International Litigation: Problems of Jurisdiction and the United Kingdom Asbestos Cases" [2001] 50 ICLQ I; Blumberg, The Multinational Challenge (note 4 above), chap. 10 (for a general discussion on the various forms of organizations). The English Insolvency Act 1986 (s. 249, 435) provides definitions for 'connected persons' and 'associate' for the purpose of the Act. The definitions apparently comprise members of corporate groups (see Muscat, The Liability (note 44 above), p. 221 and 224). However, the Act does not define what a corporate group is. Similarly, The English Companies Act offers no formal definition of a group, though it seeks to define the key players within a group. For certain purposes the definition refers to group of undertakings embracing the broader concepts of control and referring to control contracts. This was a result of implementing the Seventh Company Law Directive (83/349) by the Companies Act 1989 and it echoes German Law, yet it remains incomprehensive in nature (English Companies Act 1985, s. 736. For an analysis of the definitions for group members within English company law see Davies, Gower Company Law (note 33 above), p. 205- 209; Farrar, Company Law (note 33 above), p. 533-536. See also D. Milman, "Groups of Companies: The Path towards Discrete Regulation" in D. Milman (ed.), *Regulating Enterprise* (1999), p. 220).

[47] Note 33 above,

affiliates may differ between enterprises with different degrees of autonomy enjoyed by affiliates[48].

Professor Muchlinski in his work[49] provides a comprehensive analysis of the various forms employed by multinational enterprises that can be used here to observe on the range of possible structures of MCGs. Essentially, multinational enterprises' structures could be classified into a number of principal types[50]. 'Equity-based' forms of multinational enterprises may occur in the classic 'pyramid' form of ownership that crosses borders[51], or alternatively as transnational mergers in which two or more parent firms integrate their business operations and jointly hold a limited liability company[52]. Additional example could take the form of cross- shareholding groups coupled with coordinated management[53]. 'Contractual-based' forms of MCGs emphasize contractual linkages between foreign companies or international 'network organizations'[54]. Such structures can be achieved via the establishment of distribution franchise alliances, by licensing production rights as part of a production franchise package[55], or by establishing an international consortium[56]. Another typical form of MCGs is the 'international joint venture' between companies from more than one country. In these cases, two or more parent undertakings (or controlling entities) cooperate to pursue a commonly commercial activity. The parents are linked via the

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[48] See OECD Guidelines (note 33 above), "Concepts and Principles" p. 3. The guidelines do not provide a precise definition of multinational enterprises, yet it states that such enterprises: "...usually comprise companies or other entities established in more than one country and so linked that they may co-ordinate their operations in various ways. While one or more of these entities may be able to exercise a significant influence over the activities of others, their degree of autonomy within the enterprise may vary from one multinational enterprise to another. Ownership may be private, state or mixed". See also P.T.Muchlinski, "Corporations in International Litigation: Problems of Jurisdiction and the United Kingdom Asbestos Cases" [2001] 50 ICLQ I 1, 8.

[49] See Muchlinski, Multinational Enterprises (note 9 above), p. 61- 80.

[50] See *Id.* See also Blumberg, The Multinational Challenge (note 4 above), p. 244-253; Janet Dine, *The Governance of Corporate Groups* (2000), p. 39- 42.

[51] Typical of US and UK held multinational enterprises (Muchlinski, Multinational Enterprises (note 9 above), p. 65-66).

[52] This is especially common in Europe (*Id.*, p. 66-69). A transnational merger can emerge by the creation of a twin holding company locating in each home state, based on joint shareholding by the founding parent companies, and the transfer of operating activities to subsidiaries that may be jointly or separately owned and controlled by the holding companies (*Id.*). See for instance the case of the Unilever group in J. Keir, "Legal Problems in the Management of a Group of Companies" in Schmitthoff C.M. and Wooldridge F. (Eds.), *Groups of Companies* (1991).

[53] Developed in Japan (Muchlinski, Multinational Enterprises (note 9 above), p. 69-70).

[54] As such associations were described by Teubner (see references in note 46 above).

[55] Muchlinski, Multinational Enterprises (note 9 above), p. 62-64.

[56] Most often used for specific, large scale international construction or engineering projects (*Id.*, p. 64-65).

joint venture (which they either own or with which they have a contractual linkage) and typically share the control over it[57]. In addition, another type of MCG form is the 'informal alliances' that lack clear legal structure (for instance, when a bundle of companies cross-hold each other's shares, however, this is done in a way which does not make them subsidiaries or associates[58]). Finally, multinational enterprises may be partly or wholly state-owned, or they may be structured as supranational forms of international business. Such types of supranational entities can be part of a group in which the top company can be supranational as well or a national one[59]. To summarize, firms may subdivide their economic activities among separate entities operating in different countries in a variety of legal patterns (such as networks and other type of interrelations) rather than exclusively relying on the basic equity based 'pyramid' form.

Evidently, all these various structures involve a number of companies that are linked in some form or another. As a result, a degree of coordination or of mutual involvement may potentially occur in any of the above legal patterns. Thus, for instance, parent and subsidiaries (linked by equity) may altogether operate a single business, or parents may be significantly involved in the management of the subsidiaries. Similarly, where international business is carried on by means of contract, there may emerge a relationship of control and dominance by one party which creates a degree of business integration[60].

Consequently, any of these legal forms may bring about an insolvency scenario of multiple debtors (if the enterprise or any part thereof collapses) where a worldwide perspective to the group's insolvency may be fair and efficient. For instance, issues of

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[57] Although, it may be that one of the parents exercises dominant influence over the venture (*Id.*, p. 72-73). See generally on the phenomenon of joint ventures in M. Lower, "Joint Ventures" in D. Milman (ed.), *Regulating Enterprise* (1999), p. 241.

[58] For example, each holds 30% of each other's shares (Muchlinski, Multinational Enterprises (note 9 above), p. 74).

[59] See the initiatives within the EC: the Statute for a European company (SE) (Council Regulation (EC) No 2157/2001, OJ L 294/1, 10.11.2001) and Council Regulation (EEC) 2137/85 of 25 July 1985 on the European Economic Interest Grouping (EEIG) // 1985 OJ L 199/1. See also Commission of the European Communities "Communication from the Commission to the Council and the European Parliament - Modernising Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward", May 21, 2003 (COM/2003/0284 final); Muchlinski, Multinational Enterprises (note 9 above), P. 75-80; Davies, Gower Company Law (note 33 above), p. 23-26.

[60] Muchlinski, Multinational Enterprises (note 9 above), p. 62 and p. 81. See also note 109 *infra* chapter 5 (on the issue of group liability in network enterprises).

responsibility of one member of a group to the insolvency event of another member may arise where certain entities might have been involved in the management of other entities[61]. Additionally, it seems that multiple debtors that operated with significant coordination in their ordinary course of business may benefit from a unified handling of their insolvencies[62].

Therefore, in order to follow changes in economic realities, and since (at least in potential for the time being) global means may be useful in any of the legal forms of multinational corporate enterprises; a global approach to insolvency should be designed to accommodate the various patterns of MCG. It would be of limited practical value to apply a model only to certain sorts of group structures. Such a 'limited' model will both permit MCGs to evade legal consequences (in the context of insolvency), and prohibit other MCGs from the benefits a global model may propose, if the MCG is structured in a way different than the 'basic' traditional one. Hence, a limited method that applies only to a restricted version of the MCG will lack generality and will be deemed useless.

The MCG should therefore be defined (for the purpose of this study) as: "any enterprise comprised of a number of separate entities situated or established in more than one country and which are in fact mutually connected either by common ownership or via other links so that they may co-ordinate their businesses"[63]. 'Ownership' should receive a broad definition including the various legal forms indicated above. It includes both parent-subsidiary relationship and affiliates linked via a common individual shareholder (or a number of shareholders)[64]. In addition, the group can consist of directly owned subsidiaries as well as multi-tiered groups. Furthermore, holdings structures can differ from a full ownership to partly owned subsidiaries. 'Other links' may be performed via contracts or cross-shareholdings as explained above. Finally, the MCG may occur in a range of sizes and dimensions. It can vary from a large business enterprise with operations that span the entire globe to

[61] See *infra* chapter 5 section 5.2.4.
[62] As will be demonstrated in *infra* chapter 4.
[63] Similar to the statement within the OECD Guidelines with regard to multinational enterprises (note 48 above).
[64] However the proposed model only deals with the companies in the group. The position of individual shareholders is outside the scope of this work (see also *infra* chapter 5 section 5.2.4.2).

small sized groups[65]. Namely, the definition of the MCG will include all groups' sizes and will not be limited only to the large organizations.

1.4 The diversified scene of insolvencies within MCGs– focusing on key factors relevant to the application of a global approach

Indeed, there are various possible legal forms by which MCGs can conduct their business. We argue here that it is crucial for an appropriate global approach to be applicable to this variety of legal structures. A priori, we should not exclude any of those possible structures from being treated by a global approach.

However, as the insolvency within any particular MCG may take many forms, a specific solution, perhaps appropriate to one possibility, may in fact be completely inadequate to deal with a different scenario. Hence, any attempt to construe a comprehensive global approach for such cases ought to take into account the variety of potential situations. Therefore, in order to set the infrastructure for any suitable model, it is crucial to describe the variety of relevant MCG insolvency scenes parsimoniously by defining prototypical organizational structures and the corresponding insolvency scenarios (hereinafter: Prototypes), hence, enabling some measure of generalization across cases and scenarios. Ultimately, the aim is to create a model that will correspond to the business structure and insolvency scenario of the enterprise concerned.

To this end it is advisable to identify and explore several key factors which hold a fundamental relevance to the application of appropriate global means and therefore could serve as the dimension around which our Prototypes could be defined. However, it should be emphasized that a global approach is concerned with providing a framework for linking between foreign affiliates in their insolvencies. Accordingly, the factors that will be chosen bear relevance to issues pertaining to the creation of

[65] See for instance Davies, Gower Company Law (note 33 above), p. 178, 202 noting that even relatively modest businesses often operate through groups of companies; Dr. Muscat (Muscat, The Liability (note 44 above), p. 3, 15, 448-449) showing that the use of the corporate group structure is not limited to the large business enterprises, although in the case of the smallest private business enterprise the typical form of organization is the single independent company (see also Muchlinski, Multinational Enterprises (note 9 above), p. 39; V. Bornschier and H. Stamm, "Transnational Corporations" in S. Wheeler (ed.), *The Law of the Business Enterprise*, (1994) p. 345; T. Hadden, *The Control of Corporate Groups* (1983) p. 1).

such linkage (on the global level). Therefore, other factors that may be good indicators of different aspects of the MCG's structure or the insolvency scenario will not be considered as key for our purposes. In other words, the idea is not to identify all variety of insolvency situations in all levels and respects, but rather to define a number of stereotypical situations that are substantially different in the 'eye of a global approach'[66]. As such, these prototypes will later on be referred to by the proposed model

Consider first the different types of insolvencies in terms of the companies involved in the process: it can be a case in which only one subsidiary of the MCG is under insolvency or a number of subsidiaries or a case of an entire MCG in distress. This will reflect on the appropriate global linking means to be applied. For instance, an insolvency of a subsidiary may put the focus on issues of liability[67], while a total collapse may suggest the need for joint administration[68].

A second critical variable is the actual degree of integration among the constituents of the enterprise prior to the insolvency. As was explained above, the legal structure of the firm may take various forms, based on equity linkages as well as contractual ones. In any of these cases the interrelations among the entities may create an integrated group[69]. Yet, the degree of integration may differ between enterprises with different degrees of autonomy enjoyed by affiliates[70]. This factor will have profound implications on the appropriate global linking tools to be applied. Thus, for instance, it could be a case of intermingling of assets and debts between entities and hosting states or conversely a case of an MCG that was operating in a more separate mode, neatly organized within national borders[71]. Accordingly, a global approach that would suggest, for example, a pooling of assets and debts mechanism to be applied on the

[66] An example of the meaning of other factors or indicators (that will not be regarded as key factors for our purposes) can be a situation where most of the group's assets are subjected to fixed charges. Whereas this is an important factor that may be influential for instance on the path in which the proceeding will take this is not of a particular imporatnce to a global approach striving to achieve an optimal link between an MCG's affiliates.
[67] See *infra* chapter 5 section 5.2.4.
[68] See *infra* chapter 4.
[69] See section 1.5.2 below.
[70] *Id.*
[71] *Id.*

MCG insolvency case[72] may be appropriate to the former but unsuitable for the latter of the above mentioned scenarios.

Whether and to what extent the MCG was centrally managed and controlled is a contributing factor in determining the degree of integration of the MCG[73]. Yet, it is not a prerequisite for integration. Indeed, an MCG can be integrated, displaying systems of managerial control and productive cooperation or having a significant level of interdependence, although decentralized[74]. Nevertheless, the degree of centralization of an MCG (or degree of autonomy exercised by its constituents)[75] is crucial in determining whether a particular venue should be used to handle the MCG insolvency process as well as in suggesting different solutions to the handling of the MCG insolvency case[76]. Thus, for our purpose, it will also be critical to distinguish between scenarios where the MCG was controlled and managed from one specific country, and a case of an MCG whose entities had high degree of autonomy in decision making.

Another factor, that is determinative to particular aspects of a global approach, is the way control was actually exercised within the group. There may be various scenarios and circumstances of corporate group behaviour which may or may not have amounted to misuse of the corporate (or the contractual) form prejudicing the interests of stakeholders. Accordingly, there will be cases in which it would be appropriate to link between affiliates in the sense of imposing liability for the debts of other members within the group while in other scenarios such an approach will not be adequate at all[77]. However, this factor (the misuse of control within the group) will be discussed separately within the discussion of the goal of fairness (particularly group responsibility), as it is specifically relevant to this issue[78].

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[72] See *infra* chapter 4 section 4.3.
[73] See section 1.5.2 below.
[74] See Blumberg, The Multinational Challenge (note 4 above), p. 142. See further 1.5.2 below.
[75] See note 48 above, and accompanying text.
[76] See *infra* chapter 4 sections 4.13.6-4.1.3.8 and *infra* chapter 7.
[77] See *infra* chapter 5 section 5.2.4.
[78] See *infra* chapter 5 section 5.2.4.

1.5 Classifying each factor into main representative scenarios

Apparently, each of the key factors delineated above entails a range of possible scenarios or degrees. For instance, integration can be very strong or non existent, members can be all in distress or only part of them collapsing etc. Therefore, in order for the above mentioned factors to serve as the dimensions around which we will later on construct our Prototypes we first need to classify each of the three factors (the insolvency scenario, the degree of integration and the degree of centralization) into a number of main representative classes. Here too, the representative categories reflect cases that are relevant to a global approach that aims to link between affiliates of an MCG in the event of insolvency. Eventually, by combining representative classes from each of the factors we will be able to define prototypical scenarios of an MCG in distress that bears significance to the application of a global model.

1.5.1 The insolvency scenarios

Most important for our purposes would be which parts of the group are under insolvency: whether it is an entire group that collapses or only the subsidiaries or otherwise whether it is a case of a specific member of a group under insolvency. A case of 'total collapse' will be treated differently than a case of a single member in distress, and will raise different issues. Typically, when there are several affiliates under insolvency; questions of ways to administer the process arise[79]. Conversely, in the single insolvency scenario (where a subsidiary is under insolvency) the focus will be put on group liability (the liability of another entity, typically the parent, to the debts of the subsidiary under insolvency[80]). Whether or not the 'controlling entity' (the parent or any other company that was the one controlling the group; hereinafter: the controlling entity) of the group is under insolvency will have additional implications. Thus, the ability to identify a centre for the MCG in one of the entities under insolvency will be influenced by the presence of the controlling entity in the insolvency proceedings[81] and thus it will imply on the question of jurisdiction[82].

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[79] See *infra* chapter 4 section 4.1.2.
[80] See *infra* chapter 5 section 5.2.4.
[81] See *infra* chapter 7.
[82] *Id.*

It is therefore suggested here, that the insolvency scenarios should be classified into three distinctive cases. The first class will incorporate the case of a collapse of more than one entity within an MCG (it can be a total collapse of an MCG or a collapse of a division thereof) including the controlling entity. This type of case will also include those instances where it appears that only one affiliate is insolvent but a closer examination will reveal that there is another affiliate (or affiliates) that although allegedly solvent is in fact under the threat of insolvency, or is highly dependent on the insolvent affiliate and expected to suffer from a 'domino effect' ending up in a state of insolvency[83]. It will also include cases where a parent and a sub-subsidiary (second-tier subsidiary) are under insolvency[84].

The second class will depict the case of multiple collapses within the MCG (similar to the first class) which does not include the controlling entity. This case involves situations in which a bundle of sister companies faces insolvency with no controlling entity subjected to the insolvency[85].

Finally, the third class of insolvency scenarios will portray a case where only a subsidiary (which is not a controlling entity) is insolvent, raising the issues of liability of another member within the group to the situation of the insolvent member. It does not refer though to cases where only the parent (or the controlling entity) is insolvent since there is no question then of holding one company liable for the debts of the other[86]. However, it should be noted that issues of group liability could also arise in cases where both the subsidiary and the controlling party are insolvent[87].

1.5.2 The integration factor

Critical factual areas have been identified in legal literature so as to help evaluate the extent to which constituents of corporate groups were genuinely separate entities or

[83] See *infra* chapter 4 sections 4.1.3.9 and 4.2.4. However, this is different from the scenario in which a parent is insolvent and the subsidiaries are genuinely solvent in which case there is no justification to drag the subsidiary into an insolvency process.
[84] Though typically joint administration will be relevant among subsidiaries and their immediate holding entity (see *infra* chapter 4 section 4.1.2)
[85] Yet, a common individual shareholder might be under a bankruptcy process as well. However, the proposed approach will apply solely to the companies under insolvency.
[86] See note 106 *infra* chapter 5.
[87] See *infra* chapter 5 section 5.2.4.

rather altogether a de facto single entity. Professor Blumberg in his treatise on the law of corporate groups[88] provides a useful 'checklist'[89] for analyzing corporate groups when dealing with the question of the legal consequences arising in their insolvency. He suggests to look for a combination of the following fundamental elements when evaluating whether the corporate group should be recognized as a single entity or not: (a) financial interdependence; (b) economic integration; (c) participation by the parent in the decision making of the constituents; and (d) holding out the group as a single integrated enterprise to the public. This can be done by assessing such factors as whether there is commingling of accounts and difficulty in segregating individual assets and liabilities, the degree of intra-group transfers, the presence of separate books and accounts and the representation to the public of the constituent companies as integral part of the group.

Professor Blumberg additionally identifies certain patterns of group interrelationship and integration, and roughly classifies corporate groups into 'strongly integrated groups', 'weakly integrated groups', 'conglomerate groups' and 'investment companies'[90]. The latter two types represent groups in which typically integration is not present. As to conglomerate enterprises and other diversified groups (that conducted variety of businesses in different industries) Professor Blumberg argues that it is more likely that the constituent companies comprising such groups will be independent, since the enterprise does not collectively carry out a common business[91].

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[88] See Blumberg, Bankruptcy (note 43 above), p. 696- 699.

[89] And it will be suggested below to employ these factors in assessing integration for the purpose of a global appraoch, together with other aspects emphasized eleswhere (see note 98 below).

[90] Blumberg, Bankruptcy (note 43 above), p. 14-16; Blumberg, *The Law of Corporate Groups: Procedural Problems in the Law of Parent and Subsidiary Corporations* (1983), section 22.02.3. This classification will be repackaged for the purpose of this study (see text preceding notes 101 and 102 below). However, it does not imply a divergence of the basic propositions suggested by Professor Blumberg in his landmark writing.

[91] Phillip I. Blumberg, The Multinational Challenge (note 4 above), p. 144-145. See also Davies, Gower Company Law (note 33 above), p. 202 explaining that an integrated business strategy does not include all groups of companies. In conglomerate groups that operate diversified businesses the group structure may be used for various reasons other than the imposition of a single business strategy. See also the way group enterprises were categorized by the American Federal Trade Commission in a statistical analysis. Groups were divided into five categories of various types of integration: horizontal extension, where the firms are actual competitors in some relevant markets; vertical extension, where the firms occupy adjacent stages in some vertical chain of production and distribution; product extension, where the firms, although not in actual competition, sell products functionally related in terms of manufacture or distribution; market extension, where the firms sell in geographically distinct markets; and pure conglomerates, where the firms are in essentially unrelated fields (F.M. Scherer, *Industrial Market Structure and Economic Performance* (3rd edn, 1990), p. 90-96; Farrar, Company Law (note 33 above), p. 9).

However, Blumberg also points out that this sort of enterprises may in fact operate in an integrated way through financial and administrative interdependence[92]. It is also suggested there that economic interrelationship and control may be present and an integrated firm may emerge within other sorts of enterprises such as companies organized in networks via contracts[93].

Typically, control will not be exercised (and an integrated group will not emerge) where companies restrict their activities to investment return distinctive from the corporation's main line of business. In these scenarios the parent is completely removed from participation in the business operations of the constituent companies[94]. It may also be the case where a joint venture or an international consortium is established for a specific and limited purpose[95]. However, it should be noted that, some joint ventures acquire a permanence which then makes the structure similar to an integrated group[96]. In some cases the entities started as joint ventures and then developed an integrated international structure, more similar to a transnational merger[97]. Furthermore, the relationship between a parent which is a partner in a joint venture and the company held and controlled by it can be regarded as an integrated group.

Other findings have concentrated on two sets of factors in ascertaining the degree of integration in management and control: first, the general influences on the locus of decision taking and, second, the degree of influence commonly exercised by the parent in relation to particular types of decisions[98]. That is, the degree of centralization/ decentralization in decision making will indicate the degree of autonomy local affiliates possessed. Integrated MCGs can emerge in the more decentralized groups as well. Yet, in decentralized network operations the head office of the group will have a different role than it has in the centralized enterprises. Its

[92] Blumberg, The Multinational Challenge (note 4 above), p. 144-145.
[93] See *Id.*, p. 246-247.
[94] See Blumberg, Bankruptcy (note 43 above), p. 432
[95] See *Id.*, p. 15. See also note 57 above.
[96] Muchlinski, Multinational Enterprises (note 9 above), p. 72.
[97] See note 52 above, and accompanying text. See also Muchlinski, Multinational Enterprises (note 9 above), p. 66.
[98] See OECD Structure and Organization of Multinational Enterprises (Paris, 1987); Dunning, Multinational Enterprises (note 46 above), p. 222-232; Martinez and Jarillo "The Evolution of Research on Co-ordination Mechanisms in Multinational Corporations" [1989] 20 Journal of International

function will be more of a coordinator than an ultimate decision maker[99]. In addition, the more the enterprise tends to be decentralized the more the affiliates gain autonomy and can be regarded as free- standing units[100].

For the purpose of this study, the possible degrees of integration within MCGs will be classified into three classes. That is, the strongly integrated MCGs, the integrated MCGs and the non-integrated MCG. The various proposed definitions, factors and typical cases with regard to corporate group's inter-relationships as indicated above[101] will be used to identify the relevant class of the three potential scenarios. It is a slightly different classification than that mentioned by Professor Blumberg[102] so as to accommodate the specific relevant traits of a proposed global model. As noted above, integration will be a decisive factor in the application of a global unified administration to multiple debtors of MCGs under insolvency[103]. Hence, at the outset, the question will be whether the case is of an integrated or a non-integrated MCG. Non-integration (of whichever type) may suggest, initially, avoiding the application of global means; however the case dynamics may change the approach[104]. 'Integration' to a certain degree will suffice for the application of the main tools of a global approach[105]. Additionally, it will be important to distinguish between two sorts of integration- the very highly integrated groups and the case of integration in a more moderate level. Strong integration will be designated as a separate class since it may suggest a need for specific and more interventionist global means for such a group's insolvency[106]. It should be noted that similarly, this classification can be looked at from the point of view of the companies comprising the group. Namely, a certain company within an MCG can be strongly integrated with the rest of the group, integrated or completely separated and autonomous.

Business Studies, 489; P.T. Muchlinski, "Corporations in International Litigation: Problems of Jurisdiction and the United Kingdom Asbestos Cases" [2001] 50 ICLQ I 1, 9-10.

[99] See Muchlinski, Multinational Enterprises (note 9 above), p. 59.

[100] See *Id.*, p. 60-61. See further in section 1.5.3 below on factors to identify the degree of centralization.

[101] The 'fundamental elements' proposed by Professor Blumberg (note 89 above) and other factors suggested for ascertaining the degree of integration (note 98 above).

[102] See note 90 above and accompanying text.

[103] See section 1.4 above; see further on the implications of integration in *infra* chapter 4 section 4.1.2.

[104] See *infra* chapter 4 section 4.1.2.

[105] *Id.*

[106] See *infra* chapter 4 section 4.3 and *infra* chapter 5 sections 5.2.2 and 5.2.4.

With regards to identification of the classes, the 'strongly integrated MCG' obviously represents the highest broad level of integration. Essentially, it refers to instances where the business of the group has been conducted (whether by a coincidence or as a strategy) as if it were a single entity, and outsiders were not aware of the group's legal structure. To put it in other words, strongly integrated groups demonstrate an organization pattern in which the group represented itself and acted functionally inter-dependently and in close integration. In terms of degree of centralization, there is obviously very low level of autonomy of the groups' members and high level of centralized control and integration of activities, as explained above. Not all relevant elements indicating high level of integration must be present in order to identify a 'strongly integrated MCG' case. Rather, the full factual picture should be considered and appreciated when determining what the type of enterprise at hand is. Thus, for instance, it is possible that a certain group although highly financially interdependent with no separate books and accounts, represented itself to the public as a conglomerate of different separate entities. If the degree of interdependence is extensive it is indeed a strongly integrated group notwithstanding the fact that it was not represented as such to outsiders.

The most powerful example of what is regarded here as strong integration is where the assets and debts of the various companies were hopelessly mixed together so at the point of insolvency it is practically impossible to disentangle the specific business of each component[107]. Strong integration could amount to an abusive integration if, for instance, integration was a planned strategy designed purposely to deceive creditors or to shield the group from potential claims[108] (this class will be referred to as "strongly integrated MCGs").

The second class – 'integrated MCG' will refer to those worldwide enterprises that were managed as a group (before the collapse), jointly operating a single business that was altogether coordinated (in the more decentralized groups) or centrally controlled (to a certain extent), or that (although diversified in their structure to a certain degree[109]) their components were inter-linked resulting with financial and

[107] See examples provided in *infra* chapter 4 section 4.3.
[108] See Muscat, The Liability (note 44 above), p. 291. See further on the issue of abuse within the MCG in *infra* chapter 5 section 5.2.4.
[109] For instance in cases of conglomerate structures (notes 90 and 91 above, and accompanying texts).

administrative interdependence. The entities are not commingled or very highly inter-dependant (as are the strongly integrated MCGs) but still they are integrated to a significant degree. An example can be an enterprise operating in a specific field, comprising of several subsidiaries conducting different activities yet all related and required for the conduct of the group's business. Although each entity has its own separate assets and liabilities and an independent management, ultimately, these activities are altogether coordinated (for example by the group's parent)[110].

In any case, here too, it should be looked at as a combination of factual circumstances (using the elements and factors mentioned above) that reaches a critical mass of links indicating a case of 'integration' (hereinafter: integrated MCGs).

The third class is the 'non-integrated MCGs'. Here as well, the identification of the specific organizational arrangement is a matter of degree. The idea is to include in this type all sorts of MCGs (or companies within the MCG) that were not integrated enterprises. In these cases, local affiliates will demonstrate high level of autonomy and the group as a whole will tend to be largely decentralized and un-coordinated. Low level of integration is more likely to be seen in pure conglomerates and other highly diversified groups[111]. In addition, typically, companies held for pure investment purposes will be truly autonomous and non-integrated[112]. It is also more likely that an autonomous company will be partly owned rather than fully held by the holding company[113] (hereinafter: non-integrated MCGs).

Finally, it should be noted, that various combinations and degrees of integration may arise within a particular MCG. An MCG may be partly non-integrated and partly integrated. For instance, it could be a strongly integrated group; however, a particular unit may be regarded as separated, if for instance, it was not part of the main line of the enterprise's business[114].

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[110] See examples provided throughout *infra* chapter 4 sections 4.1 and 4.2.
[111] See notes 90 and 91 above, and accompanying texts.
[112] See note 94 above, and accompanying text.
[113] See section 1.5.3 below.
[114] A typical example may be a finance unit of an enterprise.

1.5.3 The degree of centralized control

As explained above, integrated MCGs can vary in the degree of centralized control that the head office of the enterprise exercised over local affiliates. It was also noted above, that this factor may be crucial to the issue of international jurisdiction and the proper venue in which to handle the insolvency process.

MCGs may be hierarchically structured with skills and senior decision-takers concentrated around the parent company[115]. Alternatively, they can operate in a more decentralized manner. As was explained elsewhere[116], as a firm becomes multinational the division of responsibilities and tasks between the headquarters, regional offices and affiliates may change. In cases where the need to coordinate the global activities is important, the locus of decision taking remains in the centre, though, the role of the head office may change. Instead of the ultimate policy-maker and directing 'brain' the headquarters will act as coordinator and identifier of new business opportunities and the creator of task force networks within the firm[117]. Where the managements of local units need a great deal of local information the locus of decision taking may be largely decentralized to regional offices and/or local affiliates.

Various factors have been suggested in order to evaluate the degree of centralized control in multinational firms (and accordingly the amount of autonomy granted to local affiliates). The size of the group, the type of products it manufactures, the degree of integration of activities with the other members of the group, the targeted market and how the subsidiaries are owned are relevant factors to consider for determining the degree of autonomy a group's constituent company has. Less autonomy is expected if the company belongs to a large MCG established in many foreign countries, if it manufactures fairly standardised products; if the activities of the members are largely integrated; if it has been created to serve a market larger than the country in which it is established; or if the parent company holds a large portion of the equity[118]. Other factors to take into account are the nationality and resulting business culture of the parent; the age of the subsidiary, in that centralisation may decrease over time; the method of entry into the host state, in that a new establishment may be

[115] Muchlinski, Multinational Enterprises (note 9 above), p. 60.
[116] See Dunning, Multinational Enterprises (note 46 above), p. 223.
[117] See Muchlinski, Multinational Enterprises (note 9 above), p. 59.
[118] OECD Structure and Organization of Multinational Enterprises (Paris, 1987), p. 35.

more closely controlled than an acquired local company; the industrial sector in which the firm operates, in that some industries will be more globally integrated and centralized than others; the performance of the subsidiary, in that poor performance increases central control; and the tendency of geographically organised multinational enterprises to be less centralized than functional, product or matrix-organised firms[119].

For the purpose of a global approach the various degrees of 'centralization' or 'local autonomy' will be classified into two main representative patterns- the centralized MCGs and the coordinated MCGs. For each of these types of cases a different global mechanism (specifically related to the issue of the proper forum and its role in the insolvency process) may be used, as will be discussed later on[120].

In the centralized MCGs the head-office is the ultimate policy-maker and directing 'brain'. In the coordinated MCGs the enterprise is decentralized to a certain degree, with self-standing units of decision-takers while the head office coordinates the entire operation. This includes conglomerates in which the parent and subsidiaries are in different industries however the parent supervises the operation at least in some respects[121]. The factors indicated above should be used to identify the specific type of case at hand.

1.5.4 Other relevant factors not decisive to the application of global means

As noted above, the percentage of ownership may reflect on the degree of integration[122]. It can also prove relevant to the issue of abusive control[123]. However, it is not in itself a vital factor for the issues administration, jurisdiction or group liability that lies in the core of our model, and thus need not be promoted to being decisive in our attempt of classification. Indeed, an integrated group may be the result of a variety of factors (although it is a company less than fully controlled) implying a need for a

[119] Dunning, Multinational Enterprises (note 46 above), p. 225-226. See also P.T.Muchlinski, "Corporations in International Litigation: Problems of Jurisdiction and the United Kingdom Asbestos Cases" [2001] 50 ICLQ I 1, 10.
[120] See *infra* chapter 4 sections 4.1.3.6- 4.12.3.8, *infra* chapter 5 section 5.1 and *infra* chapter 7.
[121] See Blumberg, Bankruptcy (note 43 above), p. 434-435.
[122] See section 1.5.2 above.
[123] See note 108 *infra* chapter 5.

unifying process[124]. An abusive behaviour may be exercised by a controlling shareholder even if it only partly owns a subsidiary[125].

Similarly, the size of the MCG may indicate on the autonomy of companies and the complexity of the group and thus prove relevant to the degree of integration and centralization[126]. Still, an integrated group and/or a centralized group can emerge in small sized MCGs as it is a matter of a combination of factors[127]. It may imply on the occurrence of abuse, but an abusive control could happen in all range of enterprise dimension[128]. Thus, it is a sub-factor within integration and centralization[129] and within types of misuse of control within the MCG[130], but need not to be distinctive in our classification.

1.5.5 Considering the entire factual picture

Finally, it is important to bear in mind that the key factors identified above will sometimes have implications on more than one aspect of a global approach. For instance, the insolvency scenario may affect issues of group liability, as well as manner of administration and international jurisdiction[131]. In addition, there may be mutual influences among factors. Thus, the degree of integration may affect the degree of centralization and vice versa[132]. Hence, in order to properly evaluate the insolvency situation and determine on the proper global means to apply to the case it will be necessary to portray the specific case along each of those dimensions together. It will then enable to get a complete and comprehensive factual analysis of the case at hand. Indeed, the identification of Prototypes is geared exactly to this end and will be of assistance in this regard.

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[124] See section 1.5.2 above.
[125] See note 108 *infra* chapter 5.
[126] See section 1.5.3 above.
[127] See sections 1.5.2 and 1.5.3 above.
[128] See notes 137 and 138 *infra* chapter 5, and accompanying text.
[129] Discussed in section 1.5.2 above.
[130] Discussed in *infra* chapter 5 section 5.2.4.
[131] As will be seen in subsequent chapters (*infra* chapters 4 and 5 and 7).
[132] See sections 1.5.2 and 1.5.3 above.

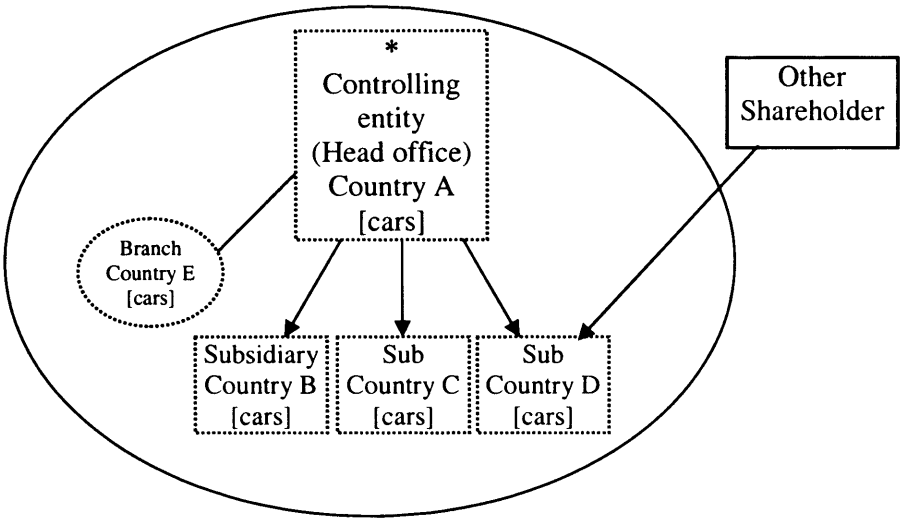
1.6 Defining 'Prototypes'

The above representative classes (distinctively classified along the three factors) can be combined together to provide 7 principal Prototypes of potential insolvency events within possible organizational types of MCGs. As aforesaid, these Prototypes do not attempt to cover all possible scenarios of MCGs in default, but rather concentrate on a number of possible cases which are most relevant to the application of a global model. Therefore, these prototypes derive from the combination of the concept of degree of integration in the variety of business forms[133] and the idea of amount of centralization[134] coupled with the basic insolvency circumstances of whether the entire MCG is collapsing or only parts thereof[135]. Later on in this work, reference will be made to these Prototypes providing some concrete examples and actual cases to demonstrate them.

The Prototypes are illustrated below accompanied by a brief explanation of what each illustration signifies. Throughout the various illustrations we will make use of standardised visual symbols. First, a box will signify a unique entity (that is, a legally different company). Second, the type of border used for these boxes will signify the insolvency status of the entity. That is, a solid box will represent a solvent company while a dotted box will represent an insolvent company. Third, arrows from one box to another will signify a linkage between affiliate entities (either equity or contractual relationships). Fourth, a star symbol will be used to indicate centralization or coordination[136]. Finally, the weight of the ellipse surrounding the boxes will signify the degree of integration within the group. That is, a thin line will represent an integrated scenario whereas a thick one will represent a strongly integrated scenario.

[133] As explored in findings in legal literature (see section 1.5.2 above).
[134] See section 1.5.3 above.
[135] See section 1.5.1 above.

Prototype A: Integrated and centralized collapsing MCG



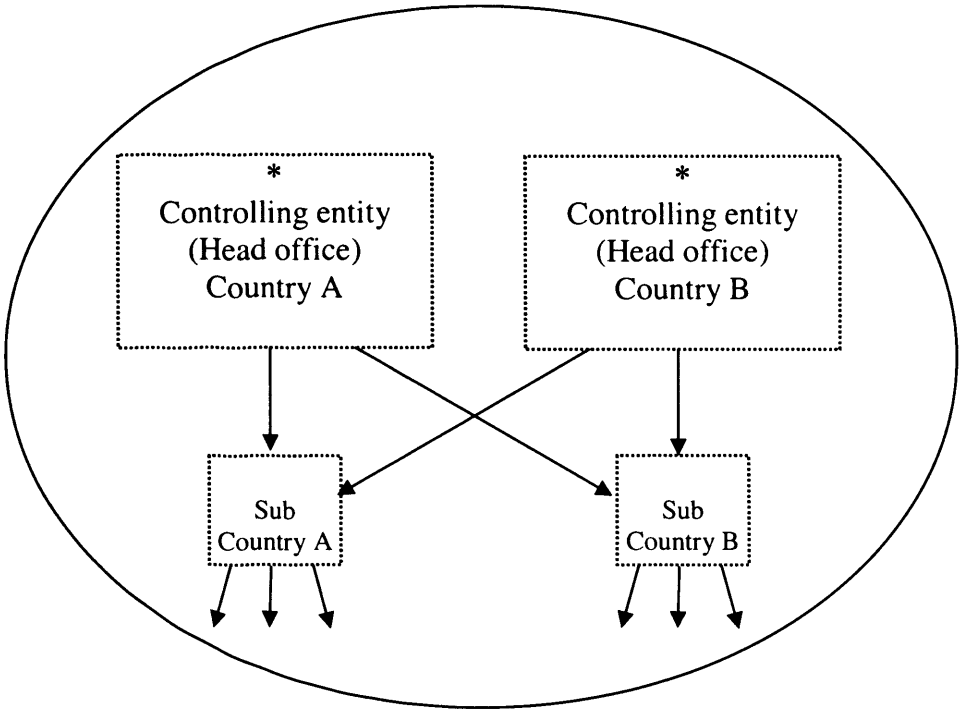
- In this case both the parent and the subsidiaries are under insolvency (all companies surrounded by the dotted line)[137].
- This Prototype includes a branch (taking the form of a small ellipse to distinguish it from a subsidiary) to illustrate the fact that the MCG may be comprised of affiliates as well as branches (subsequent Prototypes will not include branches for simplicity reasons, however obviously branches can be present in any of the Prototypes).
- It also includes a scenario where a subsidiary (the subsidiary in country D in the illustration) is also held by additional shareholders (only partly held by the controlling entity). This can be also the case in subsequent Prototypes yet again for simplicity reasons it is illustrated only here.
- The ellipse around the enterprise group represents the integration between the components (here the companies are integrated[138]).

[136] Where the star is located only in the parent's (or controlling entity's) box it is a centralized MCG, while where it is located both in the parent and the subsidiary it is a coordinated one.
[137] As in the first class of insolvency scenarios (see section 1.5.1 above).

- In this case all companies operate in the same industry (the car industry in this example) as it is typically the case in integrated centralized MCGs. The parent company in the example undertakes part of the business as well; however it can be that it will operate merely as a holding company.
- As explained above, the star [*] represents centralization. Here the enterprise is centralized with the head-office controlling the entire business[139]. In the illustration the head office is located where the immediate parent or controlling entity is located (since this is typically the case[140]). However, it may be located in one of the other affiliates' or branches' locations. The point is that the enterprise is commonly and centrally managed.
- In the illustration (and in the subsequent Prototypes as well) each entity is situated in a different country (hence representing a multinational enterprise). However, it can be that some of the entities are situated in the same place.

[138] As in the second class of the integration factor (see section 1.5.2 above).
[139] As in the first class of the centralization factor (see section 1.5.3 above).
[140] Note 115 above and accompanying text. See also *infra* chapter 7 section 7.3.

A': A 'twin holding' structure (Integrated collapsing MCG with 'double centres')

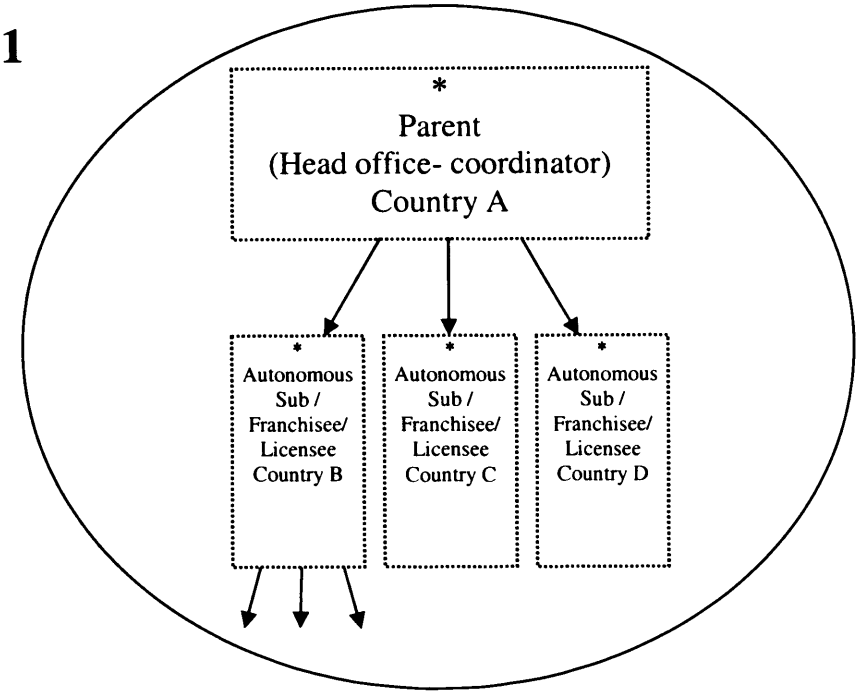


- A particular case of an integrated and centralized collapsing MCG can occur where instead of one head office there are in fact two centres controlling the entire business. This specific structure is based on joint shareholding. Thus, there are in fact two groups with two parents that together operate a single business as if they were one group (so that at the top of the enterprise there is no single controller)[141].
- It can also appear in the coordinated or the strongly integrated scenarios (as B' or C'). Yet, for simplicity reasons we put it only here.

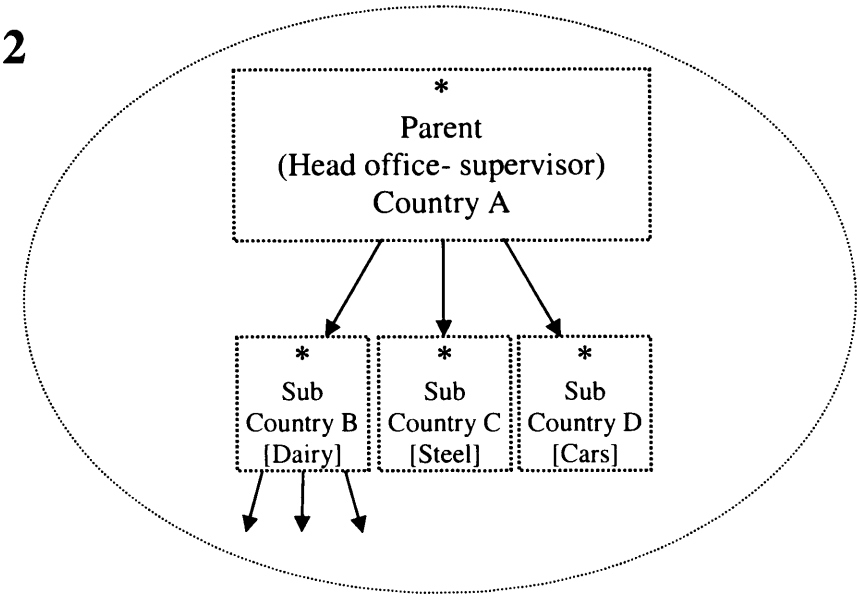
[141] See note 52 above.

Prototype B: Integrated and coordinated collapsing MCG

1



2

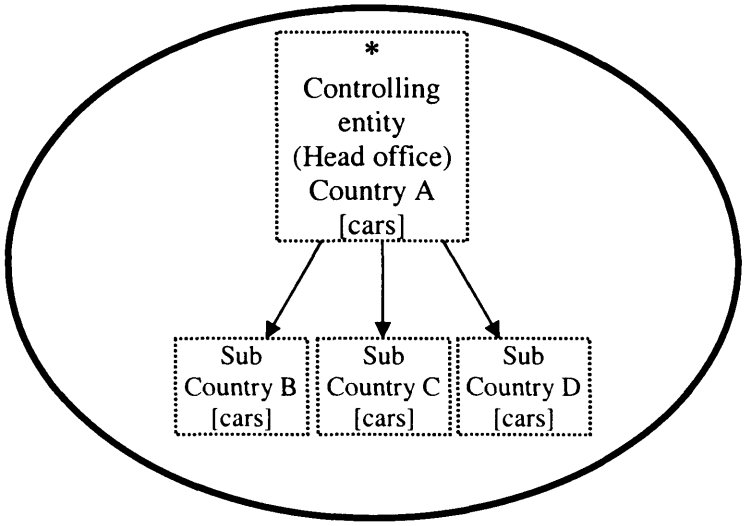


- The first figure (figure (1)) characteristically refers to more decentralized, heterarchical MCGs networks[142]. The second figure (figure (2)) refers to a conglomerate sort of enterprise (in which the companies operated different businesses), that may appear prima facie not integrated, however significant interlinks suggest it is an

integrated MCG[143]. In both figures, although the MCG is relatively diversified or decentralized, it is integrated to a significant extent; in the sense that there are considerable interrelations among the constituent companies or that the companies together comprise a single business[144].

- The enterprise is coordinated or supervised via the head-office. The local affiliates are significantly autonomous and represent separate centres of control (this is represented by the star [*] that, as opposed to the previous Prototype, also appears within the local subsidiaries). However, the subsidiaries do not function completely independently[145].

Prototype C: Strongly integrated collapsing MCG



- The wide circle represents strong integration between the components. The parent and the subsidiaries are

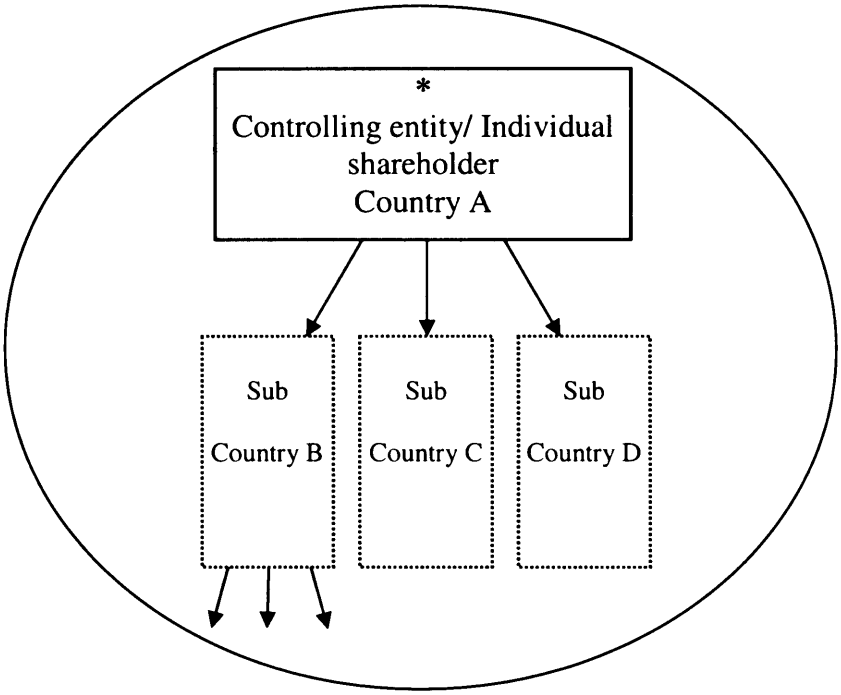
[142] See notes 93, 115 and 116 above, and accompanying texts.
[143] See notes 91 and 92 above, and accompanying text.
[144] As in the second class of the integration factor (see section 1.5.2 above).
[145] As in the second class of the centralization factor (see section 1.5.3 above).

closely interrelated and interdependent[146]. Typically, they will be centralized[147] and operate the same business, however they may have significant autonomy as in the second class of the centralization factor.

- In this scenario all companies are under insolvency[148].

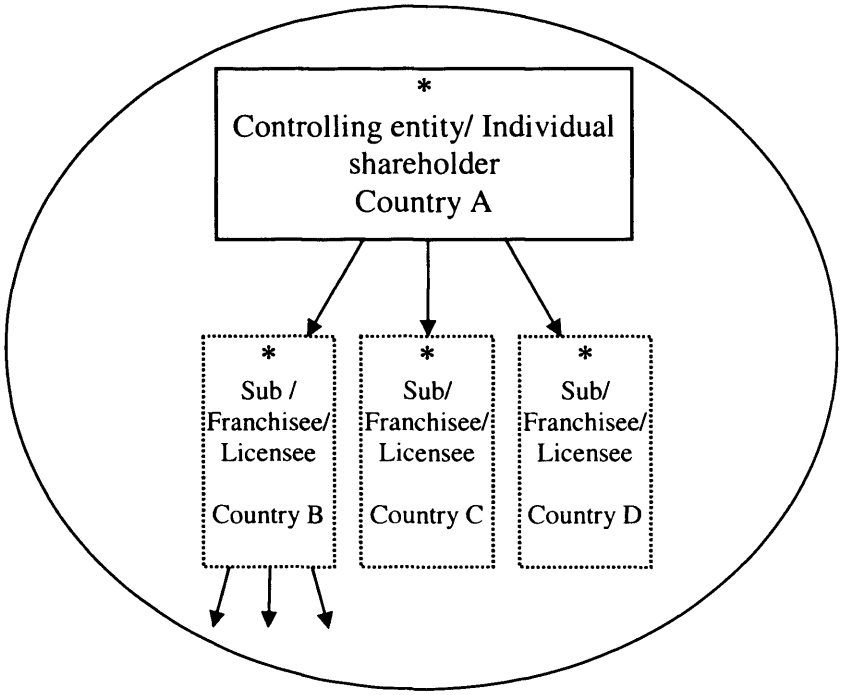
Prototype D: Insolvent subsidiaries and solvent controller within an integrated MCG

Prototype D1: Integrated and centralized MCG with a solvent controlling entity

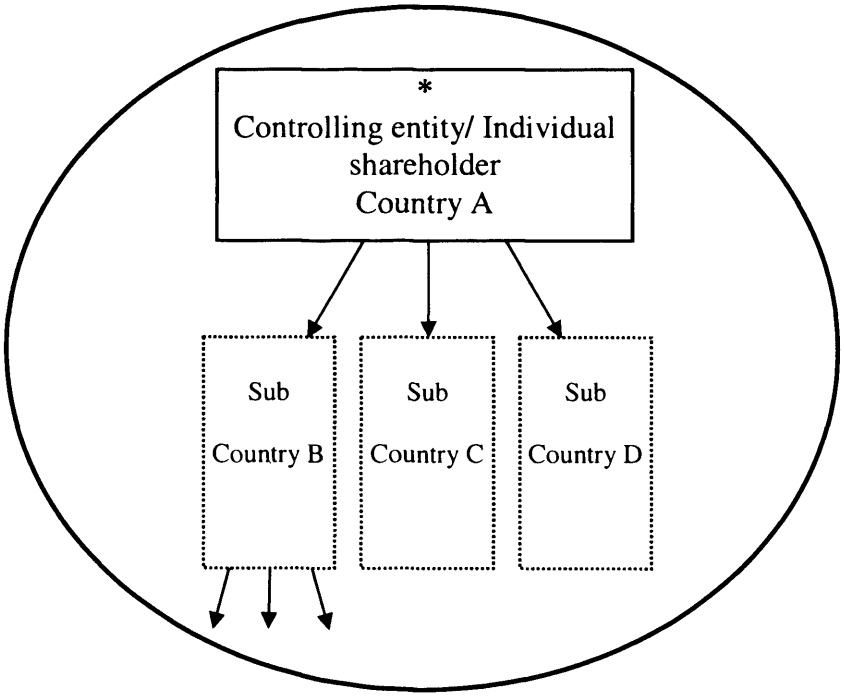


[146] As in the first class of the integration factor (see section 1.5.2 above).
[147] As in the first class of the centralization factor (see section 1.5.3 above).
[148] As in the first insolvency scenario (see section 1.5.1 above).

Prototype D2: Integrated coordinated MCG with a solvent coordinator

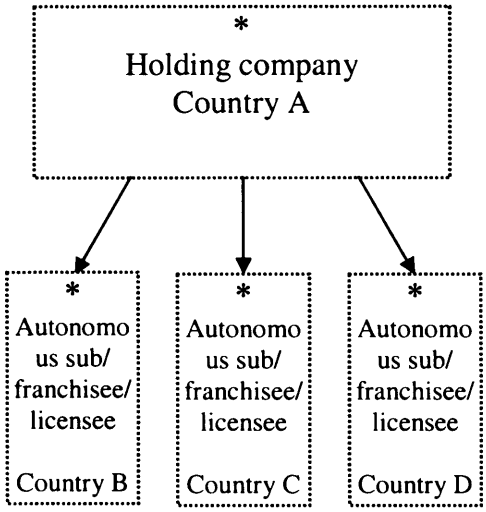


Prototype D3: Strongly integrated MCG with a solvent controlling entity



- In the above three Prototypes the corporate group was integrated to a certain degree[149] and was either centralized or commonly coordinated[150].
- However, the entity that controlled or supervised the MCG (as represented by the star [*] appearing in the controlling entity box) is not under insolvency, or the controlling shareholder was an individual[151] (note the solid line in the illustrations). Namely, it is a scenario of integrated (to a various degree) sister companies under insolvency.
- It also accommodates for scenarios in which the focus is put on the relationship between a particular insolvent subsidiary and the solvent parent[152].

Prototype E: Non-integrated collapsing MCG



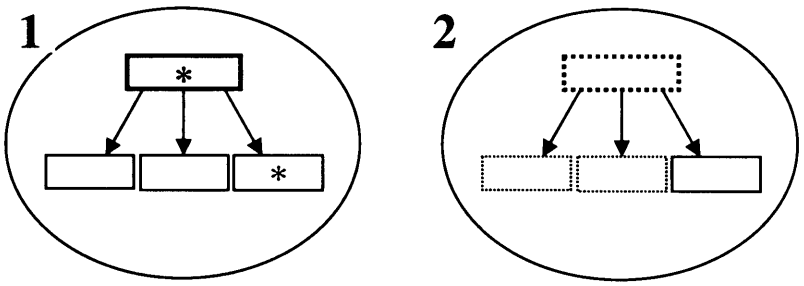
- This Prototype represents a case of non-integration[153] within a collapsing enterprise[154]. The subsidiaries function completely independently, with no significant

[149] As in the first or second class of the integration factor (see section 1.5.2 above).
[150] Either the first or the second class of the centralization factor (see section 1.5.3 above).
[151] As in the second class of insolvency scenarios; see section 1.5.1 above).
[152] As in the third insolvency scenario (see section 1.5.1 above).
[153] As in the third class of the integration factor (see section 1.5.2 above).
[154] As in the first insolvency scenario (see section 1.5.1 above).

involvement of the parent in their business operations. Accordingly, the MCG is not centralized or considerably coordinated.

Mixture of Prototypes

The Prototypes represent typical illustrative cases. However, it should be understood that a given MCG insolvency case may in reality contain a mixture of the Prototypes that were described above. Thus, for instance, it could be the case of an integrated centralized business (as in Prototype A), with one (or more) subsidiary that was significantly autonomous (as in Prototype B) – demonstrated in figure [1] below, or it could be the case of an integrated collapsing MCG with one solvent subsidiary – demonstrated in figure [2] below:



The use of the Prototypes

In the following parts of this work the selection of these specific Prototypes will become clearer as we will start to refer to them when questioning the feasibility and possible benefits of a global approach to insolvencies within MCGs. For instance, when considering the application of a unified insolvency process we will need to assess its impact on strongly integrated MCGs (Prototype C) as well as integrated and coordinated or centralized ones (Prototypes A and B)[155]. Or when the concept of a central location for the insolvency proceedings will be raised we will need to refer to the cases of

integrated and centralised MCG (Prototype A) as well as integrated collapsing MCG with 'double centres' (Prototype A') or the case where only sister companies are under insolvency (Prototype D)[156]. These discussions will be based on real cases of real MCGs, thus providing examples for the relevant Prototypes, and examining the global tools needed for the particular case. However, for our purposes, there will be no need to consider other possible Prototypes as they will have a trifling impact on our proposed global model.

1.7 Summing up

This chapter began by presenting the diversity in the ways MCGs are operating today in the worldwide arena. MCGs conduct businesses in different sizes, legal patterns, and geographical spheres and operate in various degrees of integration between the components comprising the group. By definition, this poses a major difficulty in the application of a global approach since there is no one pattern of MCG that a model can address and on which a solution can be applied. Moreover, the insolvency event itself is not of one nature but rather can occur in a variety of scenarios.

Accordingly, our primary goal here was to delineate main relevant features that are significant to the application of a global approach, and that could serve as dimensions along which some shared patterns of MCGs organizational structures and insolvency scenarios could be identified. Thus, we identified key factors pertaining to insolvencies within MCGs which were in turn divided into main classes which were then combined to form our prototypical scenarios.

Thus, we have set the scene for the collapse of the MCG. We will rely on it when addressing key aspects of the application of a global approach.

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[155] See *infra* chapters 4 and 5.
[156] See *infra* chapter 7.

Chapter 2

The theoretical platform and current models for international insolvencies and their applicability to the MCG case

2.1 Introduction

In the previous chapter we have set the infrastructure of MCGs' operations and default. We discussed the various organizational structures of multinational groups and how they operate on the international arena. Consequently, the complexity of the MCG insolvency scenario became apparent, and a way to simplify and tackle this issue was proposed. In this chapter, we move a step forward and provide an overview of the legal policies and models currently employed for dealing with insolvencies happening on a worldwide scale.

It was already indicated in the introductory chapter that we eventually seek to devise a 'global model', taking an international perspective on the event of the MCG's collapse, even disregarding the corporate form if necessary[1]. The basic paradigm underlying this approach is 'universalism'. That is, embracing a unified approach to the matter, ideally managing the company's assets and activities globally, as will be elaborated herewith. In the scenario of an MCG this may imply considering the group as a whole although it operates in a number of countries via separate subsidiaries. This chapter will begin by reviewing the main features and theoretical background of such approach confronting it with its main critique- the territorialist position. We will thus introduce the main arguments against universalism including the particular potential hardship in applying this paradigm to the MCG case. The following chapters will refer to this universality vs. territoriality debate (as well as the second relevant 'battle', between the need to respect the corporate entity and the need to unify between the affiliates' insolvencies[2]) while advocating the case for a global approach to international insolvencies of MCGs.

The current chapter will then proceed to review main available models for dealing with international insolvency cases, placing them in the context of the above

[1] Disregarding or 'lifting the corporate veil' concerns the extent to which the corporate form should be respected and will be introduced in the next chapter (*infra* chapter 3).
[2] *Id.*

mentioned universalist-territorialist debate. Clearly, it is essential to appreciate how existing models (initially designed for the single debtor insolvency scenario) opted to tackle cross-border insolvency; what tools they suggest applying and on what ideas they are grounded, before moving on to examine the advantages of embracing global tools for the MCG insolvency event.. It will be shown though that there is clear absence within those available models of explicit or inclusive reference and treatment of the particular issue of MCGs' general defaults.

2.2 Universalism v. Territorialism: alternative theoretical approaches for international insolvencies

The main dispute regarding how international insolvencies should be dealt with is between two traditional approaches (positioned on the two ends of the 'theoretical spectrum' of this issue) - universalism and territorialism[3], with their supporting principles of unity and plurality[4]. These two polarities are indeed very different in nature. One asserts separateness in the handling of the international insolvency; the other suggests a unified administration of the process. This debate is initially concerned with single debtors, but to some extent it also applies to the problem of corporate groups[5]. In fact, a major critique has been put forward against universalism regarding its ability to be applicable to cases of multiple entities operating worldwide[6]. However, before venturing forth to discuss these controversies we will first consider the basic ideas of universalism and territorialism.

True universalism[7] is aimed towards administration of multinational insolvencies by a single court applying a single insolvency law[8]. The central theoretical idea which

[3] Another position is 'contractualism' (see Robert K. Rasmussen, "A New Approach to Transnational Insolvencies" [1997] 19 Mich. J. Int'l L. 1; Robert K. Rasmussen,"Resolving Transnational Insolvencies Through Private Ordering" [2000] 98 Mich L. Rev. 2252). The theoretical benefits of such a system are highly controversial and it is regarded as unworkable both nationally and internationally (see Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2303-2307).

[4] See Ian F. Fletcher, *Insolvency in Private International Law* (2005) [hereinafter: Fletcher, Insolvency], p. 15.

[5] See e.g. Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 716-725; Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2311-2315; Lynn M. LoPucki, "Universalism Unravels" [2005] 79 Am. Bankr. L. J. 143, 152-158; Samuel L. Bufford "Global Venue Controls Are Coming: A Reply to Professor LoPucki" [2005] 79 Am. Bankr. L. J. 105, 135.

[6] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 716-725; Lynn M. LoPucki, "Universalism Unravels" [2005] 79 Am. Bankr. L. J. 143, 152-158.

[7] 'Modified universalism' will be discussed below (see text accompanying notes 18-23 below).

underlies this approach is 'market symmetry' with respect to insolvency law[9]. Namely, the assertion that for an insolvency system to be effective it has to be symmetrical with the market, covering all or nearly all transactions and stakeholders in that market with respect to the legal rights and duties embraced by those systems[10]. This derives from the consensus in bankruptcy theory that insolvency is a collective legal mechanism[11]. Insolvency demands a single proceeding in which all of the debtor's assets and claims are administered under a single set of rules. To achieve that result, it is necessary that the bankruptcy law will cover the entire market in which the debtor operates, and will bind all of its participants[12]. As this is almost universally accepted within domestic regimes[13] it should similarly be adopted as the proper approach for a multinational default. That is, an approach that aims to create a single legal regime to govern insolvencies at the international level. In other words, since a global market demands a global insolvency law, a global universalist approach is the most suitable to deal with international insolvencies[14]. Ultimately, the idea is to have an international bankruptcy system.

The universalist ideology (purely or modified as will be explained below) is a widely held approach among scholars in the cross-border insolvency field[15]. Nonetheless,

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[8] Ideally, the system will comprise of both elements (single law and single forum). Yet, compromises can be made by providing only one of the elements or having only international choice of law or choice of forum rules (see Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2292-2293; see also J.L. Westbrook, Theory and Pragmatism in Global Insolvencies: Choice of Law and Choice of Forum, [1991] 65 Am. Bankr. L.J. 457, 461).

[9] The traditional ideas from which universal jurisdiction flew were in rem jurisdiction and the idea that the debtor's assets were held for the benefit of creditors. The requirement to resolve property (in rem) questions made it necessary for one court to make all decisions involving the insolvency estate (see Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 6).

[10] Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2283-2288.

[11] Fletcher, Insolvency (note 4 above), p. 8-10.

[12] Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2284; Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 6.

[13] Note 11 above.

[14] Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2287.

[15] See e.g. T. Kraft & A. Aranson, "Transnational Bankruptcies: section 304 and Beyond" [1993] Colum. Bus. L. Rev. 329, 349-351; Kent Anderson, "The Cross-Border Insolvency Paradigm: A Defense Of The Modified Universal Approach Considering The Japanese Experience" [2000] 21 U. PA. J. INT'L ECON.L. 679; Lucian Arye Bebchuk & Andrew T. Guzman, "An Economic Analysis Of Transnational Bankruptcies" [1999] 42 J. L.& ECON. 775; Ronald J. Silverman, "Advances In Cross-Border Insolvency Cooperation: The UNCITRAL Model Law On Cross-Border Insolvency" [2000] 6 ILSA J. INT'L & COMP. L. 265; Liza Perkins, "Note, A Defense of Pure Universalism in Cross-Border Corporate Insolvencies" [2000] 32 N.Y.U. J. INT'L L. & POL. 787; Hannah L. Buxbaum, "Rethinking International Insolvency: The Neglected Role of Choice- of-Law Rules and Theory" [2000] 36 STAN.

those who maintain a universalist approach realize the difficulty in putting into practice such a regime in the near future due to the patchwork of laws in the global market[16]. Hence, the current goal is to design an 'interim solution' until there will be sufficient international consensus on the various legal matters pertaining to insolvency law so as to enable complete universalism. True (or- pure) universalism is thus regarded as an appropriate or idealistic long term solution[17].

Similar to pure universalism, under 'modified universalism' international insolvency cases are dealt from an international perspective, taking the view that assets should be collected and distributed on a worldwide basis. However, the approach takes into account the current situation in which insolvency laws differ among countries and where the cross-border insolvency case may demand proceedings to be opened in more than one state[18]. In this scenario of multi-forum, multi-law world, courts applying the modified universalism approach will seek a solution as close as possible to the ideal of single court, single law resolution[19].

They will aim at identifying a single place from where proceedings against the debtor could be handled. At the least such designated jurisdiction should be regarded as the 'main' venue for the proceedings. They will use mechanisms such as 'ancillary' (in

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J. INT'L L. 23, 60; Lore Unt, "Note, International Relations and International Insolvency Cooperation: Liberalism, Institutionalism, and Transnational Legal Dialogue" [1997] 28 LAW & POL'Y INT'L BUS. 1037; Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276.

[16] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2299-2302. Though, Professor Westbrook predicts that 'global econimic integration is driving convergence of law at a suprisingly fast pace' and that 'this trend will make it possible to achieve a workable international bankruptcy system much sooner than might have been thought' (*Id.*, p. 2291). See also, Fletcher, Insolvency (note 4 above), p. 445 (explaining that an international treaty or an international court applying single bankruptcy law is not within reach); Harry Rajak, "The Harmonisation of Insolvency Proceedings in the European Union" [2000] C.F.I.L.R. 180, 186 (stating that virtually no one considers creating a unified system attainable, at least in the short to medium term).

[17] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2299. See also Fletcher, Insolvency (note 4 above), p. 12.

[18] Until countries can agree on a specific single place to handle multinational insolvency. Even under the EU Regulation where the idea is that a single court will have international jurisdiction, in certain cases it is allowed to open a secondary process in another country or countries (see section 2.4.3.2 below).

[19] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2299-2232. This view was expressed by numerous universalists, e.g. Richard A. Gitlin & Evan D. Flaschen, "The International Void in the Law of Multinational Bankruptcy" [1987] 42 Bus. Law. 307, 322; M. Sigal et al., "The Law and Practice of International Insolvencies, Including a Draft Cross-Border Insolvency Concordat [1994-95] Ann. Surv. Bankr. L .1,2; A. Nielsen et al., "The Cross-Border Insolvency Concordat: Principles to Facilitate the Resolution of International Insolvencies" [1996] 70 Am. Bankr. L.J. 533, 534.

aid of a "main" proceeding)[20] or 'secondary' proceedings handled in 'parallel' to the main process[21]. The idea is to either defer to another court which can be regarded as handling the main process of a debtor's insolvency, or cooperating to the maximum extent with the principal insolvency process. In any case, the view is to handle the default and its resolution with a worldwide approach and to cooperate with other courts to the maximum extent possible. Recognition may not be automatic under such approaches but rather domestic courts may still have discretion to evaluate the fairness of the home-country procedures and to protect the interests of local creditors[22]. Modified universalism is thus regarded by universalist supporters as the paramount solution for the short term and as such that will foster the smoothest and fastest transition to complete universalism[23].

Another approach, similarly recognizing the need for a collaborative response to international insolvency while suggesting modifications to traditional universalism, is the 'internationalist principle' approach[24]. Mainly, it asserts that unless there is a treaty or agreement between countries, cross-border effects can take place only by use of private international law rules of the countries at hand. Yet, countries should cooperate to the maximum extent. In addition, it suggests allowing both 'plurality' and 'unity' principles to apply (with none playing a dominant role). That is, it should be possible either to have the entire estate administered in a single jurisdiction or to have a number of proceedings being handled in several countries, depending on the circumstances of the case at hand, and on cost-efficiency considerations[25].

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[20] Ancillary proceedings are not full domestic insolvencies, but rather, are limited proceedings having a narrow purpose to assist the principal process (see Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 10-12). See further on the ancillary mechanism included in the Model Law (section 2.4.4.2 below), and adopted in the ALI Principles (section 2.4.5.1 below).

[21] Parallel proceedings are full domestic insolvencies (as opposed to limited proceedings with a narrow purpose) in each country where the debtor has assets, and are generally regarded as favouring local law. Secondary proceedings can be viewed as a sub category of the parallel-proceeding approach (see Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 10-12). See further on the secondary proceeding appraoch adopted within the EU Regulation regime in section 2.4.3.2 below.

[22] See the system under the former s. 304 of the United States Bankruptcy Code (11 U.S.C. s. 304, repealed by Bankruptcy Abuse Prevention and Consumer Protection Act of 2005, Pub. L. No. 109-8, s. 802(d)(3), 119 Stat. 23, 146), and the recognition mechanism under the Model Law (section 2.4.4.2 below) and the ALI Principles (section 2.4.5.2 below). Cf. the system under the EU Regulation under which recognition is automatic (section 2.4.3.2 below).

[23] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2277, 2302.

[24] Fletcher, Insolvency (note 4 above), p. 15-17.

[25] *Id.*

By contrast, territorialism suggests that national systems will each deal with any stake of the business located within its borders as a separate estate. Instead of managing the company's assets worldwide (when we look at the single debtor case) this approach opts for 'state by state' insolvency, although the enterprise operated globally. As a consequence, where the company had operations in several countries then several independent bankruptcies might result. Each court will decide, according to local laws and practices, whether the assets within its country would be reorganized or liquidated[26]. This approach follows the ideas of 'vested rights' and national sovereignty that has also been at the core of traditional ideas of private international laws. Essentially, these concepts stress that national sovereignty imposes the law of the sovereign on all that is within its territorial reach, and that law grants vested rights in assets so situated at the time an insolvency proceeding is instituted. Thus, the law of the *situs* controls the distribution of those assets, a system which was assumed to benefit local creditors[27].

Professor LoPucki (who is perhaps the main propagator for territorialism) advocates for territoriality that includes an element of 'cooperation'- a 'cooperative territorialism'. That is, a system for international cooperation in insolvency cases grounded in territoriality[28], apparently recognizing the increasing integration of world economy. Under the proposed system each country would administer the assets located within its borders while cooperating with other countries in a variety of matters through treaty or convention.

In essence, its main claimed advantages are that it protects social and economic local policies; that the implementation of this approach requires only minimal changes in current practices, and that it enhances predictability[29]. The latter claim is arguably stemming from the fact that universalism (as compared with territorialism) is most prone to forum manipulations. The need to identify a 'home country' for the debtor

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[26] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 701; Lynn M. LoPucki, "The Case for Cooperative Territoriality In International Bankruptcy" [2000], 98 MICH L REV. 2216; Lynn M. LoPucki, Courting Failure How Competition for Big Cases Is Corrupting the Bankruptcy Courts (2005) [hereinafter: LoPucki, Courting Failure] chaps. 7 and 8; Lynn M. LoPucki, "Universalism Unravels" [2005] 79 Am. Bankr. L. J. 143.

[27] See Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, footnote 19 in p. 5, explaining that these notions were firmly entrenched in the US.

[28] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 702.

[29] *Id*, p. 751-753.

under a universalist approach (as the jurisdiction that will govern the worldwide process) makes the resulting system (according to this view) very uncertain and unpredictable[30]. In addition, as suggested, with regard to MCGs, a territorial approach fits with the way such enterprises normally operate, that is neatly within the country of operation of each subsidiary comprising the group[31].

2.3 Modified Universalism as the suitable approach for cross-border insolvency

It was convincingly argued that real cooperation in a territorial system is very limited[32]. The 'cooperative' element under this system will come to force only where it will be apparently useful to do that or 'mutually beneficial', while as a starting point each national court manages a separate process, according to national rules[33]. However, national insolvency laws and procedures differ from one another 'almost infinitely'[34]. This is the situation also with regard to national private international law rules (concerned with insolvency)[35]. Therefore, such a system will deny stakeholders from having equivalent protections and facilities across countries (or will not make any real effort to provide equal treatment).

The cooperative territorialism is not fully committed to cooperation and coordination as means to enable a worldwide perspective on the international insolvency case. Moreover, it does not aim at having the proceedings jointly directed or handled at a single forum under a single legal regime. Such narrow cooperation will hence not suffice to achieve the best results, especially in cases of reorganization attempts, which require full cooperation to the highest degree[36]. It might also defeat creditors' expectations and will fail to achieve justice, where, for example, national systems are free to deny priority treatment to foreign creditors, or where the location of the proceeding is to be grounded only on the whereabouts of assets rather than on more

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[30] *Id.* P. 713-718, 751.
[31] *Id*, at 750.
[32] Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2302.
[33] Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 750.
[34] Fletcher, Insolvency (note 4 above), p. 5.
[35] *Id.*, p. 7.
[36] Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2309. See further on the efficiency aspects and reorganization with respects to MCGs in *infra* chapter 4.

substantial predictable tests of jurisdiction[37]. Essentially, territorialism (and cooperative territorialism) fails to provide a symmetrical system to the global market, thus it does not fit with the collective nature of insolvency proceedings. The outcome of cases under this approach totally rests upon the location of assets, while this place may be elusive and manipulated, resulting with high unpredictability and susceptibility to fraud[38]. With regard to corporate groups, territorialism assumption that subsidiaries operate separately within each country of the local corporations[39] fails to contain the diversified scene of MCG. Particularly those cases where assets and liabilities were not maintained territorially, or were there were significant inter-relations among the group's members[40]. The solution provided by territorialism to these scenarios (for instance, where there was shuttling of assets), under which cooperation is achieved by way of agreement will not be sufficient or at all achievable[41]. In addition, this approach does not deal with issues of group liability, which as will be proposed in this work are an essential part of a reputed international insolvency system[42].

In addition, the "vested rights" theory[43] is unpersuasive where the local availability of valuable assets will often be fortuitous and unpredictable and will grow even more so as assets become ever more quickly transferable from country to country[44].

Indeed, as we will see below in our review of existing international initiatives to cross-border insolvency of a single debtor[45], major international models can be seen as reflecting a sort of 'universalist' view with 'down to earth' practical rules or guidelines. In essence, they attempt a worldwide perspective to international insolvencies, promoting cooperation to the maximum extent possible. They aim at identifying a venue in which the 'main' process can be handled, instead of (or as an

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[37] Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 744-748, and see the discussion on the goal of fairness in its various aspects with regard to MCGs in *infra* chapter 5.

[38] Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2309; Fletcher, Insolvency (note 4 above), p. 14.

[39] Note 31 above.

[40] Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2313. See also *supra* chapter 1.

[41] See section 2.4.2 below.

[42] See *infra* chapter 5 section 5.2.4.

[43] See note 27 above, and accompanying text.

[44] See Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 9.

[45] See in section 2.4 below (the ALI Principles (section 2.4.5 below) deal with corporate groups to some extent).

alternative to) having a number of full parallel proceedings[46]. They are designed however to reflect the circumstances where there is no single bankruptcy law and in certain circumstances no specific international forum to handle the entire process[47]. In this sense they do not correlate with pure universalism but rather they represent a sort of 'modified universalism'[48].

Nonetheless, there are a number of persuasive arguments against universalism (mostly modified universalism)[49]. However, these are valid only to the extent, and where they relate to the fact, that in the attempt to modify pure universalism 'the exceptions may swallow the rule', or where the rules are not refined enough so as to enable a comprehensive and clear result. One such argument claims that a 'secondary proceeding' mechanism (as a sort of modified universalism) could result with multiple local proceedings rather than a worldwide insolvency[50]. Another argument, relates to the 'home country' standards underlying universalist approaches[51]. That is the tests and rules for identifying the single venue for handling the 'main' process against the debtor company. As aforementioned, identifying a single forum for the international insolvency is a major feature of universalism. However, it was claimed that the rules in this regard are vague and may result with uncertainty and be prone to strategic manipulations[52]. Furthermore, and most related to this study, prima facie the Achilles' heel of universalism is the difficulty to apply it to MCGs. Arguably, 'the greatest uncertainty as to the meaning of 'home country' results from the fact that most large firms are not single entities, but corporate groups'[53]. That is, it is argued that the test for determining the proper jurisdiction for MCG insolvencies is greatly uncertain. It continues to (convincingly) claim that to date, 'no court or commentator has addressed directly the critical question of whether the home country... is determined once for the

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[46] See sections 2.4.3.2, 2.4.4.2 and 2.4.5.1 below.
[47] *Id.*
[48] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2299-2302.
[49] For the list of what Professor LoPucki identifies as the 'problems' of universalism and modified universalism see Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 709-725; 728-732; 734-737. See also Lynn M. LoPucki, "Universalism Unravels" [2005] 79 Am. Bankr. L. J. 143, 143-144.
[50] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 734.
[51] For instance the concept of COMI under the EU Regulation (see notes 92-99 below and accompanying text).
[52] Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 713-718, 720-723.
[53] *Id.*, p. 716.

entire corporate group, separately for each member of the group, or for the financially distressed entities of the group as a whole'[54].

As this study will put forward the case for universalism, as part of the argument for a 'global approach' it will need to address (in subsequent chapters) these very complex issues[55]. While exploring in subsequent chapters[56] the advantages or the flaws in a unified process for the MCG insolvency case, it will become clearer why territorialism is not compatible to deal with the cases (or why certain claimed problems of universalism are not 'real' notwithstanding the complexities of the multiple entity scenarios). On the other hand, specific tools, refinements and additional features to existing paradigms will be suggested, to make the proposed approach compatible to deal with the MCG case and in order to overcome universalism's real flaws.

2.4 From theory to action- international models for cross-border insolvency and their applicability to MCGs

2.4.1. Limitations of domestic solutions

Notwithstanding legislative reforms on matters of insolvency including international aspects[57] as well as international initiatives aimed at encouraging standardization of insolvency laws[58], currently, as was indicated above, national laws still widely differ. This refers to rules of substance as well as procedure, rules of private international law and other domestic powers of assistance and cooperation and the method in which they are applied[59]. In addition, although universalism (and modified universalism) is favourably embraced in legal literature and can be regarded as the basic methodology

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[54] *Id.*, p. 716-717. See also Lynn M. LoPucki, "Universalism Unravels" [2005] 79 Am. Bankr. L. J. 143, 143-144.

[55] See *infra* chapters 4-7.

[56] *Id.*

[57] Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2278; Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1.

[58] See e.g. UNCITRAL Legislative Guide on Insolvency Law (2005) [http://www.uncitral.org/pdf/english/texts/insolven/05-80722_Ebook.pdf] [hereinafter: UNCITRAL Legislative Guide]; Creditor Rights and Insolvency Standard, based on The World Bank Principles for Effective Creditor Rights and Insolvency Systems and UNCITRAL Legislative Guide on Insolvency Law, Revised Draft [December, 2005] (http://web.worldbank.org/WBSITE/EXTERNAL/TOPICS/LAWANDJUSTICE/GILD/0,,contentMDK:20774191~pagePK:64065425~piPK:162156~theSitePK:215006,00.html) [hereinafter: World Bank-UNCITRAL Standard].

[59] See Fletcher, Insolvency (note 4 above), p. 3-15.

of certain domestic insolvency approaches to international insolvencies[60], countries have generally applied a more territorialistic method (a "grab rule" approach)[61].

This multiplicity and incompatibility of local insolvency laws impose a substantial barrier on achieving efficient coordinated insolvencies that cross borders. In principle, one country acting alone cannot achieve a legal system that will deal with all aspects and difficulties involved with insolvency of multinational companies[62]. It has been thus observed, that in order to attain the goals of universalism a more uniform and comprehensive regime is needed on the international rather the national level[63].

2.4.2 Ad hoc means for tackling international insolvencies

Before examining the major international models for cross-border insolvencies, which attempt to provide a framework that can be systematically used in cross border insolvency cases, another 'group of methods' to approach international insolvencies, should be mentioned. That is, 'ad hoc' - case-by-case mechanisms that are based on full reciprocity. This refers to the use of private international agreements ("Protocols"), the appointment of office holders in order to facilitate parallel insolvencies taking place in different countries and communications between courts and appointees.

Protocols that enable office holders to run concurrent insolvency proceedings taking place in different countries in a coordinated manner are one such example. They are negotiated and agreed upon during the insolvency proceedings (by lawyers and

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[60] See e.g. international cooperation by the UK courts under section 426 of the Insolvency Act 1986 (portrayed in Fletcher, Insolvency (note 4 above), p. 225-247) and the ancillary proceedings pursuant to former section 304 of the US Bankruptcy Code (see Jay Lawrence Westbrook, and Jacob Ziegel, "NAFTA Insolvency Project" [1997-1998] 23 Brook. J. Int'l L. 8, 14; Flethcer, Insolvency (note 4 above), p. 247-262).

[61] See Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 8; David Costa Levenson, "Proposal for Reform of Choice of Avoidance Law in the Context of International Bankruptcies from a U.S. Perspective" [2002] 10 Am. Bankr. Inst. L. Rev. 291, 293; Elizabeth J. Gerber, "Not All Politics Is Local: The New Chapter 15 to Govern Cross-Border Insolvencies" [2003] 71 Fordham L. Rev. 2051, 2058; Evelyn H. Biery et al, "A Look at Transnational Insolvencies and Chapter 15 of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005" [2005] 1 Bost. Col. L. Rev., 23, 26-27.

[62] See Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 5; Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2279; Fletcher, Insolvency (note 4 above), p. 495-496.

[63] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2288; Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 5; Flethcer, Insolvency (note 4 above), p. 227.

accountants for the parties), may cover any range of issues and are approved by the courts[64]. The idea is to avoid potential conflicts and 'international chaos'[65]. This mechanism can be used together with the appointment of 'examiners' or 'foreign representatives' by the courts involved. These office holders may accordingly act as mediators and facilitators of the parallel insolvency process and can also negotiate Protocols[66].

Bridging between parallel proceedings can be also achieved using direct communication between the courts involved. Instead, or additionally to Protocols courts have recently been using this method of 'direct judicial conversations'[67].

The use of Protocols and direct judicial communication has become 'a routine' in cases involving Canada and the United States[68]. This mechanism is used not only for single debtors operating worldwide but also for corporate groups[69]. Indeed, in most

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[64] See e.g. the Protocols used in the case of Maxwell (*Re* Maxwell Communications Corp. [1993] 1 W.L.R. 1402 (Ch. 1993); 170 B.R. 800 (Bankr. S.D.N.Y. 1994)) and Nakash (In re Nakash, No. 94-13-44840 (BRL) (Bankr. S.D.N.Y. May, 23, 1996); D.C. (Jm.) 1595/87, In re Nakash [1996]). See also Evan D. Flaschen, Anthony J. Smith, J., Leo Plank, "Case Study: Foreign Representatives in U.S. Chapter 11 Cases: Filling the Void in the Law of Multinational Insolvencies" [2001] 17 Conn. J. Int'l L. 7-13.

[65] See *Id.*

[66] See the Maxwell and Nakash cases mentioned above (note 64 above) in which the US court appointed examiners to coordinate and negotiate Protocols; and the Singer case in which the US court appointed a foreign representative to coordinate a consistent approach to the overall international conglomerate (In re Singer Company N.V., 262 B.R. 257 (Bankr. S.D.N.Y 2001)). See also Evan D. Flaschen, Anthony J. Smith, J., Leo Plank, "Case Study: Foreign Representatives in U.S. Chapter 11 Cases: Filling the Void in the Law of Multinational Insolvencies" [2001] 17 Conn. J. Int'l L. 7-18 (indicating the shortcomings of 'examiners' and Protocols and proposing that the 'foreign representative' is an appropriate method for cross-border insolvencies to which the US is a party, as it enables to retain the 'debtor in possession' while appointing a facilitator and mediator sufficiently independent of the debtor).

[67] This can be done by various means such as telephone conversations, videoconferences and exchanging emails. On April 14, 2003, a formal inter-court communication has been conducted involving (for the first time) England and the United States, in respect of Cenargo International Plc and related companies (*Re* Norse Irish Ferries & Cenargo Navigation Limited (unreported, 20 February, 2003), Ch D); see Insolv. Int. 2003, 16 (6), 47-48 (NOTICEBOARD- Co-operation Between Courts); Shandro, Sandy and Tett, Richard, "The Cenargo Case: A Tale of Conflict, Greed Contempt, comity and Costs", Insol World- Fourth Quarter 2003, 33-35; Susan Moore, "Cenargo: A Tale of two courts, comity and (alleged!) contempt!", January 2004 (http://www.iiiglobal.org/members/committee_c/cenargo.PDF).

[68] See Jay Lawrence Westbrook, "International Judicial Negotiations" [2003] 38 Tex. Int'l L.J. 567, 572 footnote 30. See also generally Jacob S. Ziegel, "Corporate Groups and Crossborder Insolvencies: A Canada- United States Perspective" [2002] 7 Fordham J. Corp. & Fin. L. 367; Robert K. Rasmussen, "The Problem of Corporate Groups, a Comment on Professor Ziegel" [2002] 7 Fordham J. Corp. & Fin. L. 395.

[69] See, e.g., *Re* Maxwell Communications Corp., [1993] 1 W.L.R. 1402 (Ch. 1993); 170 B.R. 800 (Bankr. S.D.N.Y. 1994); In re Inverworld 267 B.R. 732, 740 n. 10 (Bankr. W.D. Tex. 2001); In re Smouha 136 B.R. 921 (in the BCCI cases); In re Loewen Group Int'l., Inc., No. 99-1244, 2002 U.S. Bankr. LEXIS 199 (Bankr. D. Del. 1999); In re Enron, No. 01-16034, 2001 Extra Lexis 304, at 2, (Bankr. S.D.N.Y. Dec. 10, 2001); In re Singer Company N.V., 262 B.R. 257 (Bankr. S.D.N.Y 2001);

cases where it was used, the result was an efficient administration of the whole insolvency proceedings and in some cases enabled a worldwide settlement or an optimal combined plan of reorganization[70]. However, the practicality of ad-hoc solutions on a global scale is limited.

Clearly, the success of such mechanisms is highly dependant on local courts' willingness and capability under domestic laws to cooperate with a foreign court. Ad hoc means lack the authoritative element and the needed framework to enable consistent predictable outcomes. Producing "real-time" responses through the use of judicial communication for instance may prove difficult in cases where numerous parties are involved especially when they are located in different time-zones and use different languages. Similarly, negotiating Protocols could be highly costly and even unfeasible where numerous countries are involved[71].

All in all, these methods can prove highly useful; however they should be part of more orderly regimes in order to be broadly effective[72]. Even then, and specifically for the case of the corporate group, they are insufficient as stand alone methods for dealing with the unique demands of these cases, and where national laws highly differ. These cases will demand a variety of tools more adequately designed to the different Prototypes of potential insolvency scenarios and groups' structures[73], including

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Global Crossing Ltd (Chapter 11 No. 02-40188-reg (REG) (Bankr. S.D.N.Y.); Federal Mogul (Re T&N Ltd And Others ([2004] All E.R. (D) 283 (Oct)). See also Jay Lawrence Westbrook, "International Judicial Negotiations" [2003] 38 Tex. Int'l L.J. 567, 571-573 (referring to the Maxwell, re Loewen and re Inverworld cases); Jacob S. Ziegel, "Corporate Groups and Crossborder Insolvencies: A Canada-United States Perspective" [2002] 7 Fordham J. Corp. & Fin. L. 367, 369 (explaining the phenomena of corporate groups cases operating both in Canada and in the United states); Robert K. Rasmussen, "The Problem of Corporate Groups, a Comment on Professor Ziegel" [2002] 7 Fordham J. Corp. & Fin. L. 395, 404 (referring to the re Loewen Group case); Douglas G. Baird & Robert K. Rasmussen, "The Four (or Five) Easy Lessons from Enron" [2002] 55 Vand. L. Rev. 1787 (discussing the Enron group case); E. Bruce Leonard, "Coordinating Cross-Border Insolvency Cases" International Insolvency Institute, June 2001 (http://www.iiiglobal.org/members/committee_a/Co-ordinating_Cross-Border_Insolvency_Cases.pdf).

[70] See *Id.*

[71] See Evan D. Flaschen, Anthony J. Smith, J., Leo Plank, "Case Study: Foreign Representatives in U.S. Chapter 11 Cases: Filling the Void in the Law of Multinational Insolvencies" [2001] 17 Conn. J. Int'l L. 13-14.

[72] Indeed, the Model Law provides explicitly for direct communication between courts (see section 2.4.4.2 below) however it does not provide a mechanism for achieving it. The ALI Principles encourage direct communication. They further adopt guidelines for such communications and attach two exemplary protocols as Appendix (see section 2.4.5.2 below). The subject is unadressed by the EU Regulation.

[73] See *supra* chapter 1.

enforceable tools to deal with issues of group liability. Evidently, such issues can not be fully resolved by relying on good will and mutual consent[74].

In any case, clearly, an international framework of some sort is essential for cross-border insolvency cases. This understanding was the driving force behind recent initiatives on the international level that will now be examined.

2.4.3 The EU Regulation[75]

2.4.3.1. The conceptual approach

The EU Regulation, in force since 31 May 2002[76], contains provisions regarding jurisdiction, recognition of judgments and the law applicable to the insolvency proceedings. These provisions are binding and directly applicable in Member States. In other words, it creates internationally enforceable rules with multinational application. It is hence a rather drastic scheme, enabling close coordination of transnational insolvencies[77].

However, as it is confined within the boundaries of the European community[78], designed for exclusive use among the Member States, it is limited in nature[79]. Namely, it does not apply globally as it is a regional instrument. Obviously, insolvency cases may involve foreign elements that extend beyond the Member States. As a result, parties can be deprived of the facilities the Regulation proposes or evade legal consequences (sometimes purposely)[80]. Nevertheless, the Regulation can significantly affect the rights and interests of parties from third states involved in a European centred case. Furthermore, the Regulation is of great importance in

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[74] See *infra* chapters 4-7.

[75] Council Regulation No. 1346/2000 on Insolvency Proceedings [http://www.europa.eu.int/eur-lex] [hereinafter: EU Regulation or Regulation, interchangeably].

[76] For history of the EU Regulation see Fletcher, Insolvency (note 4 above), chap. 7 section 7.1. See also on the process leading up to the Regulation in Harry Rajak, "The Harmonisation of Insolvency Proceedings in the European Union" [2000] C.F.I.L.R. 180, 180-190.

[77] See I.F.Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL, Cross-Border Insolvency, 15.

[78] Encompassing all Member States, except for Denmark.

[79] See Fletcher, Insolvency (note 4 above), p. 443-444.

[80] This is true even if part of their operations is located within the community as long as the centre of main interests of the debtor is in a non-participating country, as will be elaborated below.

providing a scheme which operates in practice for developing global solutions for cross-border insolvencies[81].

The Regulation recognizes the increasing number of companies operating on a worldwide basis[82]. It also appreciates that in order to ensure the proper functioning of the internal market it is necessary to have a framework for cross-border insolvency at community level (rather than national level), providing means for cooperation and coordination[83]. Accordingly, its aim is that every debtor will be subjected to a unitary insolvency process having universal effects.

Therefore, the Regulation can be viewed as based on a universalist approach[84], as it intends to look at the international insolvency case with an international perspective (as long as it falls within the scope of the Regulation, as aforesaid). It actually refers to the idea of 'market symmetry', which is in the core of the theoretical basis of universalism[85], when it states that its adoption is necessitated by the integration of the internal market. The goal is hence to have the cross-border insolvency proceedings administered in a manner beneficial to all creditors regardless of the Member State to which they happen to belong, and that creditors will receive equal treatment, wherever they are located[86].

The Regulation is 'modified' however, in that it attempts to balance the 'unity' principle with the need to have regard to legitimate expectations of creditors[87] with the result of allowing a local (rather than solely global) proceeding to take place in certain circumstances, in the form of 'secondary' proceedings[88]. In addition, it provides a set of exceptions to the basic choice of law rule[89]. These modifications are the result of acknowledging the wide differences between Member States' substantive laws[90].

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[81] See I.F.Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL, Cross-Border Insolvency, 15-16.
[82] See Recital (3) to the EU Regulation (note 75 above).
[83] See Recitals (1)-(8) to the EU Regulation (note 75 above).
[84] See the Universalism-Territorialism debate described in section 2.2 above.
[85] See text preceding note 10 above. See also Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 6.
[86] See I.F.Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL, Cross-Border Insolvency, 15, 20.
[87] See Recitals (12) and (24) to the EU Regulation (note 75 above).
[88] See the discussion on the 'secondary' proceeding device in section 2.4.3.2 below.
[89] See the discussion on choice of law under the EU Regulation in section 2.4.3.2 below.
[90] See Recital (11) to the EU Regulation (note 75 above).

It is a question though whether these exceptions 'swallow the rule' to a degree that makes the Regulation more territorial than universal in its underlying approach[91]. Looking at the main elements of the Regulation it seems that unity is indeed the ultimate goal though it may be at risk if local proceedings are opened without restraint and if local courts focus on domestic interests. A closer look at the various provision of the Regulation will enable to appreciate the various tools it provides and their underlying ideas.

2.4.3.2. Key Provisions

The Regulation imposes mandatory rules for the taking of jurisdiction to commence an insolvency process. The key concept in this respect is that the main proceedings against the debtor should take place in the jurisdiction where its centre of main interests is located (hereinafter: COMI)[92]. This is also the decisive criterion for the application of the Regulation. The Regulation applies only to proceedings where the debtor's COMI is located in the Community[93] .

The concept of COMI thus plays a vital role. Yet, there is no definition for this test in the Regulation, except that Recital (13) (taken from the Virgos-Schmit Report)[94] explains that it is the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties[95]. This

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[91] See note 50 above and accompanying text.

[92] Article 3(1) of the EU Regulation (note 75 above).

[93] Recital (14) to the EU Regulation (note 75 above). In the *Brac* case it was made clear by the English High Court that this includes companies incorporated in third states whose COMI was located in one of the Member States (see In re Brac Rent-A-Car Inc [2003] EWHC (Ch) 128, [2003] B.C.C. 248).

[94] Report Virgos/Schmit (nr. 75); The Report has been issued to serve as an interpretive guide to the Insolvency Convention of 1995, which five years later has been altered to the Insolvency Regulation. The Report has been recognized as an unofficial guide to interpretation [hereinafter: Report Virgos/Schmit] (see comments made in this regard in EU Regulation courts' decisions for instance In re Brac Rent-A-Car Inc [2003] EWHC (Ch) 128, [2003] B.C.C. 248 and in Geveran Trading Co Ltd v Skjevesland [2003] B.C.C. 209).

[95] See also I.F.Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL, Cross-Border Insolvency, 15, 27-28; Fletcher, Insolvency (note 4 above), p. 366-369; Bob Wessels, "International Jurisdiction to Open Insolvency Proceedings in Europe, In Particular Against (Groups of) Companies" Working Papers Series, Institute for Law and Finance, Johann Wolfgang Goethe University (http://www.iiiglobal.org/country/european_union/InternJurisdictionCompanies.pdf), p. 4-6; The importance of meeting third parties' legitimate expectations with regard to jurisdiction to open insolvency proceeding was also expressed in several EU Regulation cases, see e.g. Geveran Trading Co Ltd v Skjevesland [2003] B.C.C. 209; Daisytek- ISA Ltd, Re [2003] B.C.C. 562 (Ch D); Re Parmalat Hungary/Slovakia, Municipality Court of Fejer, 14 June, 2004; Ci4Net.com. Inc [2005] B.C.C. 277 (Ch D); Eurofood IFSC Limited [2004] B.C.C. 383. Both the preliminary opinion, by an advocate General attached to the European Court of Justice in the case of Eurofood (Eurofood IFSC Ltd (C- 341/04)

relative absence of a well defined test may lead to uncertainty and enhance jurisdictional conflicts. Indeed, a major critique against universalism and its application in international models is the vagueness of the home country standard[96]. We will examine these potential flaws at a later stage while attempting to construe adequate solutions to the issues of forum shopping, the need for legal certainty and the proper jurisdiction for the MCG[97]. What is significant to note for now, is that it is a test that apparently looks for the 'real seat' of the debtor[98], while the place of the company's incorporation is only the point of departure (a rebuttable presumption)[99].

The main proceeding being handled in the jurisdiction of the debtor's COMI has a universal scope and is intended to encompass the debtor's assets on a world-wide basis and to affect all creditors, wherever they may be located[100]. In addition, the main rule is that only one set of proceedings may be opened in the community against the debtor, thus reflecting the principle of unity.

As indicated above, the universalist approach is modified in that it is possible to open local proceedings against the debtor in particular circumstances. The key concept in relation to the opening of such proceedings is the existence of an 'establishment' in relation to the debtor[101]. Here too, the test looks for substantial links to the territory, rather than the mere presence of assets of the debtor[102]. The idea is to evaluate the external impression with regard to the debtor's operation (rather than the subjective intentions of the debtor), as a reliable factor for allowing local creditors equal rules and conditions as compared to national operators with whom they are competing in

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[2005] B.C.C. 1021 (AGO), at paras. 106-126) and the ECJ decision in the case (Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397, paras. 33-37) emphasized the significance of the requirements of transparency and ascertainability by creditors of the COMI. See further on the issue of jurisdiction and creditors' expectations in *infra* chapter 5 section 5.1.

[96] See notes 51-52 above, and accompanying text. The issue of identifying the proper venue for the MCG insolvency will be discussed in *infra* chapter 7.

[97] See *infra* chapters 6 sections 6.1 and 6.2, and *infra* chapter 7.

[98] Thus, it is regarded as a victory for the civil law inspired 'real seat' theory of jurisdictional competence over the 'state of incorporation' theory traditionally espoused by the members of the Anglo-American common law 'family' (see Fletcher, Insolvency (note 4 above), p. 368-369).

[99] The COMI is presumed to be in the place of the debtor's registered office. This presumption can be rebutted if a party can show that the company's main interests is conducted on a regular basis at a place in some other Member State in a manner which is ascertainable by third parties (Article 3(1) and Article 3(2) of the EU Regulation (note 75 above)); I.F. Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL CROSS-BORDER INSOLVENCY A Guide to Recognition and Enforcement, 15, 27-31).

[100] Virgos-Schmit Report (note 94 above), para. 73.

[101] Article 3(2) of the EU Regulation (note 75 above).

[102] See para. 71 of the Virgos Schmidt report (note 94 above). The EU Regulation refers to the place where the debtor carries out a non-transitory economic activity (with human means and goods) (Article 2(h) of the EU Regulation (note 75 above)).

the same territory. That is, whether external appearances suggest a locally-established business operation[103].

A problematic restriction with regard to the opening of territorial proceedings is that they must be winding up proceedings, thus limiting the possibilities of global rescue plans[104]. In addition to these strictly defined circumstances in which territorial proceedings can be opened, the effects of the territorial proceedings are restricted to the assets of the debtor situated in the territory[105].

The Regulation adopts the concept of enabling a territorial process to be taking place in 'parallel' to the main proceedings[106]. This means that, the proceedings are separate in the sense that they are handled locally (assets are distributed on a territorial basis) and are subjected to the domestic insolvency law[107]. In this respect, it was argued that the Regulation tends to be territorial[108]. The 'territorial' proceeding in parallel to the main process mechanism arguably contradicts a universalist approach, since it can result with multiple local proceedings rather than a worldwide insolvency[109]. Both with regard to the effect of the opening of the main proceeding and the binding effect of a reorganization plan, the situation under the EU Regulation is not entirely clear when such local proceedings are opened in parallel to the main process, and there is a potential of disrupting the success of the international insolvency process[110].

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[103] Fletcher, Insolvency (note 4 above), p. 376-377.

[104] See Article 3(2) of the EU Regulation (note 75 above); Fletcher, Insolvency (note 4 above), p. 370-371. See further on the merits of a global approach with regard to global reorganizations in *infra* chapter 4 sections 4.1.3.1- 4.1.3.9.

[105] Article 3(2) of the EU Regulation (note 75 above).

[106] Article 3(2) of the EU Regulation (note 75 above).

[107] This is because the basic choice of law rule provides that the law applicable is that of the state of the opening of proceedings (see note 130 below and accompanying text).

[108] See Jay Lawrence Westbrook, "Managing Defaulting Multinationals within NAFTA" in I.F.Fletcher, L. Mistelis, M. Cremona (eds.), *Foundations and perspectives of International Trade Law* (2001), p. 476..

[109] Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 734-735.

[110] See, for instance, the question posed by Prof. Westbrook in this regard, that is whether a creditor who opposed a plan that was approved over its dissent in a main proceeding in country A may nonetheless sue the post re- organization debtor in country B on the original debt if there was a secondary proceeding in country B (Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 36). See also the concern expressed in this regard in Harry Rajak, *Company Liquidations* (2006) [hereinafter: Rajak, Company Liquidations], p. 356-357 that through secondary proceeding, local creditors may either secure a better deal for themselves or make a severe nuisance and blackmail the liquidator of the main proceeding into complying with their demands).

Yet, there are strong indications in the Regulation that re-affirms its main and basic principle – the essential need for unity[111]. Thus, if territorial proceedings are opened in parallel to main proceedings (that is subsequently to the opening of main proceedings[112]) they do not take place in complete isolation because they become designated as 'secondary' proceedings and as such are subject to rules which are designed to ensure that the secondary proceedings are integrated into the overall process of administering the insolvent debtor's estate for the benefit of creditors generally[113] (thus can be regarded as 'truly secondary'[114]). In particular, the unity of the debtor's estate is maintained through rules based on the doctrine of Hotchpot[115], on the consolidation of any surplus left over at the conclusion of the secondary proceedings[116], and on the right of all creditors to lodge claims in the main and in any secondary proceedings[117] and to participate in all proceedings, whether main or secondary[118]. In addition, once multiple proceedings emerge the liquidators have to communicate information and co-operate with each other[119]. In sum, the Regulation provides a balance between the need to meet creditors' expectations and the universalist idea, reflected in the secondary proceeding mechanism. Accordingly, though, if this mechanism is used without restraint the balance may be disrupted thus it may jeopardise unity, especially where reorganization is sought[120]. We will look at the issue of opening local proceedings when we will discuss later on the particular case of MCG, referring to the above secondary mechanism[121].

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[111] See I.F.Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL, Cross-Border Insolvency, 15, 44; Rajak, Company Liquidations (note 110 above), p, 354- 357.

[112] Territorial proceedings can also be opened in advance of any main proceedings. In this case they are 'free standing' (see Article 3(4) of the EU Regulation (note 75 above)).

[113] See Fletcher, Insolvency (note 4 above), p. 374.

[114] See Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 11-12.

[115] Article 20 of the EU Regulation (note 75 above) (the common law rule according to which a creditor that receives a distribution in a foreign insolvency proceeding must stand aside in a local distribution until creditors of the same class (under local law) have gotten as much from the local proceeding as the first creditor got from the foreign one.

116 Article 35 of the EU Regulation (note 75 above).

[117] Article 32 of the EU Regulation (note 75 above).

[118] Article 32 of the EU Regulation (note 75 above).

[119] Article 31 of the EU Regulation (note 75 above).

[120] Prof. Westbrook indicated 'a worst case' for universalism in this context, and that is where the debtor has establishments with creditors who have preferential claims, in all the countries where it has substantial assets, giving creditors both the motive and opportunity to initiate secondary proceedings (see Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, footnote 124 in p. 34).

[121] See *infra* chapter 4 section 4.1.3.8.

The jurisdictional rules explained above are matched by mandatory rules for the recognition of such proceedings in other member states and of the effects deriving from such recognition[122]. These rules represent an 'unparalleled advance' in the conduct of international insolvency, in that it enables automatic recognition for judgments[123]. Member States can deny recognition only in the rare case where it will be contradictory to national public policy[124]. This enables the office holder to take speedy measures in other Member States to assert his rights to control and administer the estate as a unity[125].

The Regulation does not provide, however, any procedure or mechanism for determining the proper jurisdiction in cases where two or more countries can be possibly regarded as the proper candidates (for a proper forum), but merely grants primacy of effect to the first court to open proceedings. The possibility to request a preliminary ruling of the ECJ in such an event will be hardly effective, since only a 'supreme national court' (the court of the last resort) can seek such a ruling[126]. It has been indicated that the concept of trust among Member States is especially important in this regard to prevent rewarding those who win the "race to the courthouse" [127]. In any case, thought should be given to the issue of resolution of jurisdictional disputes when considering a global approach, taking into account the need for quick responses in the insolvency context and the need to prevent forum shopping[128].

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[122] Articles 16-26 of the EU Regulation (note 75 above).

[123] See I.F.Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL, Cross-Border Insolvency, 15, 39. However, recognition outside the community depends on the laws of each relevant country and especially whether the relevant country adopted the Model Law (on the Model Law see section 2.4.4 below).

[124] Article 26 of the EU Regulation (note 75 above). See also Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397, at paras 60-68 (stating that the fundamental right to be heard falls under the public policy exception); I.F.Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL, Cross-Border Insolvency, 15, 40.

[125] See *Id.*, p. 38-39.

[126] See Article 68 of the Consolidated EC Treaty (formerly Article 73p ECT). This is due to the fact that the convention has been converted into a Regulation, adopted under Title IV of the EC Treaty. It means that this will be time consuming and costly (see I.F. Fletcher, "The Challenge of Change: First Experiences of Life under the EC Regulation on Insolvency proceedings in the UK", Annual Review of Insolvency Law, 2003 (Toronto, Carswell, 2004), 431, 436-437; Fletcher, Insolvency (note 4 above), p. 438-439).

[127] See Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397, at paras. 39-44; Fletcher, Insolvency (note 4 above), p. 371-372; Bob Wessels, "International Jurisdiction to Open Insolvency Proceedings in Europe, In Particular Against (Groups of) Companies" Working Papers Series, Institute for Law and Finance, Johann Wolfgang Goethe University (http://www.iiiglobal.org/country/european_union/InternJurisdictionCompanies.pdf), p. 14-18.

[128] See *infra* chapter 6 section 6.1 on the issue of forum shopping and *infra* chapter 7 on determining the proper venue for the MCG insolvency case.

Another major step taken within the Regulation to promote unity is with respect to the issue of the law that will govern the international insolvency process. Although, the Regulation does not attempt to harmonize the national systems of insolvency law, it does provide a uniform set of choice of law rules[129]. The basic rule is that the law governing most of the issues (both substance and procedure) pertaining to the insolvency is the law of the state in which the proceedings are opened[130]. This rule is subject to a set of exceptions, where a particular issue may be governed by a law other than that of the state of the opening of proceedings, through the application of a special choice of law rule to the specific facts of the case[131].

The Regulation aims to ensure equal treatment to all creditors throughout the Community[132]. In order to overcome the disadvantageous situation of foreign creditors, it requires taking immediate steps to inform them about the opening of insolvency proceedings including notification of related issues such as time limits and information regarding the lodgement of claims[133]. Foreign creditors are also entitled to lodge claims in the insolvency proceedings[134].

In sum, recognizing that national assistance is not enough and cross-border insolvency should be regulated on community level, the Regulation enables close coordination of international insolvencies falling within its scope. Essentially, this is achieved by providing rules of international jurisdiction (using the concepts of 'main' and 'secondary' proceedings) and unified choice of law rules coupled with rules for automatic recognition within Member States.

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[129] In Articles 4-15.
[130] Article 4 of the EU Regulation (note 75 above).
[131] Articles 5-15 of the EU Regulation (note 75 above). See also I.F.Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL, Cross-Border Insolvency, 15, 31-38; Also see Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, footnote 122 in p. 34 (Prof Westbrook expresses the opinion that some of the exceptions are large ones (e.g., for secured creditors) and seem regrettable).
[132] See Articles 39-42 of the EU Regulation (note 75 above). See also Fletcher, Insolvency (note 4 above), p. 41-43.
[133] Article 40 of the EU Regulation (note 75 above).
[134] Article 39 of the EU Regulation (note 75 above); Cf. the position of the Model Law (or lack of position) on this matter (Note 175 below).

2.4.3.3. Application (of the EU Regulation) to groups of companies

Most important for our purposes, the Regulation does not contain provisions to deal with the issue of corporate groups. This was expressly indicated in the Report Virgos-Schmidt (1996)[135]. Namely, courts should identify the COMI of the debtor, notwithstanding its relationship with other affiliated companies, as the basis for ascertaining jurisdiction. Similarly, territorial proceedings can be opened where the debtor has an 'establishment' by way of local operations or a branch, but not a subsidiary company. Indeed, the English High Court in the case of *Telia v. Hillcourt*[136] rejected the submission that the business premises of a subsidiary company could rank as an 'establishment' of the parent for the purposes of Article 3(2) of the EU Regulation. The reason for this judgment was apparently based on the notion that the separate personality of the subsidiary must be respected[137].

Although several pan-European restructurings have been successfully coordinated via placing all affiliated companies' proceedings under a single forum and single law, this was only possible where COMI was found in that jurisdiction for each company separately[138].

This approach was reaffirmed by the preliminary opinion given by an Advocate General attached to the ECJ in the case of *Eurofood*[139]. The advocate general asserted that the Regulation applies to individual companies and not to corporate groups, and that it does not regulate the relationship between parent and subsidiary companies. Accordingly, the COMI concept refers to single companies, and nothing can necessarily be inferred in this regard from the fact that a debtor company is a

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[135] The report indicates in Paragraph nr. 76 that "The Convention offers no rule for groups of affiliated companies (parent-subsidiary schemes). The general rule to open or to consolidate insolvency proceedings against any of the related companies as a principal or jointly liable debtor is that jurisdiction must exist according to the Convention for each of the concerned debtors with a separate legal entity. Naturally, the drawing of a European norm on associated companies may affect this answer".

[136] Telia Soneria AB v. Hilcourt "Docklands" Ltd. [2003] B.C.C. 856 (Ch).

[137] In the case, a creditor threatened to pursue winding up proceedings against a Swedish company (a company whose registered office and centre of main interests was in Sweden) in the UK on the grounds that it had a subsidiary in the UK. The judge posited that, winding up proceedings directed at Telia can only be brought in Sweden and that the courts of England and Wales have no jurisdiction (*Id.*); See also Bob Wessels, "International Jurisdiction to Open Insolvency Proceedings in Europe, In Particular Against (Groups of) Companies" Working Papers Series, Institute for Law and Finance, Johann Wolfgang Goethe University, http://www.iiiglobal.org/country/european_union/InternJurisdictionCompanies.pdf.), p. 19; Fletcher, Insolvency (note 4 above), p. 379.

[138] See examples provided in *infra* chapter 4 section 4.1.3.7.

[139] Eurofood IFSC Ltd (C- 341/04) [2005] B.C.C. 1021 (AGO).

subsidiary of another company. Each subsidiary within a group must be considered individually[140]. The ECJ upheld this opinion reinforcing the approach expressed by the Advocate General in respect to corporate groups. Though the court has not disqualified 'parental control' over a subsidiary as a relevant factor in determining the proper jurisdiction, the focus was on the whereabouts of the registered office and operations of the particular subsidiary[141]. Apparently, this takes the EU Regulation a step back in their potential applicability to the corporate group case, at least in preventing an 'implicit' use of the COMI notion in MCG cases (in particular the possibility to de facto apply joint administration of group proceedings grounding the decision on 'group considerations'[142]).

2.4.4 UNCITRAL Model Law[143]

2.4.4.1. The conceptual approach

The model law is the most significant scheme for regulating cross- border insolvencies currently at hand in terms of the potential breadth of its application. It is an international initiative (rather than regional), targeted at every country that wishes to embrace it[144].

On the other hand, it is less 'pretentious' in the means and mechanisms it provides and more modest in its goals (compared to the EU Regulation[145]). It appreciates that it is unrealistic for the short to medium term to have a wide global regime that includes substantive law rules and that attempts to be fully uniformly and consistently applied in nation states[146].

Thus, though similarly designed to facilitate the governance of cross-border insolvencies, it deliberately refrains from including rules of direct jurisdiction or

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[140] *Id.*, paras 106-126.
[141] Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397, at paras. 26-37.
[142] See further *infra* chapter 4 secton 4.1.3.8 and *infra* chapter 5 section 5.1.
[143] U.N. Comm'n on Int'l Trade Law (UNCITRAL), UNCITRAL Model Law on Cross-Border Insolvency with Guide to enactment, U.N. Sales No. E.99.V.3 (http://www.uncitral.org/pdf/english/texts/insolven/insolvency-e.pdf) [hereinafter: Model Law or UNCITRAL Model Law interchangeably].
[144] It was adopted unilaterally by UNCITRAL in May 1997 (for the history and evolution of the Model Law see Fletcher, Insolvency (note 4 above), p. 446-452; R. W.Harmer, "Documentation B, UNCITRAL Model Law on Cross-Border Insolvency" [1997] 6 Int. Insolv. Rev., 145, 146-147).
[145] See section 2.4.3.1 above.
[146] See Fletcher, Insolvency (note 4 above), p. 443-446.

choice of law[147]. It merely aims at providing a system of cooperation among the courts having jurisdiction over aspects of the assets and affairs of the international debtor company[148].

Designed as a set of model legislative provisions rather than an international treaty (or other sort of supranational legislation[149]), the Model Law is also not binding. The ultimate form of legislation which could result from the Model Law is left to each country. Thus, it has the merit of being acceptable on a widening circle of states. Yet it is also prone to the danger of passivity, and lack of uniformity in application of the rules[150]. Currently, however, a wide adoption of the Model Law looks in reach, as a number of countries (some of which commercially important) already adopted the model law or are in the process of adopting it[151]; most significantly it was recently embraced within the bankruptcy laws of the US[152] and the UK[153]. On the other hand, enactment is not always faithful to the terms provided in the model law which can then diminish its practical value[154].

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[147] Cf. the provisions of the EU Regulation (in section 2.4.3.2 above).

[148] See Fletcher, Insolvency (note 4 above), p. 497-498 (asserting that the Model Law reflects the 'art of the possible' and offers the best prospects of formulating a global framework for international cooperation in cross-border-insolvencies). See also I.F.Fletcher, *The Law of Insolvency* (3rd Edn. 2002) [hereinafter: Fletcher, The Law of Insolvency] p. 862; Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2279-2280 (asserting that in many civil law countries, its adoption will provide an essential legislative direction permitting courts to cooperate with courts in other countries to manage cross border insolvencies. In most adopting countries it is likely to make cooperation in reorganization cases much easier, while frustrating efforts to engage in manipulation of assets and other fraudulent activity).

[149] Such as the EU Regulation (see section 2.4.3.1 above).

[150] See Fletcher, Insolvency (note 4 above), p. 445; R. W .Harmer, "Documentation B, UNCITRAL Model Law on Cross-Border Insolvency" [1997] 6 Int. Insolv. Rev., 145, 152; Rajak, Company Liquidations (note 110 above), p. 360.

[151] For the current statues of the enactment of the Model Law see http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency/1997Model_status.html.

[152] With the entry into force of the new chapter 15. It is predicted that now that the US has adopted the Model Law, many of its trading partners will follow suit (see *GLOBALTURNAROUND,* "Canada follows US with insolvency reform", December 2005, issue 71, p. 1).

[153] SI 2006/1030 (http://www.opsi.gov.uk/si/si2006/20061030.htm). On the enactment of the Model Law in Great Britain see: I.F. Fletcher, "Better late than never: the UNCITRAL Model Law enters into force in Great Britain" [2006] Insolv. Int., forthcoming.

[154] For instance, certain countries included a 'reciprocity condition', namely that reciprocity must be shown on the part of the foreign state in which the insolvency proceedings have opened. See the way the Model Law has been enacted in the laws of Mexico and South Africa as described in Fletcher, Insolvency (note 4 above), p. 489-490. In terms of uniformity, Japan's version of the Model law is regarded as the least uniform of those adopted so far (see Fletcher, Insolvency (note 4 above), p. 490; Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 24).

The model law will also have great effect if adopted within groupings of states (that may already be a party of regional cross- border insolvency models)[155], thus ensuring a high level of cooperation among those countries and the rest of the world[156].

As will be elaborated herewith, the model law aims to help with three main issues: access to foreign courts; recognition of foreign insolvency proceedings; and relief to protect assets in foreign jurisdictions. It also encourages cooperation between courts and endeavours to provide for co-ordination if there were two or more proceedings in respect of the same debtor. It is 'universalistic' in that it attempts to harmonize and unify systems in their approaches to cross border insolvency[157], although it is confined to basic provisions and does not attempt anything too ambitious[158]. The 'modification' of universalism is demonstrated here in that local proceedings may be opened under the model, either in full parallel, or as an ancillary process[159].

The Model Law is heavily influenced by the EU Regulation and follows its lead in many respects. Mainly, it adopts the notions of 'COMI' (with the presumption accompanying it) and 'establishment' used in the Regulation[160], for the purpose of recognition, relief and concurrent proceedings[161].

2.4.4.2. Key provisions

The Model Law facilitates access to a foreign insolvency proceeding, both for a foreign representative and foreign creditors[162]. Essentially, it aims to remove or at

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[155] Such as the EU countries, or the NAFTA countries.

[156] See Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 3-4, 38-41.

[157] See the text of the decision of UNCITRAL to adopt the Model Law (at the 630th meeting on 30 May 1997) (in Fletcher, Insolvency (note 4 above), p. 450-415). See also Article 8 of the Model Law (note 143 above) that urges the courts in the adopting state to seek uniformity with other adopting states in the interpretation of the law.

[158] See R. W.Harmer, "Documentation B, UNCITRAL Model Law on Cross-Border Insolvency" [1997] 6 Int. Insolv. Rev., 145, 146-147.

[159] See chapter IV and V of the Model Law (note 143 above). See also Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 17.

[160] See section 2.4.3.2 above. The definition of 'establishment' has one addition in the Model Law version (extending the definition to include the words 'or services') (see Artcile 2(f) of the Model Law, note 143 above).

[161] See the definitions of "foreign main proceeding" and "foreign non-main proceeding" in Article 2 of the Model Law (*Id.*).

[162] Articles 9-14 of the Model Law (*Id.*).

least lessen the barriers to jurisdiction and standing[163]. It also includes the obligation to give notification to foreign creditors whenever notification is to be given to creditors under local laws[164].

The main contribution of the Model Law is the relatively simple, fast and inexpensive procedure for the recognition of foreign insolvency proceedings, and the further assistance and relief provided to the foreign representative in the foreign jurisdiction[165]. For this purpose, the Model Law provides a set of conditions and presumptions to facilitate the recognition procedure[166]. This involves the identification of the foreign proceedings either as 'main' or 'non main' (the definitions imported from the EU Regulation[167]), and presentation of formal certificates. Then if the criteria are met there is a mandate for recognition.

The relief provisions are graduated according to time, and aimed to protect the assets and business interests of the debtor. They are provided by the local court (granting recognition) according to local laws. Urgent interim-type relief are available for the time of filing an application for recognition until the application is decided upon[168]. Most importantly, the model law enables automatic relief upon recognition of a foreign main proceeding[169]. This basic automatic assistance is designed to give some certainty of effect to an application for recognition of a 'main' proceeding and is, therefore, consistent and collateral to the main intent of the Model Law[170]. Indeed, relief of this sort was recently granted by courts of enacting states[171]. Subsequent to recognition, either as foreign main or non main proceedings, there is additional relief that may be granted upon the request of the foreign representatives[172].

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[163] See R. W. Harmer, "Documentation B, UNCITRAL Model Law on Cross-Border Insolvency" [1997] 6 Int. Insolv. Rev., 145, 149.
[164] Article 14 of the Model Law (note 143 above).
[165] Articles 15-23 of the Model Law (*Id.*). See also R. W. Harmer, "Documentation B, UNCITRAL Model Law on Cross-Border Insolvency" [1997] 6 Int. Insolv. Rev., 145, 149-150,
[166] Articles 16 and 17 of the Model Law (note 143 above).
[167] Notes 160-161 above, and accompanying text.
[168] Article 19 of the Model Law (note 143 above).
[169] Article 20 of the Model Law (*Id.*). It is 'semi-automatic' since it is granted only upon recognition.
[170] See R. W. Harmer, "Documentation B, UNCITRAL Model Law on Cross-Border Insolvency" [1997] 6 Int. Insolv. Rev., 145, 150.
[171] See e.g., the MMA insolvency case (La Mutuelle du Mans Assurances IARD (MMA) (chapter 15 No.: 05-60100 (BRL) (Bankr. S.D.N.Y, 2005) in which the company (a marine insurance business) successfully filed for chapter 15 protection in front of Judge Burton R. Liefland in the bankruptcy court for the Southern District of New York. The US court recognized the foreign proceeding as foreign main proceeding thereby entitling the foreign representative to a stay under US Bankruptcy Code section 362 (the 'automatic stay').
[172] Article 21 of the Model Law (note 143 above).

Yet, it has been noted that it is an anomaly that the scheme does not impose a broader stay than that available under the domestic law of a given country. This stay does not restrain the bringing of lawsuits for the sole purpose of preventing termination of rights nor the initiation of a local insolvency proceeding. On the contrary, the stay may be modified or terminated as a result of the opening of a local proceeding involving the same debtor[173].

Although the Model Law generally invokes for equal treatment to foreign creditors[174], it is silent on the issue of treatment of foreign creditors with respect to distribution preferences. Here too The Model Law leaves the matter to local laws, which may pose another threat to full international cooperation[175].

Commonly regarded as the main novelty of the Model Law are its provisions concerning cooperation among courts and representatives[176]. Indeed, the Model Law explicitly directs the courts involved in an international insolvency process to co-operate 'to the maximum extent possible', including by way of direct communication, a notion that is regarded as new and even strange for many countries[177]. This again exemplifies the universalist approach taken by the Model Law in demanding maximum cooperation in order to reach a conclusion as close as possible to the ideal of single court, single law resolution[178]. The Model Law envisages situations where proceedings related to the same debtor are taking place in foreign countries in any possible version (in parallel or as an ancillary process, ordinary lawsuits or combinations of the above) and authorizes the courts involved (and also the foreign

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[173] Article 28 of the Model Law (*Id.*). See Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 17.

[174] Foreign creditors have the same rights regarding the commencement of, and participation in, the insolvency proceedings (Article 13(1) of the Model Law, note 143 above). Foreign creditors should also be given notification with respect to the insolvency process in the same way it is given to local creditors (Article 14 of the Model Law (*Id*)).

[175] See Article 13(2) of the Model Law (*Id.*). See also Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 16.

[176] See Fletcher, Insolvency (note 4 above), p. 480. See also Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 16-17; R. W. Harmer, "Documentation B, UNCITRAL Model Law on Cross-Border Insolvency" [1997] 6 Int. Insolv. Rev., 145, 150-151.

[177] Article 25 of the Model Law (note 143 above). See also section 2.4.2 above; Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 17.

[178] See section 2.2 above.

representatives[179]) to cooperate. It further provides for the manner or methods by which co-operation may be most appropriately applied, including the use of Protocols[180].

The Model Law accommodates the whole spectrum of 'modification' of the unified approach underlying the models for cross-border insolvencies. Accordingly, it acknowledges the fact that under the scheme it provides, more than one full insolvency proceeding may be opened against the same debtor, possibly causing problems of conflicts between the concurrent proceedings which may compete with one another for attention, position, priority and effect. To deal with this problem, it provides rules for promoting coordination and reducing these conflicts[181]. Thus, it directs courts to ensure consistency in the relief they grant and to seek cooperation and coordination with the other jurisdictions in which concurrent proceedings are taking place[182].

As mentioned above, the model law does not contain choice of law rules to be applied uniformly[183]. Instead of introducing provisions concerning applicable law, it leaves the matter to domestic laws. Accordingly, local courts will apply their own national private international laws on the matter at hand. Therefore, as mentioned above, stay of proceedings and other relief will be granted by the country recognizing the foreign proceeding according to its local laws, rather than applying the foreign remedies locally.

In sum, the Model Law provides a modest baseline enabling international cooperation on a worldwide scale, as long as a substantial number of countries will opt to adopt it in a uniform manner. The main procedural advantages it provides are based on the recognition of the foreign proceedings within local jurisdictions, using the notions of main and non main proceedings consistently following the EU Regulation ideas in this regard.

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[179] Article 26 of the Model Law (note 143 above).
[180] Article 27 of the Model Law (*Id.*). See section 2.4.2 above on ad hoc means for cooperation and coordination.
[181] Articles 28-32 of the Model Law (note 143 above). See also R. W. Harmer, "Documentation B, UNCITRAL Model Law on Cross-Border Insolvency" [1997] 6 Int. Insolv. Rev., 145, 151.
[182] *Id.* It also includes the 'Hotchpot' rule of distribution, available in the EU Regulation too (see note 115 above).
[183] Section 2.4.4.1 above.

2.4.4.3. Application to group of companies

Similarly to the EU Regulations the Model Law does not deal explicitly with the issue of corporate groups[184]. Rather, it deals with debtor companies that their insolvency involves international elements, or even full insolvency proceedings taking place in more than one jurisdiction (regarding the same single debtor)[185].

The foreign representative, a concept recognized under the Model Law[186], is the person authorised in a foreign proceeding to administer the reorganization or the liquidation of a debtor's assets or affairs[187]. Recognition is then given to the foreign proceedings with the subsequent relief that may be granted with regard to the debtor's local assets or local proceedings[188]. Yet, the Model Law does not give authorization to recognize foreign proceedings of affiliated companies and accordingly does not grant relief with regard to companies related to the debtor. This is also the case with regard to cooperation and co-ordination. These mechanisms refer to proceedings taking place for a single debtor, not to two or more proceedings taking place against different separate entities (belonging to a multinational corporate group).

2.4.5 The ALI Principles[189]

2.4.5.1. The conceptual approach

Another major initiative essentially designed for use among the countries belonging to NAFTA[190] is the ALI Principles .Thus, like the EU Regulation it is a regional solution[191].

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184 However, following exchange of views and information provided in a colloquium held by UNCITRAL (Vienna, 14-16 November, 2005), the secretariat of UNCITRAL has recently proposed that the topic of corporate groups will be referred to a working group for consideration (see United Nations (2006), A/CN.9/596, Insolvency law: possible future work, Note by the Secretariat http://daccessdds.un.org/doc/UNDOC/GEN/V06/517/90/PDF/V0651790.pdf?OpenElement).

185 See the scope of application and the definition of foreign proceeding (Articles 1 and 2 of the Model Law, note 143 above).

186 Section 2.4.4.2 above.

187 See Article 2(d) of the Model Law (note 143 above).

188 Section 2.4.4.2 above.

189 The American Law Institute, *Transnational Insolvency: Cooperation among the NAFTA Countries* [2003] [hereinafter: Principles or ALI Principles, interchangeably].

190 North American Free Trade Agreement. Namely, Canada, Mexico and the U.S.A.

191 However, a new initiative of the ALI in collaboration with the International Insolvency Institute is aimed at evaluating the possibility of adapting the Principles so as to provide a standard statement of principles suitable for application on a global basis in international insolvency cases (Prof. I.F.Fletcher and Prof. B.Wessels were appointed by the International Insolvency Institute as Reporters of the project, approved by the Institute's Council in December 2005).

Unlike the EU Regulation, the ALI Principles are merely unofficial best practice recommendations[192], developed by the private sector[193]. It has been observed that they are heavily reliant upon judicial initiative thus rendering the result of its use somewhat uneven and unpredictable[194]. The Principles were designed in order to achieve closer integration and cooperation in the insolvencies of multinational companies within NAFTA, understanding that such development is essential to full realization of the free flow of investment contemplated by the NAFTA[195].

In its rationale the ALI Principles attempt to include rules that reflect common grounds among the countries involved, rather than recommending more ambitious broader mechanisms[196]. Using the Principles should also facilitate developing the protocol approach, which as was mentioned above, is becoming a common tool for facilitating cross-border insolvencies taking place in North America[197]. However, the Principles expressly disclaim any attempt to adopt choice of law rules[198], the choice of ancillary versus parallel systems[199], and priorities in distribution. It focuses solely on the process of cooperation rather than substantive outcomes[200].

The Principles are supported by intensive comparative studies of the three NAFTA countries' law and practice in insolvency matters, so that they promote predictability and facilitate cooperation among these countries[201]. The Principles were also designed

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[192] Whereas the EU Regulation is positive binding law (see section 2.4.3.1 above).
[193] The ALI (American Law Institute) is a private-sector law reform organization.
[194] See Fletcher, Insolvency (note 4 above), p. 444.
[195] See Jay Lawrence Westbrook and Jacob S. Ziegel, "NAFTA Insolvency Project" 23 Brook. J. Int'l L. (1997-1998), p. 7; Jay Lawrence Westbrook, "Managing Defaulting Multinationals Within NAFTA" in I.F.Fletcher, L. Mistelis, M. Cremona (eds.), *Foundations and perspectives of International Trade Law* (Sweet & Maxwell, 2001), 465, 466; Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 30.
[196] Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 32.
[197] See section 2.4.2 above. See also Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 33, 41.
[198] See ALI Principles (note 189 above), at section II, Topic D, Subtopic 2; Cf. the EU Regulation approach (section 2.4.3.2 above).
[199] Cf. the EU Regulation's 'secondary proceeding' approach (section 2.4.3.2 above). See also Jay Lawrence Westbrook, "Managing Defaulting Multinationals Within NAFTA" in I.F.Fletcher, L. Mistelis, M. Cremona (eds.), *Foundations and perspectives of International Trade Law* (Sweet & Maxwell, 2001), p. 465, 468, 470, 475 (the ALI Principles reflect some preference for an ancillary system).
[200] Jay Lawrence Westbrook, "Managing Defaulting Multinationals Within NAFTA" in I.F.Fletcher, L. Mistelis, M. Cremona (eds.), *Foundations and perspectives of International Trade Law* (Sweet & Maxwell, 2001), p. 465, 468; Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 34.
[201] *Id.*, p. 31.

with UNCITRAL Model Law[202] in mind. Thus, they should be able to work in harmony with it (and therefore, include an express recommendation for the adoption of the Model Law by the countries concerned[203]). In addition, they follow both the EU Regulation and the Model Law in the adoption of the 'main' insolvency proceedings concept and the 'COMI' test of the EU Regulation[204].

The Principles implement a modified universalist approach with the goal of achieving a solution as close as possible to what would have been achieved under a single transnational proceeding. It is thus committed to full cooperation, under the current situation where the laws of the countries involved still differ[205]. Although the Principles accommodate both the ancillary and the parallel approaches they encourage deference to the 'main' proceeding[206].

2.4.5.2. Key provisions

Like the Model Law scheme, under the ALI Principles, recognition is the central legal action. Recognition is not automatic but rather a procedure that should be sought in each relevant country[207]. Similarly, the effects of recognition (the relief available) are not immediate. Yet, once a 'main' insolvency proceeding is recognized, a broad moratorium can follow quickly[208].

Such relief actions (and powers given to foreign representatives) are granted by the local court imposing national laws and national remedies. It is once again an approach

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[202] See section 2.4.4 above. See also I.F. Fletcher, "The Challenge of Change: First Experiences of Life under the EC Regulation on Insolvency proceedings in the UK", Annual Review of Insolvency Law, 2003 (Toronto, Carswell, 2004), 431, 442.

[203] Indeed, Mexico and the U.S. have already adopted the Model Law. The new Canadian bill embracing the Model Law is about to come into force (*GLOBALTURNAROUND,* "Canada follows US with insolvency reform", December 2005, issue 71, p. 1; see also note 151 above).

[204] See section 2.4.3.2 above.

[205] Jay Lawrence Westbrook, "Managing Defaulting Multinationals Within NAFTA" in I.F.Fletcher, L. Mistelis, M. Cremona (eds.), *Foundations and perspectives of International Trade Law* (Sweet & Maxwell, 2001), p. 465, 468-469; Fletcher, Insolvency (note 4 above), p. 303-304; Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2299-2303.

[206] Jay Lawrence Westbrook, "Managing Defaulting Multinationals Within NAFTA" in I.F.Fletcher, L. Mistelis, M. Cremona (eds.), *Foundations and perspectives of International Trade Law* (Sweet & Maxwell, 2001), p. 465, 470; Fletcher, Insolvency (note 4 above), p. 305.

[207] ALI Principles (note 189 above), General Principle II, and Procedural Principles 1. Cf. the EU Regulation's approach (section 2.4.3.2 above).

[208] ALI Principles (note 189 above), Procedural Principles 1, 2, 4. The same approach was adopted in the Model Law (see section 2.4.2.2 above); See also Jay Lawrence Westbrook, "Managing Defaulting Multinationals Within NAFTA" in I.F.Fletcher, L. Mistelis, M. Cremona (eds.), *Foundations and perspectives of International Trade Law* (Sweet & Maxwell, 2001), p. 465, 471-472; Fletcher, Insolvency (note 4 above), p. 307.

similar to the one adopted within the Model Law[209], and different from the EU Regulation, as the latter makes universal the effects of the moratorium imposed by the law of the main proceedings[210]. Recognition also enables access to the local courts and to information on the debtor, and similarly requires the foreign representative to disclose relevant information[211].

In the attempt to maximize cooperation and achieve unity, the Principles urge that a recognized foreign representative will be granted control over local assets and that assets be permitted to be transferred out of a jurisdiction when that is appropriate[212]. The Principles also adopt the concept of sharing of value[213]. That is, the notion of a worldwide perspective on the distribution of assets, urging the courts to determine distributions from a universalist perspective, and expressly contemplating the possibility of dismissing one or more full insolvency proceedings. This way a reorganization plan can be adopted in the main proceeding without the complications created by detailed differences in priority rules[214]. The Principles further facilitate the universal enforcement of an approved reorganization plan[215].

The Principles comprehensively deal with the issue of communication among administrators and courts[216]. They strongly encourage such communication and contain a set of guidelines to facilitate this device[217]. They also contain exemplary Protocols to facilitate cooperation in the way of agreements negotiated between the

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[209] See section 2.4.2.2 above.

[210] See section 2.4.3.2 above; See also Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 34.

[211] ALI Principles (note 189 above), General Principle IV, and Procedural Principles 7-9.

[212] *Id.*, Procedural Principles 11 and 12.

[213] *Id.*, General Principle V.

[214] See Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 35.

[215] ALI Principles (note 189 above), Procedural Principles 26 and 27.

[216] Conversely, the EU Regulation is silent on the subject of communication between courts; The Model Law authorizes direct communication between courts and foreign representatives (see section 2.4.2.2 above).

[217] See ALI Principles (note 189 above), Procedural Principles 14 and 15; The American Law Institute, Transnational Insolvency: Cooperation among the NAFTA Countries, Principles of Cooperation Among the NAFTA Countries, Guidelines Applicable to Court-to-Court Communication in Cross-Border Cases (www.ali.org) [hereinafter referred to as "ALI Guidelines for Communication"]. The ALI in collaboration with the International Insolvency Institute are developing the ALI Guidelines for use in various regions of the world (see Institute's Guidelines for Court-to-Court Communication Gain International Approval, ALI Rep., Fall 2002, at 18; See also Jay Lawrence Westbrook, "International Judicial Negotiations" [2003] 38 Tex. Int'l L.J. 567, 581).

parties[218]. Various provisions aim at facilitating parallel insolvency proceedings, including the cross border sales of assets[219].

2.4.5.3. Application to corporate groups

Unlike the previous models discussed above[220], the ALI Principles deal with the case of MCGs to a certain extent[221] .

Recognizing the fact that international corporate group in insolvency is a complex issue which is to some extent belongs to corporate law, the Principles bound their scope to a limited number of legal issues, refraining from any attempt to deal with substantive issues, such as group liability[222].

The Principles focus on facilitating the administration of affiliated companies' insolvency proceedings[223]. They provide that insolvency proceeding against a subsidiary company can be filed in the parent company's home country (unless there is an existing proceeding involving the subsidiary in the country of its main interests)[224]. This enables consolidation of the proceedings of the subsidiary and the parent, either procedurally or substantially, under the applicable law[225].

As aforesaid, the Principles do not contain choice of law rules[226], and this applies to matters pertaining to MCGs as well. Furthermore, the Principles do not contain rules to determine on the proper jurisdiction for the corporate group consolidated process,

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[218] Appendix 3 of the ALI Principles (note 189 above); See also, Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 37.

[219] ALI Principles (note 189 above), Procedural Principles 14-22.

[220] The EU Regulation (section 2.4.3.3 above) and the Model Law (section 2.4.2.3 above).

[221] See Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 38 (explaining that the Principles "put a toe in the water" on this difficult problem). See also Fletcher, Insolvency (note 4 above), p. 311 (the Principles offer "a tentative guidance on the approach to be followed").

[222] American Law Institute, *Transnational Insolvency: Cooperation Among the NAFTA Countries* (2003), p. 77. See also Jay Lawrence Westbrook,, "Managing Defaulting Multinationals Within NAFTA" in I.F.Fletcher, L. Mistelis, M. Cremona (eds.), *Foundations and perspectives of International Trade Law* (Sweet & Maxwell, 2001), p. 465, 474. The issue of Group liability will be discussed in *infra* chapter 5 section 5.2.4.

[223] The Principles do not provide what will constitute an affiliate (or a corporate group) for the purpose of this approach (see on the issue of defining the multinational corporate group in *supra* chapter 1 section 1.3).

[224] ALI Principles (note 189 above) Procedural Principle 23.

[225] *Id.*

[226] Section 2.4.5.1 above.

they merely allow filing in the parent's jurisdiction, though this place does not necessarily reflect the centre of main interests of the group as a whole[227].

The Principles further enable cooperation and coordination between affiliated insolvency proceedings where a parallel process is taking place[228]. They do not provide when a parallel process will be appropriate as opposed to proceedings opened at the same country (for all affiliates involved), rather they urge maximum cooperation (to achieve the benefits of consolidation where possible) in the case this is the scenario at hand[229]. Finally, the Principles desire to maintain the concept of the corporate separate personality and accordingly urge to limit the effect of consolidation to reflect the fact that different claimants have rights against different entities[230].

2.5 Summary

It seems clear that in the dispute between territorialism and universalism the latter prevails, at least as it is reflected in practice (namely, in existing cross-border insolvency models) and in the academic literature[231]. Although current models basically adopt 'modified' universalism, it appears that the aspiration is for maximum cooperation. For this purpose, the models delineated embrace various different mechanisms. While certain models are more ambitious in the tools they provide, others can be broader in scope[232]. Anyhow, the question is whether this approach sustains the case of the MCG with its particular complexities.

Further to justifying a universalist approach to the MCG insolvency case, the particular adequate mechanisms will need to be discussed, as current models, for the most part, have only just begun to address the issue, and only in a limited scope. Nonetheless, existing tools available for single debtors could be used, perhaps with modifications, if prove needed. In subsequent chapters we will begin treading along the path towards finding the right ways to tackle this particular case.

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[227] On the issue of the proper jurisdiction for the MCG case see *infra* chapter 7.

[228] ALI Principles (note 189 above), Procedural Principle 24.

[229] See *infra* chapter 4 section 4.1.3.6-4.1.3.8 for a 'centralized approach' proposed for MCG's insolvencies. See also *infra* chapter 7 for the issue of proper jurisdiction.

[230] ALI Principles (note 189 above), Procedural Principle 24, and in p. 80 (explaining that "the key point is respect for the corporate form"); Jay Lawrence Westbrook, "Multinational Enterprises in General Default: Chapter 15, The ALI Principles, and The EU Insolvency Regulation" [2002] 76 Am. Bankr. L.J. 1, 38; Fletcher, Insolvency (note 4 above), p. 312. See further on the battle between the 'corporate form' notion and a global approach in *infra* chapter 3 section 3.2. On creditors' rights in the course of the MCG insolvency case see *infra* chapter 5.

[231] See section 2.2 above.

[232] Cf. the EU Regualtion with the Model Law (sections 2.4.3 and 2.4.4 respectively).

Chapter 3

The road to a suitable global approach: answering key insolvency goals while balancing between contradicting concepts

3.1 Introduction

The main body of this study provided in the next chapters[1] will assess the actual need for a global approach to MCG insolvencies and the possible damage applying such an approach entails. The variety of circumstances and scenarios of MCGs' insolvencies and the conflicting policies and goals relevant in these cases will be discussed. We will therefore be in good position to clarify the necessity of a global approach while establishing its preferred characteristics.

This chapter commences the path towards assessing and devising a workable solution for insolvencies within MCGs. It first presents the additional 'battle' between contradicting goals, particularly relevant to the case of corporate groups[2]. That is, between the need to respect the corporate form and the attempt to link between affiliates in their insolvency. The idea that will be proposed is to 'proceed with caution' when suggesting (in subsequent chapters) global means, thus reconciling between the two important objectives. Furthermore, linking mechanisms could be devised via using available tools that already exist in certain legal regime, while applying certain refinements or additional features to them so as to increase their universal compatibility and adequateness to the international scenario.

Consequently, the chapter will proceed to suggest and set forth the key factors pertaining to the administration of MCG's insolvency. In light of these factors, subsequent chapters will consider whether unified proceedings for related companies would be advantageous and whether there would be circumstances in which the corporate form should be ignored in the context of the insolvency proceedings.

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[1] *Infra* chapters 4-7.

[2] The first 'battle' was between a universalist and a territorialist approach, the two main contradicting theories to international insolvency in general (see *supra* chapter 2 section 2.2).

3.2 The 'battle' between a global approach and the need to respect the corporate entity

In the locus of the entire quest for a principled global approach stands a "battle" between the desire to find ways of connecting between the components of a global group and in certain cases even dismantling the walls or 'piercing the veil' (for the purpose of benefiting the international insolvency process and promoting the reliability of the international insolvency system)[3] and the obvious demands on behalf of traditional corporate theory that the integrity and distinctiveness of the corporate form be respected[4]. This conflict is augmented by the fact that in these sorts of cases the enterprise is one of a worldwide nature with components operating within the borders of different states.

As of today national laws differ in the extent to which they adhere to entity law. Different countries use different circumstances to justify 'lifting' the corporate 'veil' or operating other doctrines and concepts (such as 'enterprise law'[5]) for the purpose of imposing group liability or interconnecting separate entities in the course of their insolvency[6].

Hence, a global approach entails a 'double interference' difficulty- a clash with the corporate entity and a clash with the country's (within which it operates) sovereignty and legal policy.

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[3] The benefits from such approach will be discussed in the subsequent chapters (*infra* chapters 4-6).

[4] See note 8 below. The application of a global approach over those MCGs linked via contracts (see *supra* chapter 1 section 1.3) will present an equivalent question (of that related to equity based groups). That is whether a 'contractual veil' between the contracting parties should be lifted for various reasons pertaining to the insolvency (on contractual network enterprises see G. Teubner, "The many-headed Hydra: networks as higher order collective actors" in *Corporate Control and Accountability* (J. McCahery, S. Picciotto and C. Scott, eds., 1993); G. Teubner, "Unitas multiplex: corporate Governance in group enterprises" in *Regulating Corporate Groups in Europe* 67, 87-92 (D. Sugarman and G. Teubner eds., 1990); G. Teubner *Law as an Autopoietic System* (Oxford, Blackwell Publishers, 1993); Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), chap. 9, p. 328-330).

[5] See note 3 in the Introduction chapter. See also Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 695; P.T. Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), p. 328.

[6] See, for instance, the methods provided in New Zealand's Companies Act 1993, and the mechanisms of procedural and substantive consolidation and subordination available under the US bankruptcy regime, and on the other hand the more strict application of the entity doctrine under English legal regime (*infra* chapter 4 sections 4.1.3.3 and 4.3.4; *infra* chapter 5 sections 5.2.4.2 and 5.2.4.4). See also generally on domestic laws and the lack of a clear approach within the insolvency field regarding limited liability in Phillip I. Blumberg, The law of corporate groups: substantive law (1987, supp. 1992), p. xxxvi; Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 671.

Although there are national regimes that are more liberal and less strict in their adherence to the entity doctrine in the context of corporate group insolvency, accepting the need to bring the law and the commercial reality closer together[7], still the concepts of incorporation, separate personality and limited liability as general rules are strongly grounded in economically advanced countries[8]. They have been commended by those responsible for national legislation and policy as major tools for encouraging economic activity, entrepreneurial risk-taking and new investments[9]. The concepts of separate corporate personality and limited liability apply, in principle, to corporate groups in the same way they apply to single corporations, although in this area there is more controversy over the issue of ignoring the separate personalities of the entities comprising the group and whether and in what circumstances the enterprise can be regarded as one single entity[10]. The application of these notions implies that a group of companies is permitted to be arranged so as to separate liabilities for the various activities of the group letting parties ring fence risk and rest

[7] See New Zealand insolvency regime and US bankruptcy regime (note 6 above).

[8] See OECD, The Responsibility of Parent Company for Their Subsidiaries (1980), "Summary of comparative findings", paras 65-70 (this document is a comparative analysis of the legal situation concerning financial responsibility in OECD member countries) [hereinafter: OECD comparative findings]; Richard D. Kauzlarich, "The review of the 1976 OECD declaration on international investment and multinational enterprises" [1980-1981] 30 Am. U.L. Rev. 1009 1021 (explaining with regard to the OECD comparative findings that "it was clear that the legal systems of all OECD countries upheld the principle of limited liability of companies in the absence of contractual liability, with certain fairly consistent but limited exceptions"); ALI Principles (note 189 *supra* chapter 2), p. 80, stating that the respect for the corporate form is strongly grounded in the laws of all three NAFTA countries; Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), p. 328 (indicating that even the most advanced corporate group law, the German Stock Corporations Act 1965 (*Aktiengesetz*) seeks to preserve the subsidiary as a separate enterprise in that the parent owes duties of compensation to the creditors and minortiy shareholders of the subsidiary in return for the power of control); Blumberg, The Multinational Challenge (note 4 *supra* chapter 1), at chapter 7.

[9] See Blumberg, The Multinational Challenge (*Id.*), p. 145, explaining that one of the imporatnt advantages of limited liability is its encouragement of entrepreneurial risk-taking and new investment, significantly important in relation to conglomerate enterprises; Muscat, The Liability (note 44 *supra* chapter 1), p. 153-154.

[10] See J.H. Farrar, *Corporate Governance in Australia and New Zealand* (Oxford, University Press, 2001) [hereinafter: Farrar, Corporate Governance], p. 229-233, 250 (claiming that "the strict application of Salomon to groups of companies, coupled with limited liability, has led to a system of limited liability within limited liability which was never countenanced by the early legislation, and has facilitated abuses..."); Muscat, The Liability (note 44 *supra* chapter 1), p. 154 (suggesting that "despite the tenacious grip held by limited liability on the law and on current thinking... at least in the context of corporate groups- the principle is due for a critical re-*examiniation*"); D. Milman, "Groups of Companies: The Path towards Discrete Regulation" in *Regulating Enterprise* 218, 220 (D. Milman, ed., 1999); Blumberg, The Multinational challenge (note 4 *supra* chapter 1), p. 58-60 (Blumberg claims that limited liability of corporate groups, although one of the most important legal rules in modern economic society, appears to have emerged as a historical accident. It was applied to the corporate group as a mere deduction from the limited liability that protected individual shareholders, ignoring the fact that by that the limited liability was extended to protect each fragment of the business from liability for the obligations of all the other fragments); Farrar, Company Law, p. 9. See further *infra* chapter 4 sections 4.1.3.3 and 4.3.4; *infra* chapter 5 sections 5.2.4.2 and 5.2.4.4.

upon the chain of ownership of a group. All in all, international ventures today are heavily based on using the incorporation device for managing the financial risks inherent to business development[11].

A global approach, by definition, challenges these deep-seated notions and their underlying goals. It is designed to connect between the entities rather than deal with each component of the group separately in all circumstances. It may create such linkage for procedural purposes, namely- for administering the insolvency proceedings of the different components jointly with some sort of cooperation and coordination, while each component remains with its own debts, assets and creditors. Alternatively, it may impose a stronger device of a complete 'lift' of the companies' 'veils', pooling all assets and debts together, all creditors thus belonging to a single entity. Such tools may be imposed in cases in which the MCGs were operated in a way that would not necessarily be accounted as 'abuse' of the corporate form, yet demand the disregard of the corporate form to some extent in order to facilitate the proceedings and/ or achieve more just results.

Hence, it entails the risk of diluting the business strategy of utilizing separate corporate formations as a method of ring-fencing financial risk. A legal system that may 'change' its attitude towards companies when they enter into the insolvency regime, in a way that disregards the corporate form, might impede new initiatives. Enterprises may hesitate before embarking on new ventures, or may face difficulties in receiving credit (as creditors may fear to be exposed to the financial state of the whole enterprise). This can be particularly pronounced in those MCGs that operated as pure conglomerate and that normally seek to diversify their businesses[12]. It may also increase accounting costs and elicit confusion during the ordinary course of the business, due to uncertainty regarding the way in which liabilities should be allocated within the group[13]. In the event of distress of a certain component it can unjustly drag down the rest into insolvency proceedings.

However, as will be argued herewith, it is quite obvious that there are substantial reasons for applying a global approach to insolvencies within MCGs. It can facilitate

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[11] See *supra* chpater 1 section 1.2.

[12] See Prototype E in *supra* chapter 1 section 1. See also Blumberg, The Multinational Challenge (note 4 *supra* chapter 1), p. 144-147.

[13] See UNCITRAL Legislative Guide (note 58 *supra* chapter 2). The guide states that certainty about the consequences of risk taking is particularly important where the group includes a company with special requirements for risk management, such as a financial institution.

the insolvency proceedings and may achieve more equitable results (comparing to a 'separate' sort of approach if applied). For example, applying a global approach may be the only method that can provide means to achieve worldwide rescue plans to multinational businesses. It is probably also the only system that can overcome unique problems inherent to the MCG insolvencies (e.g., forum shopping). Past experience shows that handling insolvency proceedings of related companies with no cooperation might be extremely disadvantageous, and sometimes completely impractical. It is quite natural that parties involved in these sorts of cases need to have tools to bridge over their boundaries and those of the countries within which they operate[14].

On the national level, certain legal regimes, realizing the need for connecting between affiliates in their insolvencies, developed doctrines enabling such linkages in certain circumstances (for domestic corporate groups)[15]. Hence, in the attempt to construct a global approach there is a sense in learning from those regimes that are equipped with rather modernised tools and at the same time making the needed modifications and adjustments so as to make them compatible universally and applicable to the international cases as well.

It will also be demonstrated that the various MCG's structures and insolvency scenarios[16] may affect the extent to which a global approach should be exercised. Furthermore, an international solution to insolvencies of corporate groups that operated in various countries interferes with these countries' policies regarding the corporate group issue. Hence, countries considering joining a global model will undoubtedly insist on knowing the boundaries and safeguards that such a model will encompass.

Overall, the challenge is to find the way to "square the circle" and balance between the need for a compatible approach and the promotion of commercial enterprise, taking into account the specific characteristics of the MCG case, the different policies regarding this issue and the various possible circumstances and scenarios that may exist in any given case. Essentially, the idea, then, is to 'proceed with caution' in recommending global mechanisms to be applied universally, and to design tests and guidelines that will clearly delineate the boundaries and the consequences of the use of

[14] As will be demonstrated in subsequent chapters (*infra* chapters 4-6).
[15] We will focus on the tools available under the US and New Zealand's legal regimes (see note 6 above).
[16] As was delineated in *supra* chpater 1.

corporate form in the context of an MCG's insolvency. It will thus facilitate MCGs' insolvency proceedings and will promote fairness between creditors in the course of insolvency while leaving open the legitimate use of the corporate form for its appropriate purposes.

3.3 Setting forth key insolvency goals to be discussed

Aims and purposes of insolvency regimes may differ among countries however, a set of main consensual goals can be identified, reflecting a sort of 'standardised policy' across nations[17].

Modern, internationally-accepted practices[18], as well as the key objectives of existing models for cross-border insolvencies for single companies[19] postulate that insolvency proceedings should operate efficiently and effectively, maximizing value of the debtor's assets and increasing return to creditors[20]. Individual collection of creditors' debts thus gives way to a collective procedure[21]. This involves the notion that creditors' rights should be a fundamental concern of the bankruptcy system, as when

[17] The question of the role and objectives of insolvency law has been long debatable among scholars, especially in the US. For instance, whether insolvency law should focus exclusivly on maximizing returns to creditors or should it also concern itself with other objectives such as employment protection or public trust on the insolvency system (see e.g. in the US: Thomas H. Jackson, "Bankruptcy, nonbankruptcy and the creditors' bargain" [1982] 91 Yale L.J. 857; Baird and Jackson, "Corporate Reorganization and the treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors" [1984] 51 Univ. of Chicago Law Rev. 97; Jackson and Scot, "On the Nature of Bankruptcy: an Essay on Bankruptcy Sharing and the Creditors' Bargain" [1989] 75 Virginia Law Rev. 155; Elizabeth Warren, "Bankruptcy Policy" [1987] 54 Univ. of Chicago Law Rev. 775; Warren and Westbrook, "Searching for Reorganization Realities" [1994] 72 Wash. Univ. L.Q. 1257. In the UK: Vanessa Finch, *Corporate Insolvency Law* (2002); Rizwaan Jameel Mokal, *Corporate Insolvency Law: Theory and Application* (2005)). However, for the purpose of this study, a set of widely accepted goals (as reflected in international models) will be referred to and subsequently discussed, without ranking or setting different weights for different goals.

[18] See e.g. the IMF Principles (Int'l Monetary Orderly Fund, & Effective Insolvency Procedural Principles: Key Issues (1999) (http://www.imf.org/external/pubs/ft/orderly/index.htm)); the Asian Development Bank ('Good Practice Standards for an Insolvency Regime' in Law and Policy Development at the Asian Development Bank, April 2000), http://www.adb.org; World Bank-UNCITRAL Standard (note 58 *supra* chapter 2); UNCITRAL Legislative Guide (note 58 *supra* chapter 2).

[19] For the discussion of current models for cross border insolvencies see *supra* chapter 2.

[20] See e.g. Articles 13 and 17, part two of the Model Law (note 143 *supra* chapter 2), and the Recitles to the EU Regulation (note 75 *supra* chapter 2) especially Recitles (2) and (8). See also Ian F. Fletcher, "The European Union Regulation on Insolvency Proceedings", INSOL INTERNATIONAL CROSS-BORDER INSOLVENCY A Guide to Recognition and Enforcemnt, 15, 20 (2003); Fletcher, Insolvency (note 4 *supra* chapter 2), p. 45; R. Goode, Principles of Corporate Insolvency Law, 2005 [hereinafter: Goode, Insolvency], p. 60-62.

[21] See e.g. Goode, Insolvency (*Id.*), p. 61; Rajak, Company Liquidations (note 110 *supra* chapter 2), p. 135.

the enterprise becomes insolvent they become its real financial stakeholders[22]. Nevertheless, another objective would be to restore the company to a profitable business where this is practical, that is where the business is financially viable[23]. This is a sort of elaboration on maximizing value, as it reflects broader objectives, such as preserving jobs for the benefits of the employees and the community in general[24]. In all, the aim is to make the most of the company's value, and at the same time reduce the costs of the proceedings as much as practicable, while pushing towards its rehabilitation where possible. This goal in its variety of aspects will be referred to as enhancing economic (or cost) efficiency.

In addition, an effective and meaningful insolvency process should aim to treat stakeholders[25] fairly, impartially and equally, and to generally promote integrity in the system[26]. This notion, which will be termed as 'fairness', in fact encompasses several elements. A key expression of fairness in the context of insolvency is the application of the 'pari passu' principle, which provides for an equal distribution from the insolvent estate for similarly situated creditors (domestic and foreign), according to the applicable system for the ranking of claims. These rules of priority should be upheld in order to preserve stakeholders' legitimate expectations[27]. Secondly, concern

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[22] See West Mercia Safetywear Ltd (in liq) v Dodd [1988] B.C.L.C. 250; Farrar, Corporate Governance (note 10 above), p. 250, indicating the general view that, in the event of insolvency the duty to creditors and the interests of the creditors in the company's assets increases, to the detriment of the shareholders. Nevertheless, the debtor and its owners and officers may benefit from an increase of the company's value as well.

[23] See Goode, Insolvency (note 20 above), p. 60-61.

[24] See e.g. Articles 13 and 17, part two of the Model Law (note 143 *supra* chapter 2); Objective (iii) (p.13) of World Bank-UNCITRAL Standard (note 58 supra chapter 2).

[25] This term mainly refers to the creditors (see note 22 above, but also note 24 above and preceeding text), including voluntary and involuntary creditors, secured and unsecured. The protection of innocent shareholders from debtor's manipulation is also a concern for insolvency systmes (see note 29 below and preceeding text). Thus, in this work we will refer to 'creditors' or 'stakeholders' interchangeably to mean that fairness to all parties are the concern of the insolvency system with an emphasis on the creditors. Where there is particular consideration of a certain group of stakeholders, this will be indicated.

[26] See e.g. Article 13, part two of the Model Law (note 143 *supra* chapter 2); I. F. Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL International, Cross-Border Insolvency, a Guide to Recognition and Enforcement 15, 20, explaining that a main objective of the EU Regulation is that the principle of equality of creditors shall be fully respected; Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 9, stating that the underlying policies of the bankruptcy law are essentially equitable in nature: to achieve fair treatment to creditors and other claimants.

[27] See e.g. Recitals 12, 24 of the EU Regulation (note 75 *supra* chapter 2); Objectives (v) and (x) (p. 13) of World Bank- UNCITRAL Standard (note 58 *supra* chapter 2). See also Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 703, indicating equality in distribution as one of the 'accepted set of goals' that were identified by universalist scholars; See generally on the principle of equality in insolvency in Goode, Insolvency (note 20 above), p. 62; Rajak, Company Liquidations (note 110 *supra* chapter 2), p. 133-134 (Professor Rajak convincingly stresses though that in the international context the principle faces strong dangers of

should be given to aspects bearing on the administration and location of proceedings (in the context of international insolvency). That is, meeting creditors' interests and expectations on matters of jurisdiction as well as ensuring due process. In this regard, existing models for cross-border insolvency suggest that the system should minimize disadvantages for creditors when participating in foreign insolvency proceedings, and be sensible to their legitimate interests[28]. The third dimension of fairness is the protection of stakeholders from manipulation and abusive behaviour by those who controlled the company[29].

Economic efficiency and fairness will also demand the application of predictable, clear and transparent rules[30]. In the context of insolvency, the absence of predictability and certainty in the handling of cross-border insolvency cases is regarded as a disincentive to cross-border investment and an obstacle to capital flows[31]. A predictable insolvency system will promote stability, enhance lending and investment and will promote consensual dispute resolutions between a debtor and its creditors[32]. Transparent rules and procedures promote fairness and integrity in the system and create an informed and communicative environment. For it to achieve predictability an insolvency regime is required to set down clear insolvency rules in all relevant aspects. It includes both procedural and substantial rules pertaining to insolvency, as well as rules of cross-border insolvency.

In addition to general insolvency goals, legal regimes dealing with insolvencies which entail international elements should also be concerned with the factor of concurrent

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ring fencing assets and applying a "grab rule" (*id.*, p. 347-348. See also Harry Rajak, "The Harmonisation of Insolvency Proceedings in the European Union" [2000] C.F.I.L.R. 180, 185). As will be elaborated below, this problem further augments in the group scenario).

[28] See e.g. Article 13, part two of the Model Law (note 143 chapter 2); Recitals 12 and 13 to the EU Regulation (note 75 *supra* chapter 2). See also Fletcher, Insolvency (note 4 *supra* chapter 2), p. 368-369. The ECJ in the case of *Eurofood* emphasized the importance of due process in the course of international insolvency (see *infra* chapter 5 section 5.1.5).

[29] See e.g. Article 14, part two of the Model Law (note 143 chapter 2). See also Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 9, explaining that fairness has at least two dimensions- equality of distribution among general creditors and protection of creditors and public investors against manipulation by the debtor and insiders.

[30] See e.g. Article 13, part two of the Model Law (note 143 *supra* chapter 2); Objective (ix) (p. 13) of World Bank- UNCITRAL Standard (note 58 *supra* chapter 2)., p. 25. The goals are inter-related, yet, for the sake of the analytical examination of the goals they will be split and considered separately.

[31] See e.g. Article 13, part two of the Model Law (note 143 *supra* chapter 2).

[32] See e.g. objective (x) (p. 13) of World Bank- UNCITRAL Standard (note 58 *supra* chapter 2). See also Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2286.

jurisdiction and its potential misuse by parties involved in the insolvency process attempting to 'shop' for the preferable forum.

An additional factor which is relevant to the design of international models is the need to take into account differences in national insolvency laws (dependant on the scope of the model and the 'group of state' in relation to which it is designed to be applied)[33].

Existing models for cross-border insolvencies of single debtors were designed to achieve these goals by applying a sort of universalist approach that delineates tools for recognition, easy access and cooperation among courts and administrators[34]. To promote greater efficiency and in order to avoid forum shopping the EU Regulation also applied rules of international jurisdiction and choice of law[35].

The analysis provided in the next chapters[36] explores the ability of a global approach for insolvencies within MCGs to attain similar goals to those set out above. That is, whether such an appraoch can push these goals forward, in relation to the specific aspetcs and issues pertaining to the international group scenario. Apparently, the case of the MCG insolvency adds complexities and particular challenges on a legal system that aims to meet such goals. Thus, prior to examining what could be a workable solution, the special difficulties and the reasons why each of these objectives are most relevant to the MCG case will be presented.

Economic-efficiency[37]

The complex case of a multiple debtor operating in different states demands a specific attention while considering what sort of insolvency regime will be the optimal in order to achieve the most cost-efficient results. This will refer both to scenarios where liquidation is the path ahead and where it is possible to reorganize and save the business or the company. As will be described in the following chapter[38], assets of the estate may be spread between different entities and may be located within different states; solvent entities may be dependant on insolvent related companies; inter group

[33] See e.g. Article 3, part two of the Model Law (note 143 *supra* chapter 2), and Recital 11 to the EU Regulation (note 75 *supra* chapter 2).
[34] See *supra* chapter 2 sections 2.4.3, 2.4.4 and 2.4.5.
[35] See Recital 4, 12 and 23 to the EU Regulation (note 75 *supra* chapter 2); See also *supra* chapter 2 section 2.4.3.
[36] See *infra* chapters 4-6.
[37] This issue will be discussed in *infra* chapter 4.
[38] *Infra* chapter 4.

dealing may be difficult to ascertain; creditors may have claims against more than one entity and so on. It is the interest of all parties involved in any MCG's insolvency to be subjected to such a regime that may tackle this unique situation and facilitate the process, and even make use of the MCG's special characteristics.

It has been argued that in order to facilitate worldwide reorganizations and worldwide sales of assets it is necessary that one single court will handle the entire group's insolvency process. However, this (according to this approach) would broaden bankruptcy jurisdiction beyond acceptable limits[39]. Undoubtedly, the specific case of the MCG insolvency introduces complex challenges in this regard. Yet, a delineation of the problems and the prospects pertaining to these cases in terms of achieving cost efficient results, while considering the various relevant organizational structures and insolvency scenarios[40] will ultimately enable to appreciate the importance of a global approach in this regard. It will also assist in establishing the characteristics a global approach should encompass in order to guarantee cost-efficient outcome.

Accordingly, both the issue of restructuring businesses and enabling profitable sales of assets will be considered in the context of an MCG scenario, and on the other hand the possibility of a global approach to reduce the costs that may be involved in an MCG insolvency case.

Fairness[41]

The notion of fairness in its various dimensions as delineated above[42] becomes more compound in the MCG scenario. In the case of a single debtor (that is not part of a group) it is clear that rights can be enforced against it and its assets in places where it operated; creditors should be able to be involved in the insolvency process of the debtor; distribution should be conducted from this debtor's assets only; creditors should be protected from manipulations done by him. Conversely, the question of morality and the ability to preserve it in the multiple companies' situation is much

[39] Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 718-720.
[40] See *supra* chapter 1.
[41] This issue will be discussed in *infra* chapter 5.
[42] See notes 25-29 above and accompanying text.

more sensitive with the multinational scenario augmenting the difficulties[43]. Unique issues and problems arise from the fact that a business is comprised of separate entities located in different states. It is unclear, for instance, whether proceedings against an MCG or against any of its members can be opened in other places where it had operations through subsidiaries; whether legitimate expectations of creditors of companies in specific states should be kept or overruled for the sake of the benefit to the group as a whole; whether there is a right to be involved in foreign proceedings of a related company; whether the pari passu principle is limited to each specific component's own estate; how inter-group claims should be treated in the transnational insolvency scenario.

The diversity of interests in the case of the MCG is overwhelming compared with the case of a single debtor. There is no one single set of creditors of a single debtor, but rather a number of 'groups of creditors' (of each component) and shareholders, dependent on the amount of companies comprising the group. Furthermore, these sets of stakeholders may be in very different positions (apart from the classification within each component). Some may have dealt with a stronger entity than others; some may still be 'potential' creditors of a solvent member of the group. Certain creditors may have dealt with the group as a 'group' while others only with a local component. In addition, the type of creditors may be different, as some may be considered 'insiders' (if the companies had inter-group dealings) while others 'outsiders' or 'third party creditors'. This special situation should be explicitly addressed on the global level. Understanding the problems relating to fairness in the cases of insolvencies within MCGs will help us value the importance of a global approach and will put focus on the problems that need to be resolved.

Considering mismanagement and manipulations will also demand special consideration in the MCG scenario. Here, the question of the responsibility of related companies (typically parent companies) for the financial state of subsidiaries arises,

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[43] See Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 9, stating with regard to domestic corporate groups in general that in proceedings involving constituent companies of corporate group or other enterprises under common control, these problems arise in particularly sensitive form; Farrar, Corporate Governance (note 10 above), p. 234, explaining that when some of the affiliated companies are in different jurisdictions the problems of dealing with unfairness within corporate groups are increased; Muscat, The Liability (note 44 *supra* chapter 1), p. 22 stating that in the transnational dimension the complexity of the problems raised by the group phenomenon is heightened and in addition other issues of a different nature arise, associated with conflict of laws (see also Rajak's assertion in note 27 above).

and whether the insolvency regime can protect stakeholders from abuse of the corporate form, including the shuttle of assets to foreign members.

The various elements of fairness with their particular implications in the MCG scenario will be discussed in the following analysis of insolvency goals in order to appreciate the strengths of a global approach and how it can overcome potential weaknesses in these respects. Accordingly, it will be examined whether a global approach can accord with creditors' expectations and rights concerning the location and administration of the proceedings where an MCG is involved; whether equality in distribution can be ensured in the particular situations present by an MCG insolvency (for instance where assets and debts of affiliates were intermingled) and whether such an approach can provide remedies for dealing with abuse and unfair behaviour within an MCG (in the event of insolvency).

Forum shopping[44]

The fact that the MCG has physical presence in more than one forum by virtue of the existence of a subsidiary (or other form of affiliate) makes it prone to transnational litigation and brings up the potential of having a concurrent jurisdiction problem[45].

Indeed, the lack of uniformity in the law as well as creditors' preference to have close control over the proceedings may motivate parties to shop for a 'better' forum in which to handle proceedings. As we have seen[46], national laws differ in their insolvency laws and in their treatment of corporate groups, as well as matters of procedure and private international law. This adds to general differences in attitudes of different forums. Thus, it may render certain jurisdictions more attractive than others in any particular case[47]. As a result, debtors as well as creditors involved with the

[44] This issue will be discussed in *infra* chapter 6 section 6.1.
[45] See Bell, Forum Shopping (note 45 *supra* chapter 1), p. 6, 7; Jay Lawrence Westbrook, "International Judicial Negotiations" [2003] 38 Tex. Int'l L.J. 567, 568-569.
[46] See note 6 above, and *supra* chapter 2 section 2.4.1.
[47] See Bell, Forum Shopping (note 45 *supra* chapter 1), chap. 2. See also Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 721. LoPucki claims that a successful international shop could offer great rewards. The shop might change the priority among creditors, render security interests invalid, or change the law governing avoiding powers. Shops might take cases to countries with corruptible judges, different languages, different treaty relationships, or locations inconvenient to creditors. There are in fact countries that already compete as "heavens" for international bankruptcies such as Bermuda, Luxembourg and the Cayman Islands (*Id*; see also LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 193-200). The Netherlands and the UK have also become 'successful' in attracting debtors, wishing to place the

enterprise may opt for a particular forum in the event of a group collapse or insolvency of any of its members. Furthermore, in practice creditors may prefer to have control over the proceedings either for preventing other parties from pulling the collapsed 'cart' in their direction or to be able to safeguard their own rights[48]. In trying to achieve close control creditors may pick the local forum where a debtor is situated, although another forum with strong connections to the group as a whole may be more appropriate[49]. These problems are thus of crucial importance and will need to be addressed while looking for the proper solution for the MCG insolvency scenario.

Predictability and Certainty[50]

In the scope of MCGs there should be clear understanding of the legal consequences of a failure occurring within a worldwide group of companies. Particularly, parties should be able to predict where the insolvency of the MCG or any part thereof will take place, and which laws will apply to the case.

Yet, the ability of a global approach to provide such clear predictable rules for the MCG insolvency cases is doubtful. Indeed, it has been observed that existing approaches to MCG's insolvencies have left the system very unpredictable[51]. Thus far, universalist systems have not determined what would be the appropriate forum in cases of MCGs (that is, what would be regarded as the "home country" of the proceedings), and what 'portion' of the corporate group will be handled by that forum[52]. This situation puts the whole universalist approach in a fragile disadvantageous position[53]. The question here is how a global approach can provide consistent and less obscure rules that will not undermine ex ante predictability, and will be clear and sufficiently certain.

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insolvency process where they have the best chance of surviving a bankruptcy (see Peter, J.M. Declercq, "Restructuring European Distressed Debt: Netherlands Suspension of Payment Proceeding... The Netherlands Chapter 11?" [2003] 77 Am. Bankr. L.J. 377, 378; *GLOBALTURNAROUND*, "French breakthrough for Euro Regulation", October 2003, issue 45, p. 9; *GLOBALTURNAROUND*, "Europe leads world in Forum Shopping", June 2003, issue 41, p. 1).

[48] See *infra* chapter 6 section 6.1.

[49] See *infra* chapter 5 section 5.1.2.

[50] This issue will be discussed in *infra* chapter 6 section 6.2.

[51] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 723-725.

[52] See *supra* chapter 2 section 2.3.

[53] Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 723-725.

State Sovereignty[54]

The differences in national regimes' laws and approaches on issues pertaining to MCG insolvencies have already been indicated[55]. For our particular purpose, this situations demands taking into account potential clash with national laws and policies when appreciating the merits (or faults) of a global approach and the traits it should encompass. Inconsistency with domestic regimes may present two sorts of problems for the application of an international system. The first is a practical one; it involves the possibility to apply a proposed international model over a widening circle of countries, where the international rules may not fit with national regimes. The second, a more theoretical issue, is whether it is at all justified to interfere with domestic policies, thus allegedly undermining the important and unique distinctions between legal regimes. In other words: is a global approach able to give enough room to national laws?

Summary

The following discussion in the subsequent chapters will deal with each of the above goals separately, systematically examining the various issues and questions pertaining to each of them. The critical question is whether or not a global approach may benefit each goal, independently, over and above any other approach so that it will contribute to its successful conclusion.

Accordingly, the traits of a global approach, which will be extracted from each separate discussion, will only present part of the picture. Thus, the entire image will be revealed step by step, as other goals of the insolvency regime will be examined. Ultimately, within an applicable model, these goals need to be combined into appropriate guidelines to where and how global tools should be imposed[56].

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[54] This issue will be discussed in *infra* chapter 6 section 6.3.
[55] See section 3.2 above; reference to national laws' appraoches will be further made within subsequent chapters (see *infra* chapter 4 sections 4.1.3.3 and 4.3.4; *infra* chapter 5 sections 5.2.4.2 and 5.2.4.4).
[56] A proposed set of such guidelines will be delineated in the concluding chapter.

Chapter 4

Enhancing Economic Efficiency

4.1 Maximizing asset values of an MCG in distress

4.1.1 Possible alternatives for a company in distress

In the case of a single debtor entering into insolvency process various options may be available. It may be that liquidation is the best path, meaning the cessation of the business, the sale of its productive units or the piecemeal sale of its assets. Usually, however, the company would do better to operate as a complete productive unit prior to its sale so as to preserve the value of its assets. Modern views suggests that in many cases rehabilitation would be the preferred path an insolvent debtor should take, since as a general rule the value of the whole (the debtor as a complete business) is greater than the value of its parts[1]. Essentially that means restructuring a corporation which may be restored to productivity and regain its competitiveness.

4.1.2 The degree of integration as the dominant factor predicting the need for linkage between the MCG's components in insolvency

In the case of a group of companies in distress (either a domestic or a multinational group) the above-mentioned alternatives may be applied separately to each specific company comprising the group. Indeed, imposing 'insolvency solution' to each insolvent part thereof as a separate process will be appropriate if the group was not economically integrated (as was portrayed earlier in Prototype E[2]). Linking between such proceedings may be superfluous and provide additional costs of communicating between foreign proceedings, when no such need exist. Most often, the insolvency of one part of such a group will not affect the rest[3], so an entire collapse would be rare. Even if the insolvency will encompass the whole group linking between the fragments of the group will not typically provide a significant advantage in terms of increasing revenues. The proceedings will involve a variety of unrelated business of different

[1] See e.g. UNCITRAL Legislative Guide (note 58 *supra* chapter 2), p. 11. This approach also reflects another objective, which is to preserve jobs (*id*; see also *supra* chapter 3 section 3.3).
[2] See *supra* chapter 1 section 1.6.
[3] See 4.1.3.1 below for the discussion on the 'domino effect' often occurs in cases of integrated MCGs.

nature, assets from diverse sorts and generally an assortment of components that do not represent one single business, which would gain from reconstruction or from a joint sale. Therefore, at least as a starting point, in terms of cost efficiency demands, the insolvencies are better handled separately, keeping the option of future linkage should an advantageous opportunity rise.

The cases of integrated MCGs (depicted by Prototypes A-D[4]) suggest a fundamentally different approach. As will be shown below, if the group was conducted as an integrated one profitable 'cross-entity' insolvency solutions are very likely to be attainable and thus it would be beneficial to operate a joint insolvency process for such an MCG. This is true not only in the strongly integrated scenario[5] (in which case it would be efficient to operate a more unified operation and treat the group as a single entity at least to some extent[6]), but also in cases of integrated groups in general which were comprised of distinct entities with identifiable assets and debts[7].

As will be shown below, whether for the purpose of liquidation or reorganization, it will frequently be advantageous to link between the separate entities, their assets and businesses "mimicking" the MCG's 'real' way of conducting the business in its 'golden days' and its operational links. This linkage in the course of the insolvency procedure will broaden the opportunities available to the stakeholders. In the case of a multinational group this advantage will be even more pronounced, since the geographical spread of the business can be used to increase its attractiveness and appeal.

The existence of inter-group transactions or cross- guarantees is also not a pre condition for a beneficial linkage (although, it adds a reinforcing justification for connecting between the insolvencies). In fact, it may be the case of a host of subsidiaries neatly organized within national borders each operating separate local activities and owning separate assets with no mutual transactions. Still, the fact that all the fragments were connected in such a way that they all operated a single business and were managed as a group suggests that it would benefit from global asset

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[4] See *supra* chapter 1 section 1.6. See also examples of such cases in sections 4.1.3.7 and 4.1.4.2 below.
[5] Prototype C (see *supra* chapter 2 section 1.6).
[6] See section 4.3 below.
[7] The approach should not be limited, though, to the scenario of equity based hierarchical group but should encompass the various forms of distressed MCGs. As was delineated earlier in this work MCGs comprised of entities linked via contract can also form an integrated group (see notes 60 and 93 *supra* chapter 1).

realizations in the event of insolvency. Similarly, if there were inter-group links this may result with a de facto integration even though the businesses may appear to be separate (the 'conglomerate' type of MCG that operate different businesses)[8]. The fact that 'under the surface' linkages and inter-relations (such as administrative support and financial interdependence) exist, may imply that the different companies are not truly commercially and financially independent and a linkage in the course of insolvency may be needed[9].

In terms of the 'insolvency scenario' we are dealing here with a situation where more than one company within an MCG is under insolvency, as in the first class of insolvency scenarios described earlier[10]. Thus, a linkage may be needed between the two or more proceedings in order to maximize asset values[11].

As long as the entities are integrated, there is no relevance in this case to whether the companies at stake are a subsidiary and an immediate holding company, a bundle of sister companies or otherwise a subsidiary and an ultimate holding company[12]. The exact ownership structure is also insignificant as subsidiaries may be partly or fully owned by a parent company[13]. The critical question is whether the companies at hand were integrated in the ordinary course of business. It is a matter of economic essence and the examination of the actual links existing within the group at stake. This economic reality is the relevant predictor for gaining economic advantages in the course of insolvency as a result from linking between the MCG components. The linkage applied follows the amount of actual integration present in the case, rather than shareholder scenario generally.

Nevertheless, the optimum cost efficient solution for a distressed MCG may change in the course of its insolvency process. Initially, it may seem that a certain company within a group should conduct separate proceedings without linking it in any way to

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[8] See notes 91 and 92 *supra* chapter 1, and accompanying text.
[9] *Id.*
[10] See *supra* chapter 1 section 1.5.1.
[11] This may also include situations where any of the companies are on the verge of insolvency or are most likely to enter into insolvency as a result of their integration with the rest of the group (see *supra* chapter 1 section 1.5.1; see also sections 4.1.3.9 and 4.2.4 below).
[12] It is assumed, though, with regard to multi-tiered structures, that more often subsidiaries and their immediate holding company will constitute together a commercial division or one enterprise in one sector. Other subsidiaries with their own immediate holding company would constitute another enterprise in a different sector (see Muscat, The Liability (note 44 *supra* chapter 1), p. 444).
[13] The percentage of equity holding is one of the factors to consider while evaluating the degree of integration (less autonomy is expected if the parent company holds a large portion of the equity), however it is not a decisive factor (see *supra* chapter 1 section 1.5.2).

another insolvent entity of the same group. Further in the process, as a result of new information being revealed or new opportunities that come along, it may appear beneficial to tighten the linkage between the insolvencies and even treat the companies as one single entity[14]. Insolvency proceedings in their nature are dynamic, thus parties should be able to embrace various solutions compatible to the specific scenario they face.

4.1.3 Effective Reorganizations within MCGs

4.1.3.1 Integrated business scenario: the benefits of a unified reorganization

A collapsed MCG may be able to produce higher returns to creditors as well as preserve jobs if it will restructure itself or reorganize. Such course of action may be available for certain companies or parts of a group separately. However, if the group or any part thereof was integrated with the rest[15], it will often be extremely disadvantageous or even impossible to rescue only parts of the business. As aforesaid, usually, in reorganization case of a single debtor the goal is to preserve the business as a whole[16]. Similarly, reorganization of an MCG should be aimed at preserving the business as a whole rather than at disintegrating it. This outcome would be very improbable unless the insolvent MCG would be put under such a regime that will link its various components and operate a reorganization, which will embrace the complete business. Under such regime, one could consider the entire enterprise's situation and seek for the best solution. This may include actions such as closing down particular parts of the business, concentrating on specific more viable elements, cutting down the number of employees or activities and basically seeking the best utilization of the MCG's resources.

Moreover, the financial state of a member of a group may jeopardize the financial survival of other affiliates[17]. Thus, the interest of any specific company within a group, that anticipates better values if it is preserved is that the entire business (or its viable part) will be preserved as well. Liquidation of another particular component may have a damaging effect upon the reputation of the rest of the group. It may also

[14] See section 4.3 below.
[15] As in Prototypes A-D (*supra* chapter 1 section 1.6).
[16] See section 4.1.1 above.
[17] See Jacob S. Ziegel, "Corporate Groups and Crossborder Insolvencies: A Canada- United States Perspective" [2002] 7 Fordham J. Corp. & Fin. L. 367, 370.

affect the financial viability of the others resulting with a 'domino affect' leading to a total shutdown. Conversely, when a certain subsidiary is a burden on the others then in order to stabilize the business it may be necessary to close it down.

It may be even more crucial to have a cross-frontiers rescue for the MCG if there were inter group links such as cross-guarantees. The inter dependence between the related companies means that the economic situation of any part of the group has the ability to severely affect the others, thus a global solution would prove to be the reasonable way to approach the process.

A global reorganization will also make possible an intelligent use of the groups' assets[18], to control the operation of the group as a whole and direct the way the business goes ahead. It would be extremely problematic to reorganize such business if each part of it is managed separately and is 'left' to pull to its own direction.

Thus, for instance, a local bank of a certain subsidiary could enforce a security or push the company into liquidation, whereas if it had the sufficient information with regard to the whole group and if it was assured that its interests will be represented in the global operation it would have acted differently[19]. In other words, local creditors of local components may take actions that can in fact produce considerable damage to the wider purpose. As a result, they may undermine a global solution that may benefit the stakeholders as a whole, eventually achieving better results for the particular local creditors as well. If indeed this company was an integral part of the business as a whole the rescue of the group may increase the value of the assets that the creditors wanted to sell. In addition, these creditor banks (for example) will obviously be able to continue benefiting from doing business with the company.

Local creditors may also be prone to take actions against a local company in order to gain control or an influential position over its administrator so that they will be able to

[18] In a reorganization of a single debtor, it is regarded as crucial that the debtor should be able to use all the assets which are important for the continuation of the business' operations, and that would be impossible if creditors in different jurisdictions can attach them, or if assets are concealed in other jurisdictions (see e.g., Article 17 of the Model Law (note 143 *supra* chapter 2), explaining that "To the extent there is a lack of communication... it is more likely that assets would be concealed or dissipated, and possibly liquidated without reference to other possible, more advantageous solutions"). See also K.S. Alwang, "Notes, Steering the most appropriate course between admiralty and Insolvency: Why an International Insolvency Treaty should Recognize the Primacy of Admiralty Law over Maritime Assets" [1995-1996] 64 Fordham L. Rev. 2613, 2625 (claiming that "reorganization is unlikely if foreign creditors can attach, in multiple countries, the assets necessary for the debtor to continue operating").

[19] See also *infra* chapter 5 section 5.1 and *infra* chapter 6 section 6.2.

influence the proceedings against the other parties. These actions may again threaten the prospect of maximizing the overall return.

4.1.3.2 The need for a global approach

A 'separable' approach to the case of MCG's insolvencies- that is, an approach aimed at territorialism[20], and at keeping group's entities entirely separate in all circumstances[21]- cannot provide efficient means to conduct global restructurings. For this purpose, a method of linking between the components' insolvencies and conducting some sort of joint administration is required. We do not mean here a complete disregard of the corporate form and treating all components as if all were one single entity[22]. In the ordinary case of integration, each company will remain responsible to its own creditors and have separate assets. Distribution of dividends will be done separately for each entity. However, the proceedings will be conducted jointly and co-ordinately. It will then enable joint decisions with regard to the reorganization of the enterprise, the transfer of information with relation to the feasibility of a rescue plan for it or any of its divisions, and the operation of a plan itself. With no such approach, as demonstrated, stakeholders will often act according to their specific and narrow interests without considering the benefit of the whole group[23].

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[20] See the Universalist- Territorialsit debrate described in *supra* chapter 2 section 2.2.

[21] See the 'battle' between a global approach and traditional corporate theory ideas described in *supra* chapter 3 section 3.2.

[22] This approach will be later on discussed (see section 4.3 below).

[23] See Jay Lawrence Westbrook, "Theory and pragmatism" [1991] 65 Am. Bankr. L.J. 457, 465, arguing that without universalism, creditors would have distorted incentives when choosing between reorganization and liquidation). But see Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 707. LoPucki claims that Westbrook's argument incorrectly assumes that creditors, rather than estate representatives, control the decision to reorganize or liquidate. This argument is unconvincing bearing in mind the ability of creditors to open liquidation proceedings, as being done in practice, sometimes purposely to gain control and influence on the course of the group proceedings (see, for example, the creditors' insolvency proceedings being opened against a number of subsidiaries of the Italian dairy group Parmalat (see note 51 below) subsidiaries in the Cayman Islands, and the courts' rejection to replace the appointed provisional liquidators at the request of the group's administrator (judgment of the grand court of the Cayman Islands in the administrator's application to replace the provisional liquidators appointed to a Cayman Islands subsidiary of Parmalat- Parmalat Capital Finance Ltd. (Grand Court of the Cayman Islands, March, 2004) [hereinafter: "the Cayman Islands' court decision"]. I am grateful to Mr. Michael Crystal, QC, of 3/4 South Square, who represented the Joint Provisional Liquidators in their successful response to the Italian administrator claim to replace them in their appointment, for supplying a copy of this document)).

4.1.3.3 National laws' approaches

'Joint administration' (or 'procedural consolidation') is a tool available in certain legal regimes. This mechanism implies that only the procedural aspect of the insolvency is being consolidated rather than the actual entities. Thus, a joint administration of the affiliated companies' proceedings is held. A particular court presides over all the cases and one office holder (or a bundle of joint administrators) is appointed for the various debtors. However, each company remains separate in the course of insolvency, and creditors recover their claims from the particular entity to which they belong. The idea is to facilitate reorganization of the affairs of the whole enterprise or to bring about a going concern sale.

The US 'procedural consolidation' is regarded as 'a matter of convenience and cost saving' and it does not involve redistribution of substantive rights[24]. In Canada and the U.S. it is counted as essential that corporate groups will be subjected to a joint administration when a financially distressed group seeks to reorganize itself[25].

4.1.3.4 The preferable approach for the international scenario

On the international level such approach is less 'obvious', even in terms of cost efficiency[26]. It entails jurisdictional complications including the need to subject an entity to a different legal regime (dependant on the specific means applied in a model, as will be suggested below) and added costs of communication[27]. Hence, if not truly justified[28] the outcome may be additional burden of costs and efforts on the estate. However, if the MCG was integrated it will be even more crucial to provide such means for its insolvency compared with the national case. No doubt, it will be much more complicated to attempt a worldwide reorganization with no means of

[24] See e.g. In re Coles, 14 B.R. 5, 5-6 (Bankr. E.D. Pa. 1981). See also Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 402-405 (on procedural consolidation in the United States). According to information supplied to the author by Mr R. DeKoven of 3/4 South Square on consolidation in the US (see note 106 below), consolidation is the common approach to corporate groups' insolvencies taking place in the US.

[25] See Jacob S. Ziegel, "Corporate Groups and Crossborder Insolvencies: A Canada- United States Perspective" [2002] 7 Fordham J. Corp. & Fin. L. 367, 376 (explaining that procedural consolidation "is almost de rigueur" in Canada and US corporate groups' reorganizations).

[26] Other considerations such as the issue of creditors' rights or sovereignty surrender involved in conducting a joint process for insolvencies that originated from different states will be discussed later on (see *infra* chapters 5 and 6).

[27] See section 4.2.3 below.

[28] As explained above (see section 4.1.2), such is often the case if the MCG was not integrated or if any specific company within the group is operationally and functionally separated.

cooperation where different legal regimes are involved and entities are geographically dispersed across countries and continents.

As was mentioned earlier[29], ad-hoc means of communication and cooperation have been used in MCG cases, mainly such that the 'centre of gravity' was in the US. Cases such as *Maxwell*[30], *ICO*[31], *Global Crossing*[32] and *Federal Mogul*[33] demonstrate the significant advantage in handling a group's insolvency proceedings jointly, as a group, and not as separate insolvencies, ultimately resulting in a worldwide settlement or an optimal combined plan of reorganization.

A global approach specifically addressing the unique case of MCG can similarly apply means to link between the proceedings and to facilitate a joint process for more profitable restructuring of an integrated global business. Such 'linkage' may indeed be achieved by Ad Hoc cooperation as mentioned above. However, relying only on Ad Hoc means is not a sufficient solution. As was previously discussed[34], such mechanisms will be normally limited to similar time zones and a small number of jurisdictions involved. For the MCG insolvency case at stake, agreeing ('privately') on the appropriate way ahead and consequently implementing and operating it without any guidelines or acceptable rules may demand extensive costs. It also reduces the probability of achieving any agreement at all. Furthermore, it may be problematic with regard to certain jurisdictions, which lack the means to cooperate without the specific authority[35].

4.1.3.5 Providing adequate tools

The main idea is that a global approach should aim at facilitating cooperation and coordination between administrators of separate entities and the corresponding courts when more than one insolvency proceeding are being held in more than one country with relation to an integrated MCG. Accordingly, a global approach should expressly provide that courts (and representatives) handling insolvency proceedings of related

[29] See *supra* chapter 2 section 2.4.2.
[30] In re Maxwell Communications Corp., [1993] 1 W.L.R. 1402 (Ch. 1993); 170 B.R. 800 (Bankr. S.D.N.Y. 1994). In this case there was more than one centre of gravity (see infra chapter 7 section 7.4).
[31] In re ICO Global Communications Servs. Inc., Case No. 99-2933 (Bankr. D. Del. 1999).
[32] Chapter 11 No. 02-40188-reg (REG) (Bankr. S.D.N.Y.).
[33] Re T&N Ltd and Others ([2004] All E.R. (D) 283 (Oct).
[34] See *supra* chapter 2 section 2.4.2.
[35] *Id.*

companies (belonging to an MCG) should cooperate and communicate either directly or through local representatives or administrators. It can be implemented by embracing particular means of communication such as provided in the Model Law for the case of a single debtor[36] or in the ALI Guidelines for communication[37], or similar to 'in action' practices that are being used in current MCG cross-border insolvency cases[38].

It should also be provided, with regard to those MCGs that are initially identified as non-integrated[39], that a line of cooperation should remain open (although it may be inactive), to enable future cooperation should the need arise. This way, the model can be sensitive to the dynamic of these cases[40].

A global approach may provide additional mechanisms that are required in order to arm administrators and courts with the necessary authority to exert control over foreign insolvency proceedings of affiliate companies and to be able to take urgent actions in the foreign proceedings for the interest of the group as a whole. Cooperation and coordination might take time to reach the stage when they will have an effect. Yet, administrators may need to take immediate actions in the proceedings of affiliates in order to stabilize a business[41]. For that purpose, tools such as easy access to other member's proceedings, recognition of foreign decisions, assistance and relief, provided in cross-border models with regard to single debtors[42] should be applied to the case of an MCG. As a result, an interim stay of proceedings (provided to protect the debtor's assets), for instance, should embrace affiliates of the debtor as well. However, these mechanisms should be available globally, independently of what is permissible domestically in each jurisdiction[43].

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[36] See *supra* chapter 2 section 2.4.4.
[37] See *supra* chapter 2 section 2.4.5.
[38] See section 4.1.3.4 above; See also the means of direct communication (*supra* chapter 2 section 2.4.2).
[39] See section 4.1.2 above.
[40] *Id.*
[41] See section 4.1.3.1 above.
[42] See, for instance, chapters II and III of the Model Law (see *supra* chapter 2 section 2.4.4).
[43] Conversely, see the Model Law and the ALI Principles regimes under which the relief actions are granted by the local court imposing national laws and national remedies (*supra* chapter 2 section 2.4.4 and 2.4.5).

4.1.3.6 A centralized proceedings approach

A major contribution of a global approach would be to embrace a 'centralized approach', by way of either enabling all the proceedings against the group members to be handled at a single venue under a single legal regime (that of the forum handling the case)[44], or at the least subjecting the process (handled in several jurisdictions) to a single direction (hereinafter: a centralized approach). This way full procedural consolidation can be feasible for the international case. The approach should aim at making this tool available globally; taking into account the fact that currently many jurisdictions lack such a mechanism[45].

With no single supervision, administrators and courts will still need to agree on every issue pertaining to the reorganization process within a system of 'equal' parties. It will undoubtedly be advantageous to provide ways to avoid the difficulties in cooperating within such a (worldwide) system[46].

In addition, embracing rules of international jurisdiction (with worldwide recognition) and applicable law (adopting these notions from the EU Regulation, and extending them to the case of transnational groups), will promote a unitary process with universal effects for the MCG. It is true, that successful international insolvencies of MCGs were conducted in the past relying mainly on cooperation, without the need to centralize the process to a single place[47]. Yet, these occasions were most notably a matter of parties' good will and courts cooperating with each other.

Having concurrent proceedings taking place in different jurisdictions (even when it is handled using effective guidelines of cooperation and coordination) regarding related companies may be problematic in achieving a global plan also because there may be significant differences in the bankruptcy laws of the countries involved. For instance, one of the jurisdictions involved may provide for a reorganization process while another has more limited schemes for rescuing companies or even lack such

[44] Similar to the principal choice of law rule (and its exceptions) under the EU Regualtion (see *supra* chapter 2 section 2.4.3).
[45] Cf. the situation under the ALI Principles, according to which consolidation is available only if it is permissible under the applicable law, and as long as proceeding have not been opened against the subsidiary in the country of its main interests (*supra* chapter 2 section 2.4.5.3). The Principles do not recommend standardised rules of consolidation with tests to their application.
[46] For the discussion on the identification of a place of 'common control' from which the proceedings could be supervised see *infra* chapter 7.
[47] See section 4.1.3.4 above.

mechanisms completely[48]. Furthermore, even in the case that a certain way to rescue the enterprise is applicable in both jurisdictions, it may still be that differences regarding for instance the ability to re-finance the business may raise substantial difficulties during the course of the reorganization[49].

Therefore, a centralized approach that can be embraced under a global model will be advantageous. It will promote achieving a harmonized process. Regarding reorganization of a group within the US it is indeed widely accepted, that a single court and a single representative should coordinate the entire business[50]. The need for such a concept is evident when looking at international experience.

4.1.3.7 Examples on the international level

The commencement of the *Parmalat* multinational group's insolvency process, encompassing numerous entities that operated in different countries around the world[51] exemplifies the difficulties that a global plan initiative may face. In this case proceedings were opened in different countries with no sufficient cooperation and no one single direction for the entire group. The mandate of the Italian Extraordinary Administrator appointed by the Italian government for several companies in the group[52] was to try and design a global reconstruction plan for the group as a whole.

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[48] This might be a significant obstacle were for examples a developing country (whose insolvency regime might still lack basic tools for reorganizations) and a developed country both hosted subsidiaries of a group willing to rescue itself; But, it may create problems even in less dramatic differences among legal regimes (see, for instance, the *Enron* case in which a complex plan needed to be designed in order to overcome the differences between the chapter 11 and scheme of arrangement regimes (In re Enron, No. 01-16034, 2001 Extra Lexis 304, at 2, (Bankr. S.D.N.Y. Dec. 10, 2001); *GLOBALTURNAROUND,* "To scheme or not to scheme Lessons from Enron", October 2004, issue 57, p. 11).

[49] For example, if the group is looking for liquid funds to pay for crucial supplies of goods and services to maintain the business activities, it will be problematic if certain jurisdictions (to which certain affiliates are subjected) do not provide for a form of priority funding and safeguards for the recovery of 'new' money. A bank for example may refuse to give credit to these parts of the business. As a result, it may be extremely difficult to enable to stabilize and sustain the entire business operations.

[50] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 707. See also Blumberg, Bankruptcy (note 43 *supra* chapter 1), Chap. 13.04. Blumberg explains, with regard to American Bankruptcy law, that the filing in the same court of petitions pertaining to a parent corporation and its subsidiary has considerable significance. See further in section 4.1.3.3 above.

[51] The Italian Dairy group of companies that was operated in Europe, but also in many other parts of the world, including South America, South Africa, Canada, U.S. and Australia, and that was headquartered from Italy. The proceedings of Parmalat produced many different episodes of litigation (see e.g. proceedings mentioned in note 54 below).

[52] The appointment took place at the end of the year 2003, in the wake of revelations of widespread fraud by executives.

The specific aim was to preserve the group as a going concern[53]. However, one of the greatest threats the administrator faced is disintegration, brought on by local creditors opening separate proceeding in different places around the world[54]. Such actions posed a major obstacle for the administrator as they reduced his hold on the units outside Italy and thus interfered with his efforts towards a global reconstruction of the group. Obviously this is true mainly with regard to those units of the group that were part of the integrated dairy business and that were essential for its industrial restructuring plan[55]. In general, the experience of the beginnings of the Parmalat insolvency process demonstrated a lack of sufficient cooperation and of central direction and single supervision[56].

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[53] See Parmalat News Briefs, DOWJONES Newsletters, International Insolvency, March 9, 2004, p. 9.

[54] One example is the provisional liquidation process against three Cayman Islands subsidiaries being opened by US insurance companies, and that were continued to be handled 'separately', after the Italian administrator's loss in gaining control over the process (see the Cayman Islands' court decision (note 23 above); see also "Parmalat ask Kroll to find assets", Financial Times, March 2, 2004; David Reilly "Judge Rejects Administrator's Push To Control Parmalat's Cayman Units", DOWJONES Newsletters, International Insolvency, March 2, 2004, p. 1, 3). Other examples can be seen in the Brazilian court's decision to appoint administrators to the Brazilian unit (see "Brazil Unit Says Two Banks Will Provide Credit Lines, DOWJONES Newsletters, International Insolvency, March 2, 2004, p. 6), in the administration order that has been given by a French court against Parmalat's milk supplier group Laitier des Pyrenees (see "Parmalat is not Europe's Enron It's Italy's Maxwell", GLOBALTURNAROUND, January 2004, issue 48, p. 2) and in the Irish high court's decision to approve the appointment of Irish provisional liquidators to Parmalat's subsidiary Eurofood IFSC (see Eurofood IFSC Limited [2004] B.C.C. 383. Previously to this decision an Italian court in Parma declared the company insolvent and placed it under Italy's jurisdiction (see Eurofood IFSC, Re (Trib (I) 19 February 2004 [2004] I.L.Pr.14). The Italian administrator appealed against the decision. The Irish Supreme Court decided to refer to the ECJ several questions concerning the proper jurisdiction issue and recognition of main proceedings (see Eurofood IFSC Ltd [2005] B.C.C. 999). The Advocate General's opinion upheld the Irish court claim to be the proper jurisdiction as he considered the appointment of a provisional liquidator as sufficient to commence main proceedings thus the Irish court was the first court to open the process (and the proceeding in Italy was improperly opened). Additionally, as the right to be heard was denied from the Irish officer the Irish court could refuse recognition of the Italian proceeding on public policy grounds (Eurofood IFSC Ltd (C- 341/04) [2005] B.C.C. 1021 (AGO)). The ECJ broadly upheld this opinion (Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397). See further on this case in *supra* chapter 2 section 2.4.3.3, sections 4.1.3.8 and 4.2.1 below, *infra* chapter 5 section 5.1.4, *infra* chapter 6 sections 6.1.2 and 6.2.2 and *infra* chapter 7 sections 7.2 and 7.3 (for background on the 'Eurofood battle' and further comments on the ECJ judgment see C. Rapinet & I. Tucker, "European Court of Justice resolves Parmalat jurisdictional battle under EC Insolvency Proceedings Regulation" Sweet & Maxwell's Company Law Newsletter issue 10/ 2006, p. 1)).

[55] For instance, with regard to Eurofood IFSC, the Irish unit, it has been argued (by this subsidiary's US bondholders) that it was a standalone unit and irrelevant to the group restructuring. Eurofood IFSC was a wholly owned subsidiary of Parmalat SpA and in essence a financing vehicle for the Parmalat group (see "Italian and Irish courts clash over Parmalat", GLOBALTURNAROUND, April 2004, issue 51, p. 3).

[56] See "Parmalat is not Europe's Enron It's Italy's Maxwell", GLOBALTURNAROUND, January 2004, issue 48, p. 2. See also the Cayman Islands' court decision (note 23 above) in relation to the agreement between the Italian administrator and the provisional liquidators appointed to the subsidiaries in the Cayman Islands. There, although the parties agreed upon a memorandum providing for co-operation and a mutual exchange and access to information and documentation, in reality "there has

As mentioned earlier in this work, although the EU Regulation does not provide a straightforward mechanism to deal with corporate groups[57], in a number of recent cases the concept of COMI[58] was applied in a manner that it resulted in putting all the components of the insolvent group under the same court in the same country. It therefore promoted the supervision of a single court and a single appointee, thus facilitating a cost-efficient administration of the estate[59]. In these cases proceedings were still separated in the sense that administration orders were issued for each company, creating a sort of parallel yet 'local' insolvency proceedings.

Such was the case of *Crisscross*[60], a pan-European Telecommunication group of companies. An English court granted administration orders over the entire MCG that was comprised of eight separate companies registered in several EU jurisdictions and Switzerland each having its own assets and creditors. This decision was apparently made on the basis that each of the companies had its COMI within the UK. However, the underlying rationale for placing all the proceedings in the UK appears to be that the companies effectively formed one business and that the management of this business was handled from the UK[61]. Granting an administration order within the UK to each of the group's companies was regarded as beneficial for the stakeholders[62]. Since this group actually formed a single business, placing it into administration under the control of one administrator and under the supervision of a single court had the potential of better returns for creditors as a whole[63].

Similarly, in the case of *Daisytek*, a multinational computer peripherals group[64], an English appointee attempted to facilitate a pan-European restructuring by opening proceedings for the different companies comprising the European division of the group at the same place (the UK)[65]. The idea here was to administer the proceedings

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been less then optimal cooperation extended by each party to the other under their memorandum of agreement".

[57] *Supra* chapter 2 section 2.4.3.3.

[58] Note 92 *supra* chapter 2.

[59] See I.F. Fletcher, "The Challenge of Change: First Experiences of Life under the EC Regulation on Insolvency proceedings in the UK", Annual Review of Insolvency Law, 2003 (Toronto, Carswell, 2004), 431, 450-454.

[60] Crisscross Telecommunications Group, Re (unreported, 20 May 2003) (Ch D).

[61] See Lyndon Norley, "INSOLVENCY: Tooled up" The Lawyer, November 10, 2003.

[62] See Crisscross is First Group Admin, GLOBALTURNAROUND, June 2003, issue 41, p. 3.

[63] *Id.*

[64] In re Daisytek- ISA Ltd [2003] B.C.C. 562 (Ch D).

[65] In Daisytek 14 companies were at issue, amongst them a French trading company and two German trading companies as well as their German holding company. The question of jurisdiction arose in

jointly, instead of having a 'patchwork of different cases in different countries'[66]. The UK court found that the COMI of each of the subsidiaries was in England. This gave the group a chance of saving itself as a whole, rather than splitting up its various European assets[67].

In the case of *Cenargo*[68], a shipping group of companies, the English judge placed the majority of the group's proceedings in the UK, including the administration of those components that were incorporated in the Isle of Man[69]. The joint administration resulted in rehabilitation of many companies in the group and was completed within 12 months of the commencement of proceedings. Apart from the jurisdictional issues at the beginning it has been largely a consensual process gaining support from creditors[70].

The cases of *MG Rover group* of companies[71], and *Collins & Aikman* corporation group[72] are also examples of attempts to facilitate pan-European restructurings by using the COMI tool, placing subsidiaries located in different European states under a main insolvency process in a particular state to be administered in a unified manner[73].

In one of the proceedings related to the *Parmalat* collapse[74], a Hungarian court placed a Slovakian subsidiary of a Hungarian company (which was also under insolvency proceedings) under insolvency proceedings in Hungary. Both companies belonged to the Parmalat group and between themselves were closely connected; hence the idea was to have main proceedings for both companies at the same jurisdiction, under a single court and a single appointee.

Recently, the Commercial Court of Nanterre (France) appointed French practitioners to administer the insolvency process of several subsidiaries of the *Emtec* group of

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respect of the German companies and the French company. The court gave fourteen administration orders against the parent and thirteen subsidiaries.

[66] See Stephen Taylor, "Daisytek chain reaction", *GLOBALTURNAROUND*, July 2003, issue 42, p. 10.

[67] See "French breakthrough for Euro Regulation" Global Turnaround, Oct 2003, issue 45, p. 9.

[68] Re Norse Irish Ferries & Cenargo Navigation Limited (unreported, 20 February, 2003), Ch D.

[69] Based on the decision in Brac (Brac Rent-A-Car Inc, Re [2003] EWHC (Ch) 128; [2003] B.C.C. 248).

[70] See *GLOBALTURNAROUND*, "Cenargo: The shape of things to come" January 2004, issue 48, p.10, 11.

[71] See the administration proceedings in the Birmingham District Registry of the High Court (the judgment handed down on May 11, 2005 is available on the EIR Database at www.eir-database.com).

[72] [2005] EWHC 1754 (Ch D).

[73] See *GLOBALTURNAROUND*, "MG Rover, Europe's biggest COMI", May 2005, issue 64, p. 3; *GLOBALTURNAROUND*, "Collins & Aikman, Europe's biggest COMI filing", August 2005, issue 67, p. 1

[74] Re Parmalat Hungary/Slovakia, Municipality Court of Fejer, 14 June, 2004.

companies, which were incorporated in different European countries. The idea was to enable a group-wide insolvency therefore avoiding a value-destroying break-up[75].

These cases demonstrate the advantage in placing the proceedings of related companies in a single location all subjected to a single supervision and a single insolvency regime for facilitating global (pan European in these cases) restructurings.

4.1.3.8 Alternative solutions matched to the specific case

However, as previously stated[76] due to the lack of rules for dealing with affiliated companies, the EU Regulation only provides a 'black or white' and a rather 'random' solution to these cases. This is because joint administration is solely achievable when all companies involved share a mutual COMI, and the courts do not consider the entire group scenario when determining whether to open local proceedings, or whether to open proceedings against foreign affiliates.

Thus, in cases such as *Daisytek* discussed above, the UK court 'struggled' to show how each of the subsidiary's COMI is in England, without being able to rely on the group scenario for justification[77]. It could be argued that the Daisytek group was in fact integrated centralized MCG[78] in the sense that it was managed as a group, with a single direction and control, coordinated and headquartered from England[79]. Yet, the court had given separate considerations to each subsidiary as a separate legal entity[80].

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[75] This was regarded as a 'U-turn' in the French system's attitude toward using the COMI concept for achieving Europe-wide insolvencies (see *GLOBALTURNAROUND*, "French revolution on COMI", March 2006, issue 74, p. 1).

[76] See *supra* chapter 2 section 2.4.3.3.

[77] Daisytek- ISA Ltd, Re [2003] B.C.C. 562 (Ch D), at p. 5-8.

[78] As in Prototype A (*supra* chapter 1 section 1.6).

[79] The court stated for instance that: "the evidence shows that the trading companies in the group are managed to a large extent from Bradford and that they are managed and controlled as a group so that the activities of the group companies throughout Europe are co-ordinated by the head office in Bradford". It also indicated that the English parent, who performed the head office function for the group gave various guarantees to major suppliers and trade creditors of its subsidiaries (In re Daisytek-ISA Ltd, and others [2003] BCC 562 (16 May 2003, Chancery Division, Leeds D.R., at p. 2; see also Bob Wessels, "International Jurisdiction to Open Insolvency Proceedings in Europe, In Particular Against (Groups of) Companies" Working Papers Series, Institute for Law and Finance, Johann Wolfgang Goethe University (http://www.iiiglobal.org/country/european_union/InternJurisdictionCompanies.pdf).

[80] This was also the finding of the French court of appeal overturning the initial decisions of the Commercial Court of Pontoise, which refused to recognise the English orders (In re Daisytek-ISA Ltd (Cour d'Appel, Versaille, 4 September 2003). But, see the case of TXU in which Mr Registrar Baister did expressly take into account (in its decision to place Irish and Dutch debtors' insolvency proceedings in the UK) the fact that a related company (of these debtors) was already the subject of an administration order in England. Placing all related companies "under one roof", as was held, could

The other side of the coin is that local courts 'fought' against decisions that apparently attempted to relocate a COMI of what they saw as a local subsidiary, to another country. This was what happened at first instance in France and in Germany in the *Daisytek* case[81]. In other situation such as in the *Eurofood* proceeding[82], where COMI (of this subsidiary) apparently was in Ireland, no linkage to the rest of the group was available.

The decision of the ECJ in the *Eurofood* case[83] seems to put further obstacles upon the possibility to take into account group considerations when determining the proper jurisdiction (in EU Regulation cases) and therefore reducing the potential of achieving cost-effective results in such MCG cases. It refrains from developing a 'group concept' and it seems to put rather little emphasise on the interrelations between the subsidiary and the parent. Rather, it states that the COMI should be determined for the particular subsidiary. Though the fact that the subsidiary is controlled by a parent situated elsewhere may be a relevant factor, it seems to receive little weight, or at least it is not clear in which circumstances 'group consideration' will prevail. This will most probably render future jointly held European-MCG insolvencies even more random, slowing down the recent tendency of European courts and representatives to strive to look at the group as a whole in applying insolvency solutions[84].

As was mentioned earlier, the ALI Principles provide some initial tools for dealing with NAFTA corporate groups, promoting cooperation and coordination between affiliates' insolvency proceedings[85]. Yet, one major flaw is that the Principles do not provide any test to determine when a parallel process will be appropriate as opposed to proceedings opened at the same country (for all affiliates involved), and do not contain rules to determine on the proper jurisdiction for the corporate group consolidated process, nor choice of law rules[86].

A global approach can both suggest a strait forward approach to those scenarios where consideration of the costs and benefits for the group as a whole implies that a

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"achieve consequential savings in costs" and result with a better coordinated process (TXU Europe German Finance BV, Re [2005] B.C.C. 90 (Ch D)). See also G. Moss, "Creditors voluntary liquidation for foreign registered companies" Insol. Int. 2005, 18(1), 12-13).

[81] See *infra* chapter 5 section 5.1.4 and *infra* chapter 6 section 6.1.2

[82] Note 54 above.

[83] Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397.

[84] See also *supra* chapter 2 section 2.4.3.3.

[85] See *supra* chapter 2 section 2.4.5.3.

[86] *Id.*

centralized approach is preferable, as well as situations where local proceedings are justified.

Thus, in the examples such as those provided in the previous section, and that are depicted by Prototype A[87], centralization is appropriate, especially if reorganization is sought. That is, centralization fits those cases where the relevant companies were integrated and defaulted (or will probably collapse in the near future), and where they were all closely controlled together via the head-office of the group. It will significantly enhance achieving maximum cooperation so that reorganization will be feasible and most beneficial; as it will mimic the economic reality of how the group was managed in its ordinary course of business. Obviously, such an approach will need to include tools to identify the proper venue for the handling of the MCG insolvency process that represents the centre of the group as a whole[88].

Yet, as will be shown below[89], 'centralizing' the proceedings may in certain cases result with higher costs and thus lead eventually to a less cost efficient result. This refers to scenarios where subsidiaries had significant autonomy locally, as represented by Prototype B[90]. In addition, the subsequent chapter[91] will show how this type of scenarios poses additional concerns that will demand alternative solutions to that of full centralization.

A case such as *Parmalat* can demonstrate a mixture of scenarios (or Prototypes[92]). The group can be seen as integrated principally, as it conducts businesses in a specified industry, under the same name, comprising of numerous subsidiaries conducting different activities yet all related to the conduct of the group's business. Although normally each entity has its own separate assets and liabilities and an independent management, ultimately, these activities are altogether related and identified as 'Italian' in origin. Nonetheless, certain subsidiaries can be regarded as being more

[87] *Supra* chapter 1 section 1.6; the need will be even more pronounced in cases of strongly integrated groups (see section 4.3 below).
[88] We will address this issue in *infra* chapter 7.
[89] See section 4.2.3 below.
[90] *Supra* chapter 1 section 1.6.
[91] See *infra* chapter 5 section 5.1.
[92] See *supra* chapter 1 section 1.6.

loosely controlled, only coordinated by the group centre and having significant autonomy locally, as in Prototype B[93].

Therefore, it should not be a fixed rule that an integrated group should always conduct all the proceedings at a single venue. Rather, when affiliates had significant autonomy it should be possible to have local proceedings. However, the various proceedings should be subjected to a single supervision as suggested above[94]. In other words, even if the situation suggests that local proceedings are necessary, it may still gain from a linkage and cooperation between the various proceedings. A global approach will be able to link between the various proceedings in this case, and to subject all the affiliates to one single court and administrator to supervise over the process whereas other current international tools (e.g., the EU Regulation) cannot[95]. The amount of control exerted over the other affiliates' processes should be appropriated according to the circumstances, depending on the specific case and the amount of coordination required[96].

Even if a particular subsidiary is apparently not integrated with the group (a mixture of Prototypes involving Prototype E[97]), still a line of coordination with the group centre should be kept open[98]. Yet, the centralized process should encompass only those entities that are indeed integrated and together centralized and controlled, and also exclude entities that are truly solvent[99]. Accordingly the COMI of the group will refer to that part of the group which is integrated and insolvent[100].

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[93] *Supra* chapter 1 section 1.6. See, for instance, the case of *Eurofood* (note 54 above) in which apparently, the subsidiary had significant autonomy and connections to Ireland, though to some extent coordinated via the group headquarters in Italy as the parent guaranteed all transactions and all policy decisions were made from Italy.

[94] Section 4.1.3.5 above.

[95] Under the EU Regulation regime, if the COMI of an affiliate is not found to be at the same place of that of another affiliate then each proceeding will be handled separately, since we are dealing with different entities.

[96] For instance, in the strongly integrated MCG scenario, where an interventionist tool may be needed, if separate proceedings should be opened they ought to be closely linked to the main process, preferably subjecting all proceedings to a single legal regime, at least if it is a complete intertwined scenario (see section 4.3 below (particularly section 4.3.7)).

[97] *Supra* chapter 1 section 1.6.

[98] See also section 4.1.2 above.

[99] That is, it is not probable that they are going to be affected by the collapse of the rest of the group (see section 4.1.3.5 above). A solvent parent may be still linked to the group in the course of insolvency if group liability issues arise (see *infra* chapter 5 section 5.2.4).

[100] See, for instance, the case of *Brac* (Brac Rent-A-Car Inc, Re [2003] EWHC (Ch) 128; [2003] B.C.C. 248) where the European operations were in a virtually independent cluster. See also Collins & Aikman corporation group [2005] EWHC 1754 (Ch D) in which after the filing of chapter 11 proceedings

Subjecting the entire process to a single direction while conducting territorial proceedings can be done using the notions of 'secondary' or 'ancillary' proceedings provided in existing cross-border insolvency models[101], applied to the MCG scenario. This means that there is no need for 'double' proceedings against a subsidiary- both main in the group's centre and secondary locally. One proceeding can be opened locally, however the court of the 'group centre' will have the authority to supervise and communicate with the entire process. Three main characteristics should be kept. The first is that local proceedings will be subjected to the supervision of the other, placed at the group's centre, aimed at aiding the main proceeding, to enable coordination of a worldwide resolution. Second, it should be possible to have either reorganization or a winding up process locally[102]. Third, opening territorial proceedings against a subsidiary should be done only when it is indeed necessary, dependant on the scenario at hand, and not automatically, in order to prevent the loss of potential benefits of complete centralization[103].

Finally, in certain situation it will be difficult or impossible to locate a single venue from which to supervise or handle the entire process[104]. A global approach can take such scenarios into account and provide alternative solutions. Here, a parallel process may be unavoidable, yet linkage between the affiliates will be still appropriate and beneficial via means of cooperation and communication, mutual recognition, access and relief[105].

4.1.3.9 Including the entire group in the reorganization

Another advantage of a global approach is that it could extend the insolvency regime to include allegedly still solvent parts of the group. While attempting a reorganization of an MCG all integrated parts thereof should be considered as they all take part in the group's business. Hence, even when some parts appear to be solvent excluding them from the reorganization regime could significantly hamper the chances of successful

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against the ultimate parent located in the US, the European operations were controlled via headquarters in the UK.

[101] See *supra* chapter 3.

[102] To avoid destabilizing 'rescue' process opened for the group as a whole (Cf. the situation under the EU Regulation in supra chapter 2 section 2.4.3.2).

[103] See the 'territorialist' critique in this regard in supra chapter 2 section 2.3.

[104] See *infra* chapter 7 section 7.4, and examples provided there.

[105] See section 4.1.3.5 above.

restructuring. Indeed, under the US bankruptcy regime corporate groups will usually file for bankruptcy for all subsidiaries, solvent and insolvent. It is justified there, as it clearly promotes efficiency, among other things[106].

This concept was also de facto applied in EU Regulation cases, for example, in Daisytek[107]. Administration orders were requested for all the European subsidiaries that were part insolvent and part likely to become insolvent within a short time[108].

A mechanism of extending the insolvency regime over apparently solvent components of the group can be adapted explicitly to the case of MCG. Once again, applying such a mechanism should be based on the examination of the inter-relations between the related companies.

4.1.4 Facilitating Global Sales

4.1.4.1 The benefits of global sales in the integrated business scenario

A sale of the entire business will often be more attractive than a sale of specific parts thereof. Thus, in the cases of integrated MCGs[109] assets will often be more valuable when presented as a package deal[110]. An obvious example will be when each company comprising the MCG owned a certain part of a complete product. In this case a combined sale may be much easier to achieve and most probably receive a higher price than separate sales.

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[106] In most large chapter 11 cases the court confirms only a single plan covering all of the debtor entities (see information provided by Professor LoPucki in Jacob S. Ziegel, "Corporate Groups and Crossborder Insolvencies: A Canada- United States Perspective" [2002] 7 Fordham J. Corp. & Fin. L. 367, 387). The author also queried Mr R. DeKoven of 3/4 South Square barrister chambers about US procedural and substantive consolidation as being conducted in practice. Mr DeKoven explained that the common practice in large bankruptcy cases is that proceedings are being opened for all subsidiaries in the group even if some of them are not insolvent at the time, to avoid the inefficiency of having new proceedings being opened consecutively and 'inorderly' and so that a plan for the group as a whole could be devised. This is possible under US bankruptcy law since insolvency is not a prerequisite for commencing the process. It should be added that this is also facilitated by the fact that the U.S. bankruptcy regime provides for a 'debtor in possession' device, encouraging group's managers to rescue their enterprise without fear that they will necessarily loose their positions.

[107] Daisytek- ISA Ltd, Re [2003] B.C.C. 562 (Ch D).

[108] *Id.*, at p. 4.

[109] Prototypes A-D (*supra* chapter 1 section 1.6).

[110] See ALI Principles (note 189 *supra* chapter 2), p. 81.

4.1.4.2 Examples of types of global sales

Consider for instance a railway network operating in a number of countries. The assets of this network are actually divided between subsidiaries incorporated in the different states in which the railway is operating. To sell the network in pieces may significantly reduce the price received. Similarly, if a number of related patents and licenses are owned each by a different entity in a group then obviously selling the assets in parts is extremely disadvantageous.

It may also be the case when assets of similar sort are scattered amongst various entities that are valuable as a mass of assets and less attractive if sold to different buyers. Generally speaking, multiple sales of different assets and parts in a group will most likely take longer, involve more effort on behalf of the administrators and will incur a larger cost from the estate compared with a single package sale. It is even likely, that a buyer for an entire enterprise (although comprised of separate entities) may be willing to pay an added premium comparing to the price of the assets alone or to the price of the separate activities of each component.

In the case of KPNQwest N.V. data communication MCG[111], for example, the assets of the group's components were sold separately, sometimes in knock- down prices[112]. The fact that the sales were conducted dis-jointly was apparently disadvantageous in terms of maximizing values. Since the companies' assets together comprised a data communication network (although different components owned different parts of cable rings) it would apparently have been more beneficial to sell the European cyber centres network as a global network of Internet and data hosting facilities, rather than sell it in parts[113].

Enabling global deals also broadens the opportunities available for the companies in distress. It gives the administrators 'a room for manoeuvre' in their attempt to reach the best deal and the best price. It may be, for example, financially wiser to reject

[111] KPNQwest group owned cables in Europe and across the Atlantic Ocean. The cables ran through various countries and were owned by subsidiaries of the group situated in these countries. On 32 May 2002 the Dutch parent company entered bankruptcy proceedings. As a result, many of its subsidiaries were put under insolvency process as well (see Van Galen, Robert, The European Insolvency Regulation and Groups of Companies, October 2003, http://www.iiiglobal.org/country/european_union/Cork_paper.pdf).

[112] Estate Gazette, "Leading data hosting site offered at a 55M GBP discount" September 14, 2002, NEWS, p. 43 ; *GLOBALTURNAROUND*, "KPNQwest in sales drive", June 2002, issue 29, p. 11.

[113] *GLOBALTURNAROUND*, "Parmalat is not Europe's Enron It's Italy's Maxwell", January 2004, issue 48, p. 2.

certain offers that may be available to a specific component in a certain moment, since a larger and better deal is starting to form elsewhere.

4.1.4.3 The advantages of a global approach

A global approach is thus needed in order to prevent connected activities and assets from being divided resulting with a serious impediment to the global returns[114]. A joint administration will be able to facilitate the process through a coordinated operation for the entire business. Thus, assets may be jointly sold even though eventually each entity will have an identified portion in the proceeds, which will then be distributed to its own creditors.

4.1.4.4 Applying proper global tools

Joint administration can be conducted by applying means of cooperation and coordination as was discussed above with regard to reorganizations[115]. This way, the office holder can reach joint decisions with regard to the options available to the group and the conduct of the realization itself. Here as well, a more effective solution would also permit to subject the process to a single direction and therefore to minimize differences and facilitate the joint operation. Especially when a large enterprise is at stake with its spread activities a single supervision will be beneficial, as it would allow a global consideration of the complete picture thus, opt for the very best solution and available deals for the benefit of the creditors as a whole.

Furthermore, extending jurisdiction over solvent parts of an insolvent MCG will considerably aid the administrators' efforts towards a package sale and better realization of assets. In cases where it is anticipated that the solvent parts will eventually fall into insolvency[116] it will be unfortunate to miss deals that would have been available for the business if the whole of it was 'for sale'. And, the fact that in a given moment only part of the group is under administration would make it difficult for the group's business to be adequately marketed and ultimately achieve the best

[114] See Crisscross is First Group Admin, GLOBALTURNAROUND, June 2003, issue 41, p. 3.
[115] See section 4.1.3.5 above.
[116] See section 4.2.4 below on the issue of successive filings.

price[117]. As aforesaid a global approach may adopt means of placing an entire group under administration. Conversely, under a 'separate regime' the decision whether to grant, for example, an administration order can only be grounded on the specific company's financial situation with no relation to that of the group.

4.2 Reducing the costs and length of the proceedings

4.2.1 Dealing with extensive litigation

The event of insolvency of an integrated MCG whose subsidiaries were located in different jurisdictions and were inter- linked by a host of inter-group transactions and guarantees will most probably elicit multiple cross-border claims. Parent companies may have claims against their subsidiaries and vice versa (as a result of inter group loans for instance). A creditor may have claims against several companies regarding the same debt (as a consequence of cross-guarantees for instance). Several Creditors of different components may have claims regarding the same asset (resulting for instance from intra-group transactions and cross-credits). In this course of action, it may be unclear which part of the group is the 'proper' debtor in relation to a given claim[118]. Finally, various components of the group may be located and operated in different countries which may elicit a flood of contested proceedings, jurisdictional conflicts, a need to shuttle claims to different entities of the enterprise etc. All such claims and disputes evidently result in high costs and lengthy processes.

Here too, the complexity and magnitude of litigation may be substantial even in the case where the MCG was not totally intermingled[119]. When the companies had a significant amount of mutual transactions it would undoubtedly reflect on the complexity of claims.

Extensive litigation may also be a result of the way the group was managed and controlled and the behaviour practiced by the corporate group. Liability claims may flood the enterprise, based on allegations such as shareholders' misrepresentation of

[117] See Crisscross is First Group Admin, *GLOBALTURNAROUN*D, June 2003, issue 41, p. 3. (Ms. Godfrey who was acting on behalf of Crisscross Telecommunication Group claimed that as in many group cases it was beneficial for creditors as a whole that all group companies were placed into administration).

[118] See the circumstances in the case of *BCCI* (see section 4.3.2 below). There, the situation was so complex that a pooling concept was applied (see section 4.3.5 below).

[119] The impact of costs in the strongly integrated MCGs cases will be discussed below (see section 4.3 below).

the financial situation of a certain entity[120]. If all such litigation is taking place trans-nationally with duplications with regard to the causes of action or parties involved then costs inevitably increase. Here as well, jurisdictional and choice of law conflicts will add costs to the process. Furthermore, the 'territorial' scenario of concurrent jurisdictions may result with the refusal of a certain court to enforce judgements given by other foreign courts. This is costly in that it might require repetitive procedures over the same issues in the courts of the various entities of the group relevant to the dispute[121].

Another aspect of further litigation may revolve around questions of control over assets and over subsidiaries. That is, administrators appointed to reconstruct or to liquidate a company, which in fact was related to a wider business with operations (through subsidiaries) across the globe may attempt to expand control over cross-border assets and subsidiaries in order to be able to design a workable plan for the business or to maximize value for creditors in any possible way. However, since each of these administrators is appointed to supervise a company rather than the entire group, such intentions are bound to end up in massive litigation. Disputes with other administrators appointed to supervise affiliates' proceedings or otherwise with local creditors are sure to emerge in addition to extensive jurisdictional battles, all of which are obviously expensive and time-consuming.

In the case of *Parmalat*[122], for example, the attempts of the Italian Extraordinary Administrator to gain control over foreign units of the group resulted with significant costs. Since the enterprise was sprawled all over the world, the administrator needed to get a grip on the non-Italian units as well. For this purpose he tried either to place non-Italian subsidiaries under Italian jurisdiction, or to place its own people as supervisors of foreign subsidiaries[123]. However, this effort was not all successful, as separate

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[120] See *infra* chapter 5 section 5.2.4.

[121] See K. Hofstetter, "Multinational Enterprise Parent Liability: Efficient Legal Regimes in a world Market Invironment" [1990] 15 North Carolina J. of Int'l Law and Comm. Reg. 299, 330, further stating that there is a potential for mutual opportunism and conflicting assertions among host country courts (in which a certain subsidiary is located) and home country courts (in which a parent is located) in applying checks on regulatory and adjudicatory powers.

[122] See note 51 above.

[123] For instance, the Italian administrator succeeded to get five Dutch subsidiaries (Parmalat Finance Corporation B.V., Parmalat Netherlands B.V., Parmalat Capital Netherlands B.V., Parma Food Corporation B.V. and Dairies Holding International B.V.) and two Luxemburg Parmalat entities (Olex S.A. and Parmalat Soparfi S.A) to be placed under Italian jurisdiction (see "Parmalat unit account unfrozen", Financial Times, February 26, 2004, p. 29; Peter, J.M.Declercq, "Restructuring European

administration proceedings have been opened against Parmalat's subsidiaries in different countries[124]. The administrator 'fought back' trying to regain control over the subsidiaries and keep his control on the sprawling assets[125], thus incurring additional costs on Parmalat's estate[126].

Further to increasing the burden of expenses on the insolvency proceedings, such amount of litigation may also slow down the whole process. It may seriously interfere with the effort to quickly stabilize the business and to present a restructuring plan for it. In order to prevent a total collapse of the estate, and to be able to use assets wisely in addition to securing refinance for going forward, claims must be resolved speedily with real time responses to conflicts arising in the course of the insolvency. Multiple worldwide proceedings will obviously prevent that. In principle, efficient administration is regarded as highly important for maximizing asset recoveries, as time is of essence especially in rehabilitation proceedings[127]. However, extensive and long litigation will take its toll on liquidation cases as well and may result in considerable value loss for the group's assets[128].

Means of linking between the insolvency proceedings even placing them under the same regime, as mentioned above, are thus crucial in order to reduce the amount of litigation and inefficiency in administrating the integrated MCG's proceedings[129]. As both administrators and courts will be able to efficiently communicate and coordinate their actions, quick resolution of claims and disposition of assets will be achieved. It will also reduce the disputes regarding the control of assets and subsidiaries' proceedings within the MCG as administrators involved in the group's insolvency process will share a common cause and interest. Additional means (rather than granting an independent cause of action for each plaintiff) will be needed to enable a

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Distressed Debt: Netherlands Suspension of Payment Proceeding... The Netherlands Chapter 11?", [2003] 77 Am. Bankr. L.J. 377, 383).

[124] See note 54 above.

[125] For instance, the administrator was seeking to replace the provisional liquidators appointed for the Cayman Islands' subsidiary. The Cayman Islands' court rejected the request and confirmed the appointment of the provisional liquidators (see The Cayman Islands' court decision, note 23 above). An extensive litigation has been taking place with regard to the Irish unit (see note 54 above).

[126] One observer commented with regard to Parmalat that "there is only about US $1 Billion of value left in Parmalat. At the rate things are going, half that could go in legal fees. And, if all this litigation continues, the restructuring could be held up for years" ("Parmalat at legal crossroads" News, GLOBALTURNAROUND May 2004, issue 51, p. 4).

[127] See e.g, UNCITRAL Legislative Guide (note 58 *supra* chapter 2), p. 12.

[128] See Jay Lawrence Westbrook, "International Judicial Negotiations" [2003] 38 Tex. Int'l L.J. 567, 573.

[129] See also *Id.*, at p. 572-573.

unified resolution of claims concerning abuse of the corporate form, as will be discussed later on in this work[130].

4.2.2 The expenses and time waste on obtaining information

A major mission of administrators appointed to supervise insolvency proceeding of a distressed company and one that is done immediately with the commencement of the proceedings is to gather all relevant information and data regarding the affairs of the company. Such information usually includes the company's financial situation, its activities and customers, its assets and liabilities, the market within which it operates etc. In turn, this information (as well as the current situation on all fronts) will also disseminate to all parties involved.

However, in a case of integrated MCGs (either those who had inter group links or simply were managed as a group[131]) information relevant to a certain company may be in the possession of another (for instance, if assets were transferred from one company to another). Furthermore, actions being made in the course of the insolvency process regarding any of the group's members, such as motions filed to court, or attempts to sell assets or to negotiate with a potential investor and so on will also be of importance (and therefore should be known) to other members of the group. Obtaining such additional necessary information will inevitably induce more efforts and costs.

By applying means of linking between the affiliates proceedings and preferably conducting it all at a single centre, a global approach can facilitate sharing and transferring information between affiliates' administrators and courts. This will reduce the need to seek data that was already gathered by a related company. It can enable easy and quick access to information regarding other affiliates or information that is held by such. It should hence expressly provide that information should be accessible to other affiliates' administrators who participate in any joint insolvency process[132]. Consequently, it may reduce costs involving the necessary actions directed at obtaining required information in the course of the insolvency proceedings.

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[130] See *infra* chapter 5 section 5.2.4.5.
[131] See *supra* chapter 1 section 1.5.2.
[132] Similar to what is provided in existing models with regard to the single debtor scenario, for instance in Article 21(1) of the Model Law (*supra* chapter 2 section 3.4.4.2).

4.2.3 The costs of conducting multiple insolvency proceedings

A collapsing integrated MCG may in fact bring about multiple proceedings being held in different places regarding the same multinational business. Thus, duplicate processes are being conducted with overlap between the duties of the different appointees as well as the actions they take. It is widely accepted that when a single debtor with branches abroad is being put into insolvency and consequently proceedings are being conducted in all those places where it had activities, this situation is inefficient and therefore should be avoided[133]. Likewise, managing a number of proceedings for an integrated MCG should be regarded as disadvantageous as a result of redundant costs.

Having several insolvency proceedings instead of one joint together, will entail having hearings for each company separately, as well as notices for creditors and meetings. In many occasions parties involved would need to be represented in more than one proceeding due to the consequences one proceeding may have on other parts of the group. Administrators might eventually do the same 'job' twice since any particular activity being done for a certain company may be relevant for another and vice versa. The recent case of *Parmalat*[134] exemplifies this kind of redundancy in actions and costs. On one occasion for instance, the Italian administrator needed to examine the records of one of the subsidiaries[135], which was located in Malta[136]. However, both he and the provisional liquidators (appointed to supervise this subsidiary's liquidation) went to Malta for the same task of reviewing these documents, ending up with completely unnecessary expenses for both[137].

In an MCG it is not only a question of one vs. a number of processes dealing with the group, it is also a matter of multiple processes held in different countries. This inevitably raises the costs of transferring information and any sort of communication

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[133] See Articles 3(1), 3(2) and paragraph (12) of the Recitals to the EU Regulation (note 75 *supra* chapter 2). See also I.F.Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL, Cross-Border Insolvency, 15, 27-31; Robert K. Rasmussen, "A New Approach to transnational Insolvencies" [1997] 19 Mich J. INT'L L. 1, 18; Jay Lawrence Westbrook, "Theory and Pragmatism in Global Insolvencies: Choice of Law and Choice of Forum" [1991] 65 Am. Bankr. L.J. 457, 461.

[134] See notes 51 above.

[135] Parmalat Capital Finance Limited, which is a member of the Parmalat group of companies.

[136] The direct parent of this subsidiary was a company incorporated in Malta.

[137] See The Cayman Islands' court decision (note 23 above) at p. 15, 16. The court eventually decided that the costs issue is not a major factor comparing to the views of third party creditors willing to have the separate provisional liquidators remain in place.

that will usually demand for travelling between countries and overcoming language and sometimes time zone differences.

Such problems were quite prominent in the case of *BCCI* banking group's insolvency proceedings[138]. In this case a globally coordinated effort was conducted in order to close all the group's operations[139]. However, since the group had operations (part through subsidiaries and part through branches) in many countries liquidators were appointed in more than 50 different jurisdictions (with the three main proceedings taking place in London, Luxemburg and the Cayman Islands from where BCCI was ultimately regulated). The liquidators ended up commuting between jurisdictions in an expensive and time-consuming operation[140]. Dealing with multiple insolvency proceedings under different time zones was also a difficulty the administrators of *Barings Bank* had to face subsequent to the bank's collapse in 1995[141].

The restructuring of the *Global Crossing* MCG[142] involved parallel proceedings taking place in the US and Bermuda[143]. Although successful, the process was highly expensive, as a result of the need to oversee and co-ordinate parallel proceedings for 16 different subsidiary companies. The multi-jurisdictional element added a further layer of intricacy to an already large-scale assignment[144].

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[138] Note 155 below.

[139] *Id.*

[140] *See* GLOBALTURNAROUND, February 2004, issue 49, p. 11; John Willcock, Letter from the Editor, GLOBALTURNAROUND, June 2003, issue 41, p. 2.

[141] Barings collapsed in February 1995 as the result of trading activities carried on in the Far East. The holding company of the group was Barings Bank PLC. On 26 February 1995 Knox J made administration orders in respect of both the holding company and certain subsidiaries and appointed joint administrators to manage the affairs of these companies in London (see in Barings plc and Anor v Internationale Nederlanden Group NV [1995] C.L.Y. 777 1995 WL 1082385 background on the Barings administration). On 27 February 1995 judicial managers were appointed in Singapore to manage the affairs of Barings Singapore (see generally Christopher Brown, "Report of the Board of Banking Supervision Inquiry into the Circumstances of the Collapse of Barings" J.I.B.L. 1995, 10(10), 446-452; Sheila C. Bair, "Remarks, Lessons from the Barings collapse" [1995-1996] 64 Fordham L. Rev. 1). The creditors were eventually rescued from a 1.4$ billion debt as a result of a buyout by a Dutch bank and insurance firm in March 1995. However, the lack of an orderly process for administration of the insolvent multinational enterprises aggravated the debt (see Jhon K. Londot, "Handling priority rules conflicts in international bankruptcy: assessing the international bar associatio's Concordat" [1996-1997] 13 Bankr. Dev. J. 163, 167).

[142] Global Crossing Ltd (Chapter 11 No. 02-40188-reg (REG) (Bankr. S.D.N.Y.).

[143] The group comprised over 200 companies registered in 27 jurisdictions. The top holding companies were Bermudian registered (for tax reasons). However, the group's business was conducted primarily from the U.S. As a result, when the group sought the protection from its creditors it simultaneously filed for chapter 11 in the US and sought the protection of the Bermudian court through provisional liquidation proceedings (see Moore, Susan, "Global Crossing versus Cenargo The right way and the wrong way, *GLOBALTURNAROUND,* January 2004, issue 48, p. 8.; *GLOBALTURNAROUND*, "How Global Crossing made it to safety", January 2004, issue 48, p. 6).

[144] *GLOBALTURNAROUND*, "How Global Crossing made it to safety", January 2004, issue 48, p. 6.

Consequently, in the case of an integrated group, placing the entire estate in a single place and handling its proceedings jointly from there[145] will reduce costs of multiple proceedings and trans-national communication. If on the other hand, the companies comprising the MCG were not integrated[146] then usually what is being done in one of the affiliates' proceedings will not hold significant relevance to the rest of the group. If a joint administration will not be required and therefore will not be conducted then substantial communication, shuttle of information and so on and so forth will not be needed in the first place. Consequently no added costs will occur as a result of the fact that there are multiple proceedings taking place with regard to that sort of group.

However, even in the integrated MCG cases, changing forum and applicable laws for a business that prior to the event of insolvency had substantial activities and operated under a rather different regime may turn out to be inefficient. It may add complexities rather than facilitate the process, since the business was well established in a specific country working under certain rules[147]. Thus, in the scenario of the integrated coordinated collapsing MCG[148], local proceedings will be justified in terms of costs[149].

4.2.4 Reducing the inefficiency as a result of successive filings

Another possible scenario of an integrated MCG is that of initially solvent components that as the main process progresses become insolvent as well. The fact that in reality the business is divided into several entities will usually mean that not all companies become insolvent simultaneously or file for insolvency at the same instance[150]. However, it is most probable that the collapse of one member within a group will affect other members as well, if they were both integrated; especially if there were significant inter company links, such as mutual transactions and cross guarantees[151].

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[145] See section 4.1.3.6 above.
[146] Prototype E (*supra* chapter 1 section 1.6). .
[147] With regard to a single debtor, this is indeed one of the reasons why under the EU Regulation it is possible to have territorial (secondary) proceedings (Recital 19 to the EU Regulation (note 75 *supra* chapter 2) (see further supra chapter 2 section 2.4.3).
[148] Prototype B (*supra* chapter 1 section 1.6).
[149] See section 4.1.3.8 above for the discussion of the alternative solution that can be provided by a global approach.
[150] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 723 (arguing that filings by one or more members of the group followed later by filings of other members are common).
[151] See section 4.1.3.1 above.

In terms of administrative costs this may suggest increased complexities. If parts of the group continue to operate regularly, then it might be more difficult to get information with relation to their financial state, existing assets and managers' actions. Administrators would need to update and modify their approaches, predictions and plans constantly, obviously resulting in inefficient administration.

A cost-efficient solution should be given for the entire business and therefore the entire group must be considered from the very beginning. A global approach is thus advantageous in this respect if it enables to address the situation of the group as whole and then decide whether to place all affiliates under insolvency regime.

4.3 The strongly integrated MCGs- A need for interventionist global means in order to avoid high inefficiency

4.3.1 The scenario

In some cases of MCGs the corporate veil was not properly maintained in the ordinary course of the MCG's business in the sense that the group represented itself and acted functionally inter-dependently[152]. Typically, this will present extreme difficulty to untangle the clutter and to identify the separate businesses of each member of the group when the MCG faces insolvency. In fact, it could practically be impossible or otherwise unprofitable to do so. Thus, an operation of insolvency proceedings for each of the members separately is very unlikely to be an efficient one[153]. It is important to note that the focus here is not on any sort of misconduct on part of the people who ran the MCG including cases of creditors' reliance on misrepresentations[154]. Rather we look at the situation of distressed affiliate companies present with high degree of integration. The event of insolvency in this type of MCG may engulf all the affiliate companies as they will all face insolvency simultaneously, but it could also be initiated with only one insolvent company whereas the other affiliates are allegedly solvent (though veritably should all undergo insolvency proceedings).

[152] See Prototype C (*supra* chapter 1 section 1.6).
[153] See UNCITRAL Legislative Guide (note 58 *supra* chapter 2), p. 276.
[154] These matters will be later on discussed (see *infra* chapter 5).

4.3.2 Unique difficulties in strongly integrated MCGs - examples on the international level

In such strongly economic integration, tracking down the mutual transactions and pointing out the specific assets and debts of each component will most likely amount in a substantial loss of money and prolonged proceedings (if at all possible). Consequently, it will dramatically reduce the amount of money available for distribution for the creditors as a whole.

Such were the circumstances in the insolvency proceedings of the *BCCI* group[155]. The BCCI representatives[156] concluded that the two main entities comprising the group were inextricably intermingled. The representatives had difficulties in deciding which asset belonged to which BCCI component and which BCCI creditors and which BCCI debtors were the creditors or debtors of which BCCI company. The manner in which many of the BCCI books had been kept prevented clear answers to these questions and suggested prospects of lengthy and expensive litigation on the path for reaching sustainable resolutions for these difficulties[157].

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[155] The BCCI group collapsed on July 1991 and was closed down by banking regulators. It was a multinational banking organization with operations in approximately seventy countries. The group was comprised of three different corporations: "BCCI Holdings", "BCCI SA" and "BCCI Overseas". BCCI Holdings operated as a holding company in Luxemburg, and owned the two other subsidiary banks, BCCI SA and BCCI Overseas, incorporated in Luxemburg and the Cayman Islands respectively. Each of these subsidiaries operated worldwide through branches and subsidiaries, one of the main branches in the United Kingdom with the preponderant volume of BCCI SA located there (see Re Bank of Credit & Commerce International S.A. (No.10) [1997] 2 W.L.R. 172 (Ch. 1996) [hereinafter: BCCI No. 10]). The BCCI insolvency happened before the EU regulation came into force, and in any case since it was a financial institution it would have not been subjected to the Regulation. Today, it would have been handled according to the winding up directive for credit institutions (Dir. 2001/24/EC of 4.4.2001; [2001] OJ L125/15.23; SI 2004/1045). However, the administration of the BCCI which operated internationally may teach lessons equally relevant for the handling of other business insolvencies (see Westbrook, Lawrence, Jay, and Ziegel, Jacob, S., "NAFTA Insolvency Project" [1997-1998] 23 Brook. J. Int'l L. 8). The proceedings were complex and produced many different episodes of litigation (see especially the Luxemburg winding up order (Bank of Credit and commerce International S.A. (District Court of Luxemburg, 3 January, 1992)) in which the Luxemburg court explained that according to the supervisory commissioner's opinion it is essential to coordinate the liquidation operations by means of cooperation agreements to be concluded with the liquidators of the different foreign entities, subsidiaries and branches, with a view to create a common pot and a common administration [hereinafter: the Luxemburg winding up order]; In re B.C.C.I. S.A. (No.2) [1992] B.C.L.C. 715 in which the English liquidators decided and the English courts determined that the insolvent estate of B.C.C.I. S.A. was to be administered in Luxemburg in accordance with Luxemburg law [hereinafter: BCCI No. 2] and BCCI No. 10 which includes background on the BCCI liquidation and a description of the agreements made between the liquidators. For general background on the collapse of BCCI see Hal s. Scott, "Supervision of International Banking Post-BCCI" [1992] 8 Ga. St. U. L. Rev. 487; Hal S. Scott, "Multinational Bank Insolvencies: The United States and BCCI" in current Developments in International and Comparative Insolvency Law 733 (Jacob S. Ziegel Ed., 1994).

[156] Appointed by the courts in Luxemburg, United Kingdom and the Cayman Islands (*Id*).

[157] See BCCI No. 10 (note 155 above).

In addition to the problem of wasting time and money on the attempt of figuring out the specific ownership of assets and debts, a strongly integrated MCG insolvency case also entails an extreme difficulty to ascertain which parts of the group are truly insolvent and which are not[158]. Based on a balance sheet analysis, some components may show a stronger financial state than others, and some can arguably be solvent at the time of opening the proceedings. However, if the integrity of the corporate form was not properly maintained (or internally respected), assets and debts could have been shuttled and therefore could not be traced back to their 'true' origins; it could not be readily proven that the correct state within the MCG in the time of insolvency is a true reflection of the accurate state of affairs of each company within the group. Or, if the companies comprising the group were highly inter-dependent, an apparently solvent component may in fact be totally dependant on the support of its parent company or other members in the group and could by no means be considered as a stand-alone entity. As a result, it would be difficult or even impossible to determine which members of the group ought to be subjected to an insolvency regime and which are not.

Another difficulty emerging in these cases relates to the veracity and magnitude of inter-company claims. If the group was strongly integrated then inter-company trading or inter-company loans (that in the event of insolvency may become a basis for disputes within the group) may have been conducted with no sufficient records and documentation, as a consequence of the entanglement of the business. In such circumstances, trying to determine who within the group owes what to any of the other members will again entail very expensive and prolonged proceedings with no guarantee of successful ending[159].

In the cases where reorganization may be viable, the disadvantage in conducting separate proceedings is even more pronounced. The incapability to resolve claims and provide responses speedily will have a devastating effect on the possibility to rescue the business[160].

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[158] In the case of *BCCI* mentioned above the majority of the group's components were formally solvent. 'Overseas' was the only insolvent company. Nevertheless, all of BCCI's components were lumped together and were subjected to the insolvency process.

[159] Also see the impact of fraud on the reliability of intra-group claims (note 150 *infra* chapter 5 and accompanying text).

[160] See section 4.2.1 above.

4.3.3 A need for an adequate solution

To avoid overwhelming efforts of entangling the specific businesses and establishing the financial dealings between the members of such groups there is a need for a sort of solution that will allow combining between the assets and liabilities of the components in the course of insolvency[161]. The more 'minor' means for linking between the related companies' proceedings will not suffice in this case. Procedural consolidation applied to the case of MCG on a global level may reduce costs by facilitating jurisdictional disputes[162], yet it cannot solve the problem of entanglement since the rights and obligations of the group's members will be still left intact[163].

4.3.4 National laws' approaches

The problem of handling corporate groups' insolvencies which were conducted as a single entity also arises on the national level with regards to domestic enterprises. In fact, there are jurisdictions under which the court can order that the winding up or reorganization of related companies will proceed on the basis of 'pooling of assets' (or 'substantive consolidation').

American bankruptcy courts have been using their general 'equity powers' provided in the Bankruptcy Code to order 'substantive consolidation'[164]. Yet, it has been observed that this doctrine is still vulnerable, on account of its questionable statutory basis and the fact that it has not been 'formally embraced' by the US Supreme Court[165]. The substantive consolidation's basic idea is to achieve just and equitable results as well as to deal with the inefficiency of handling separate proceedings in cases of highly

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[161] See K. Takeuchi, "Issues in Concurrent Insolvency Jurisdiction: Comments on the Papers by Grierson and Flaschen-Silverman" in Current Developments in International and Comparative Insolvency Law (Jacob s. Ziegel ed., 1994). Takeuchi suggests that consolidated parent-insolvency proceedings in one country running concurrently with the subsidiary's foreign insolvency proceedings will enable to deal effectively with insolvency phenomena involving global enterprises. Takeuchi claims that even without misconduct and commingling of assets prevalent in the BCCI case, a pooling or similar harmonizing arrangements should be strongly supported as a way of dealing with the failure of a multinational enterprise. As it is suggested herewith, such approach should be indeed applied in cases where substantial elements of strong economic integration are present. The scenario of misconduct within the MCG is discussed in *infra* chapter 5 section 5.2.4.

[162] See section 4.2.1 above.

[163] See section 4.1.3.2 above.

[164] See 11 USC, s. 105 (2000). See also Blumberg, Bankruptcy (note 43 *supra* chapter 1), chap. 10 (on substantive consolidation in the US).

[165] See Douglas G. Baird, 'Substantive Consolidation Today' [2005] 1 Bost. Col. L. Rev. 5, 15.

commingled corporate groups by addressing the companies as a single unit in the course of their insolvencies[166].

Using section 271(1)(b) of the New Zealand's Companies Act 1993 the courts there have a wide discretion to order that proceedings of two or more related companies[167] will proceed together as if they were one company[168]. A set of factors though should be considered prior to taking such course of action[169]. Essentially, courts have ordered pooling in cases where management has failed to operate the constituent companies as independent units, with the result that inter-company transactions were poorly documented, not documented at all or used to prejudice creditors of the insolvent company[170]. Pooling orders apply to unsecured creditors only[171].

In the English system, courts do not have an equivalent wide discretion to enforce pooling orders or substantive consolidation, or any legislative guidance as to what is permissible in this regard. On the contrary, English law in principle strictly adheres to entity law[172]. Corporate groups are no exception, and English law has not yet developed a concept of group interest[173], though, English courts have expressed some

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[166] See e.g. Chemical Bank New York Trust Co. v. Kheel (Chem. Bank. N.Y. Trust Co. v. Kheel, 369 F.2d 845, 847 (2d Cir. 1966); In re Commercial Envelope Manufacturing Co., 3 Bankr. Ct. Dec. (LRP) 647, 650 (Bankr. S.D.N.Y. Aug. 22, 1977); Union Saving Bank v. Augie/Restivo Baking Company, Ltd. (In re Augie/Restivo Baking Co.), 860 F.2d 515, 518-519 (2d Cir. 1988)). The equitable grounds for substantive consolidation will be discussed later on in this work (*infra* chapter 5 sections 5.2.2-5.2.4).

[167] The term 'related' is defined in section 2(3) of New Zealand's Companies Act 1993. The definition includes reference to the definitions of 'holding' and 'subsidiary' company, and to the holding of majority shares, but also goes wider than referring only to the formalistic structure of the enterprise by including a fact-based provision where the businesses of the companies have been intermingled (see Farrar, Corporate Governance (note 10 *supra* chapter 3), p. 240-250; Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 618-622). This wide definition goes along with the above suggestion to include within a global approach all variation of enterprises including those not linked via equity (see *supra* chapter 1 section 1.3).

[168] New Zealand's courts are also allowed to give a contribution order (see *infra* chapter 5 section 5.2.4.4).

[169] The four guidelines that the court is directed to take into account are the extent to which the related company took part in the management of the company in liquidation; the conduct of the related company towards the creditors of the company in liquidation, the extent to which the circumstances that gave rise to the liquidation of the company are attributable to the actions of the related company, and the extent to which the businesses of the companies have been intermingled. Finally the court can consider any other matters as it thinks fit (section 272(2) of the New Zealand's Companies Act 1993).

[170] See re Pacific Syndicates (NZ) Ltd (1989) 4 NZCLC 64, 757; re Dalhoff and King Holdings Ltd [1991] 2 N.Z.L.R. 296. See also M. Ross, "Tangled Webs: Unravelling the Strands after a Corporate Group Collapses" I.C.C.L.R. 1992, 3(11), 385-387.

[171] Section 271(1)(b) of the New Zealand's Companies Act 1993.

[172] See *infra* chapter 5 section 5.2.4.2 and 5.2.4.4.

[173] Farrar, Company Law (note 33 *supra* chapter 1), p. 532.

flexibility in this regard in exceptional cases of extreme intermingling[174]. In any case, the approach is not clear[175]. The Cork Report[176] favoured a more comprehensive review of groups within English law, and referred, inter alia, to the pooling order mechanism available in New Zealand[177]. However, the committee refrained from reaching conclusions due to its possible implication to company law, though it expressed the need for a reform to be considered[178].

Where substantive consolidation is allowed, it may include the disregard of inter group claims[179]. In all, the economic integration within the corporate group plays a significant role in the substantive consolidation regime[180].

4.3.5 A stronger need for an interventionist approach on the global level

The international level undoubtedly presents a stronger need for using such a method to deal with cases of strongly integrated MCGs. In such cases the disposition of assets and claims would be more difficult to resolve since assets are located within different countries and proceedings are being handled in competing jurisdictions. Hence, if the MCG was integrated to such a degree that it would be unreasonable to invest the time and money to untangle the separate businesses of each distinct entity it would make sense to embrace a more interventionist global approach that will pool the assets and debts (unsecured debts) of the related companies together, ignoring the apparently artificial structure that divides between the members.

Indeed, this rational led courts and parties involved in several past cases of strongly integrated groups with cross-border dealings to agree on a sort of worldwide 'pooling'

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[174] See Re BCCI (No 3) [1992] B.C.C. 1490. See also Re Exchange Securities & Commodities Ltd (In Liquidation) in which the liquidator proposed a scheme under s. 425 of the English Companies Act 1985 which involved pooling all the assets and then distributing proceeds to creditors according to percentages agreed with them ([1987] B.C.L.C. 425).

[175] See e.g. S. Bowmer, "To pierce or not to pierce the corporate veil- why substantive consolidation is not an issue under English Law" [2000] 15 JIBL 193 (expressing the view that English courts do not follow the US doctrine of substantive consolidation).

[176] Cork Report, Report of the Review Committee, Insolvency Law and Practice, Cmnd. 8558 (1982) [hereinafter: the Cork Report].

[177] *Id.*, at p. 438-439. See further with regard to abuse of the corporate form (and Cork Report's views) in *infra* chapter 5 section 5.2.4.4.

[178] The Cork Report (note 176 above), at p. 439.

[179] According to the American insolvency regime intra-group obligations are terminated by the consolidation order (see Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 26, 402). See also UNCITRAL Legislative Guide (note 58 *supra* chapter 2), p. 279.

[180] Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 419-420; Muscat, The Liability (note 44 *supra* chapter 1), p. 407.

solution. The case of the *BCCI* group exemplifies this approach[181]. The circumstances in the case and the 'model' adopted there demonstrate how parties accepted the necessity of some form of 'cross- border substantive consolidation' as a mean of avoiding expenses and vast difficulties of disentangling intra-group dealing and entitlements. The advantage in terms of cost efficiency was clear[182].

In the case[183], the provisional liquidators devised a number of agreements of which the most significant was the 'pooling agreement'. An improvised 'pooling' solution was designed to avoid the winding up of the group from being lost in a morass of legal argument[184]. The idea was to create a structure under which all BCCI assets would be pooled, hence the tracing and recovery of assets would be a joint enterprise, and creditors in each of the liquidations would receive the same level of dividend from a central pool. One of the liquidations was granted a 'supervisory' role in the sense that it was regarded as the principal proceedings[185]. The determination of the claims of BCCI's creditors were to be carried out in accordance with this supervisory liquidation and most of the proceeds of the realization of BCCI property was to be transmitted to this place[186]. Utilizing a pooling concept encompassing companies situated and incorporated in different countries was regarded as essential in the particular circumstances of the case. It was the initiative of the representatives who concluded that it is inter alia the most efficient approach[187]. The reason was the intertwined scenario with which the representatives were faced and the need to minimize time to

[181] See also substantive consolidation imposed in the case of *Bramalea* - a US – Canadian group (an unreported case in the Ontario Court of Justice; for a description and discussion of the case see R. Gordon Marantz, "The Reorganization of a Complex Corporate Entity: The Bramalea Story" in Case Studies in Recent Canadian Insolvency Reorganizations 1 (Jacob S. Ziegel ed., 1997)). See also Jacob S. Ziegel, "Corporate Groups and Crossborder Insolvencies: A Canada- United States Perspective" [2002] 7 Fordham J. Corp. & Fin. L. 367, 384-385; Mike Sigal ET AL., "The Law and Practice of International Insolvencies, Including A Draft Cross-Border Insolvency Concordat" [1994] 95.

[182] It is a question, though, whether it was a just and equitable approach, at least from the point of view of certain creditors (see *infra* chapter 5 section 5.2.2.3).

[183] See note 155 above.

[184] See the Luxemburg winding up order (concluding that "it results from the submissions of the supervisory commissioner of B.C.C.I. S.A. that the affairs of B.C.C.I. S.A. were inextricably linked with those of other entities of the BCCI group"), and BCCI No. 10 (note 155 above) (referring to the English court hearing of the winding up petition on 2 December 1991 indicating "the truly gargantum task of preserving and realising assets of B.C.C.I. worldwide").

[185] Luxemburg was the country of Principal liquidation (clause 3.1 and 3.11 of the pooling agreement (see BCCI No. 10, note 155 above)).

[186] *Id.*

[187] For the fairness aspect see *supra* chapter 5 section 5.2.2.3.

unpick every claim, and determine who owes what to whom. Most importantly it proved successful, especially in terms of return to creditors[188].

This example reinforces the claim that an interventionist global approach that may treat the different foreign companies as one single entity at least to some extent is clearly needed in order to promote cost efficiency. Fundamentally, this would suggest the application of a 'pooling of assets and debts' mechanism (hereinafter: "a pooling concept" or "a pooling mechanism" or "substantive consolidation" interchangeably), similar to what is being used on the local level in several national law systems (as mentioned above), to an MCG in distress.

4.3.6 Variations of pooling mechanisms

Naturally, 'strong integration' of an MCG could take various forms, which may pose different demands on the cost-efficient insolvency 'system', and therefore raise threats to its successful conduct. Accordingly, the pooling mechanism may be applied in variations so as to accommodate for the particular demands.

Thus, in a 'completely intertwined' scenario, in which both the assets and debts cannot be reasonably ascertained, it would prove efficient to pool both assets and debts together. Accordingly, the proceeds from assets sales will be distributed to the creditors as a whole, or otherwise a reorganization plan will be implemented on the entire estate while dividends will be distributed to all the creditors as if were one single estate.

If, in addition, the intra group claims are untraceable, it should be possible to avoid them in this course of action. It should be noted that in this regard deferring the inter group claims in priority (an approach provided in certain national insolvency regimes that adopted the subordination mechanism[189]) may not suffice. Presumably inquiring the nature of the claims (which is also a related factor in subordination regimes[190]) will

[188] As was explained to the author by Mr Michael Crystal, QC, who ran the joint operation of the BCCI winding up, creditors were paid 70 cents on the dollar, while at the beginning of the process it was predicted that no more than 10% of the claims will be returned to creditors. This outcome is still improving with more recoveries that keep coming in. See also Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 715 at footnote 98 and accompanying text.
[189] See *infra* chapter 5 section 5.2.4.4.
[190] *Id.*

be irrelevant here, since the mere existence and the amount of the claims are uncertain or would demand huge effort to resolve[191].

If, in other circumstances, the assets were commingled but it is possible to determine which creditors dealt with which company, then it should be permissible to pool the assets together and then distribute the proceeds to each company according to a compatible ratio (or to offer separate plans to each entity's creditors). In other circumstances it should be possible to avoid only inter group obligations without pooling the assets and debts.

Finally, if the evidence initially available suggests that a specific company was not strongly integrated with the rest of the group it should be possible to exclude it from the consolidation pro tem with the possibility to link it back up at a later stage as the proceedings progress should evidence connecting this component to the group come to light[192]. An example may be a collapsed retailer conglomerate operating internationally with one of the components structured to be the financing unit. This component was not influenced by the collapse of the 'core business'. Its assets were separated and identifiable. It also had separate creditors (bondholders, for instance). In such circumstances it is not justified in terms of cost-efficiency to pool this company with the rest of the group[193]. There would not be much gain from pooling this unit together with the rest of the group, since it was not part of the main business, and its assets were not commingled with those of the group. In addition, as aforesaid with regard to the non-integrated MCG scenario[194], redundant costs on any sort of coordination with this unit might increase the costs rather than reduce them.

These optional pooling or consolidation orders are 'partial' in the sense that they impose only part of the means available to deal with commingled businesses or apply it only on a specific section of a group[195].

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[191] For a discussion of the difference between the elimination of inter-company claims in substantive consolidation and the equitable subordination judicial technique see Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 442-444. Blumberg notes that the differences may be theoretical, not practical, since in most cases when relegated to a junior rank, the subordinated claim in fact will never be paid.

[192] See section 4.1.2 above.

[193] It may be that the people who ran the group purposely structured the enterprise so that certain parts of it would be 'bankruptcy remote'. It is questionable then whether it would be fair to creditors to recognize such moves in the course of insolvency (see *infra* chapter 5 section 5.2.4).

[194] See section 4.1.2 above.

[195] On the issue of partial consolidation see *infra* chapter 5 section 5.2.2 and 5.2.3.

4.3.7 The implementation of pooling mechanisms in the international scenario

The implementation of a pooling mechanism to the case of strongly integrated MCG demands the use of similar global means as in the case of joint administration that was discussed in respect of integrated MCGs, together with embracing the pooling mechanism universally[196]. Most fundamental is the need for cooperation if separate administrators are representing the companies. The administrators would have to coordinate in some way the unified operation, which is to be applied to the group as a whole.

This may be achieved through the application of an ad-hoc model, such that will initially require the parties to agree on the pooling concept and then to apply it and operate the process co-ordinately[197]. However, in a substantive consolidation case the costs of such approach are considerable[198]. To negotiate such complex agreements from scratch and consequently coordinate tightly linked proceedings in which assets are pooled together and claims are jointly processed is obviously a challenging and expensive task. A pooling operation is rather prone to disagreements and is naturally complicated. Therefore, predefined modes for cooperation and coordination, accompanied by guidelines on the implementation of a pooling concept, will simplify the process immensely.

Moreover, and especially in a case of a 'complete' substantive consolidation (in which all assets and debts are mixed and one distribution or one scheme of arrangement will be offered to all creditors together) such cooperation will need to be supported by a supervisory role to one specific authority and by putting the entire proceedings under a single law regime[199]. Otherwise, it will be extremely complicated to treat the companies as one unitary entity and to distribute dividends to all creditors as if they were all related to a single entity.

If the consolidation is partial in the sense, for example, that the assets are pooled but the proceeds are to be distributed separately by each entity to its own creditors, and the constituent companies had significant autonomy, then the distribution can be governed

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[196] See section 4.1.3.6 above.
[197] As was actually done in the *BCCI* insolvency (see section 4.3.5 above).
[198] See the discussion about Ad Hoc solutions in *supra* chapter 2 section 2.4.2; See also section 4.1.3.4 above.
[199] Indeed, in the case of *BCCI* it was agreed that the entire proceedings will be supervised from one specific place (Luxemburg) (see section 4.3.5 above).

by each country's own insolvency laws. Whichever be the case, supervision would be most profitable, since actions being taken by any entity within the group and the way in which each part of the business is handled through the course of the insolvency process, has significant influence on the final outcome for the entire group.

As was suggested above, in the integrated centralized MCG cases[200], a centralized approach (in the course of the MCG's insolvency) will be profitable[201]. Here (in the strongly integrated scenarios), this is even more pronounced. Thus, to avoid the massive expenses and the time it will take to operate a worldwide insolvency of essentially one entity but such that is located in different states it will usually be most advantageous to place the operation in a single place[202]. Accordingly, a model that provides rules of international jurisdiction and choice of law rules will facilitate overcoming problems and costs resulting from the need to agree initially on the pooling concept itself. A specific court can be authorized within such a global model to examine the facts and determine the appropriate solution for the case, thus dismissing the need to reach an initial agreement.

In the scenarios where it will be impossible to locate such a place in which to centralize the process or to supervise it[203], other means can be applied, as were proposed above[204]. In any case, cooperation and coordination between the foreign proceedings will need to encompass a mechanism for facilitating the joint realization of assets and distribution of proceeds.

4.4 **Summary**

It was apparent from the above examination of the economic efficiency goal, that a global approach can offer a range of suitable solutions for the particular challenges posed by the MCG insolvency. Certain MCG insolvency Prototypes will suggest that joint administration will be most profitable, either for the purpose of a worldwide reorganization or a global sale of assets. Linking between affiliates in these cases will be essential in order to increase revenues and reduce costs. Conversely, a territorial

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[200] See Prototype C (*supra* chapter 1 section 1.6).
[201] See sections 4.1.3.6- 4.1.3.8 above.
[202] In the case of *BCCI* (note 155 above) the operation took place in various states ending up with expensive and time consuming operation (see section 4.2.3 above).
[203] See *infra* chapter 7 section 7.4.
[204] See section 4.1.3.5 above.

separable approach may in fact fail to achieve the cost efficiency goal. It was also clear that various alternative solutions are needed and a 'one size fits all' approach is disadvantageous.

Bearing the 'corporate form' in mind, it was also shown that in many cases 'procedural' linkage will suffice. Using the Prototypes proposed earlier in this work[205], we distinguished between various possible scenarios, so that our solutions will match the particular demands of the case. Accordingly, only in those cases depicted by Prototype C (the strongly integrated collapsing MCGs), a sort of 'lift of the corporate veil' was necessary. In addition, several levels of pooling mechanisms were suggested, to make this tool less extreme and matched to the specific case.

Other insolvency goals will now need to be explored to see how they fit with the solutions proposed and whether a global approach is advantageous in these respects too. For instance, whether substantive consolidation will achieve fairness or whether global mechanisms as such can be regarded as clear and predictable.

[205] See *supra* chapter 1.

Chapter 5

Fairness

5.1 Ensuring due process and meeting legitimate expectation regarding jurisdiction

5.1.1 Introduction

As was suggested[1], economic efficiency considerations may justify a global approach which may impose a centralized process for the entire group's insolvency proceedings for those MCGs that were centralized and integrated[2]. An alternative solution was to supervise the entire process from a single location while handling local proceedings against subsidiaries[3]. The general idea was that a single location will be acknowledged as a centre for the entire estate in order to promote the efficiency of the proceedings in the appropriate MCG insolvency scenarios[4].

However, as our discussion here revolves around fairness, it is questionable whether such an approach is able to enhance this goal. It will be argued herewith that a global approach though encompassing certain risks can ensure the protection of creditors' rights, particularly upholding rights of due process and meeting expectations regarding the handling and the location of the international insolvency[5]. Still, this outcome will only be possible if thorough consideration will be given to certain essential characteristics of the approach which will be introduced in the following discussion.

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[1] See *supra* chapter 4 section 4.1.3.6.
[2] As exemplified by Prototype A (*supra* chapter 1 section 1.6).
[3] In cases of integrated coordinated MCGs (Prototype B in *supra* chapter 1 section 1.6).
[4] See *supra* chapter 4 section 4.1.3.8. The factors to identify the group centre will be discussed later on in this work (*infra* chapter 7).
[5] See *supra* chapter 3 section 3.3. The other aspects of fairness will be explored in subsequent sections of this chapter.

5.1.2 Considering creditors' expectations and interests with regard to the insolvency location

Creditors' expectations are fundamental to the issue of international jurisdiction in which to handle cross-border insolvencies[6]. Clearly, creditors should be able to foresee where the insolvency of a company is going to take place and calculate their risk accordingly[7]. In addition, substantial legal rights (such as the ranking of claims) might be affected by changing the location of the insolvency proceedings[8].

One view may suggest that as a rule of thumb the location of proceedings of any member of a group (and the corresponding law and forum that should supervise the process) should always be determined for each company separately. That is, without any considerations of the connections a particular member may have had with another related company or with a 'group'. Supposedly (and according to the notion of separate legal personality), creditors are related to a certain company and not to a group of companies. Therefore, they expect to enforce their rights upon it and to open insolvency proceedings in the place of its main operations regardless of any possible links to some 'group centre'. In any case, their rights should not be prejudiced because of any 'group' considerations, as it will not be fair to them. Thus allegedly, in the name of 'unification' a centralized approach may collide with creditors' expectations and may not fit with their views regarding the forum that should supervise the process[9]. However, it could be that creditors may have actually dealt with a subsidiary as if it was the entire group or otherwise were given the impression that the whole weight of the group is behind the specific subsidiary they were dealing with. In such cases, treating the insolvent subsidiary separately will actually discord with its creditors expectations.

Which ever is the case, it is clear that one obstacle that a simplified 'segregating' approach will have difficulty to face is that different creditors involved with the group

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[6] Indeed, the EU Regulation applying the idea of having one centre for single debtor worldwide insolvency stresses that a major factor in determining where the main proceedings of the debtor should be taking place is third party expectations (see note 95 *supra* chapter 2).

[7] See *Id.*

[8] This issue will be discussed in section 5.2 below.

[9] See the arguments that were put in the *Daisytek* case (section 5.1.4 below). And, see the ECJ decision in *Eurofood* (and the Opinion of the Advocate General in the case) emphasizing that main insolvency proceedings can be placed in a place other than where the subsidiary's registered office is located only when this place is ascertainable by third parties but not merely because a controlling entity is located there (see *supra* chapter 2 section 2.4.3.3; see further in section 5.1.4.below).

may have different interests and different expectations regarding the location in which a certain member's insolvency will be handled. Creditors of a certain subsidiary may wish that the company will be separately managed, while the creditors of other related companies would expect all proceedings to be conducted jointly since according to their view they were given the impression that they deal with the entire group and not only with a well bounded part. Moreover, elements of both types of dealing could be found among creditors of the same company within a group. In fact, applying the simplified rule of treating each company separately without taking into account the group context may result in significant unfairness towards the majority of the MCG's creditors.

Furthermore, more often than not, a thorough examination of the facts pertaining to a group's insolvency which was integrated may reveal that it was indeed clear to 'locally oriented' creditors (of local subsidiaries) that they dealt with a member which was part of a group. Evidently, they may have negotiated with a holding company located elsewhere, or their contracts may have been subjected to the laws under which the parent company was operating. They may have supplied products to other members of the group or had other dealings with the various parts of the business. They may have received a guarantee from the parent company, and so on. Examining the way the group was operating and the way creditors were doing business with the corporation will, therefore, most likely point out to a single location from where the group was managed and in which insolvency proceedings can be handled or supervised (if it was an integrated MCG). It could be conceptualized that the genuine expectations of creditors should fit with and stem from the way the MCG was actually structured and managed. Therefore, focusing on the 'business reality of the MCG' could assist the court in verifying creditors' expectations[10]. In addition, the court would need to 'step back' and look at the way creditors dealt with the group from an objective perspective (using the notion of what a 'reasonable creditor' would have expected in the specific

[10] See, for instance, the case of *Bramalea* group (note 181 *supra* chapter 4) in which the court examined evidence and concluded that US creditors of US affiliates were aware of the fact that the group was managed in Canada, as they negotiated their loans with officers of the Parent in Toronto through sessions that had taken place in Toronto. Furthermore, many of those loans were in fact supported by the parent company's guarantee. Indeed, the rental markets for U.S. properties held by the U.S. affiliated were local, and their day-to-day operations were carried out and managed locally, but large strategic decisions were likely dealt with in Toronto (see R Gordon Marantz, "The Reorganization of a Complex Corporate Entity: The Bramalea Story" in *Case Studies in Recent Canadian Insolvency Reorganizations* 1, 18 (Jacob S. Ziegel ed., 1997).

scenario) rather than basing its decision on the expressed subjective beliefs of creditors[11].

There could also be situations where the creditors did not know precisely with which entity within a group they were dealing and where it was incorporated or held its main operations. Indeed, the increasing complexity of a technologically advanced business world (where enterprises may operate through a baffling network of corporate relations) leads to greater difficulty in establishing which company within the enterprise is actually at fault, making it hard even for more sophisticated creditors to ascertain the proper entity against which to open proceedings. In cases of small unsecured creditors there is even a greater difficulty in clearly identifying the corporate actor with whom one was contracting or suffered injury[12].

All in all, it seems that a 'global look' on the situation, one that takes into account the various entities and creditors involved, is for the creditors' benefit. It is only when considering all relevant parties' expectations and interests that a just and fair solution could be devised. A particular court will then be able to evaluate all relevant interests and expectations and determine whether the creditors as a whole could have ascertained a particular location as the centre of the entire group, so that it will be justified to conduct the various proceedings of the relevant entities from such identified location, rather than handling separate processes in each country hosting a subsidiary. Alternatively, the court may conclude that creditors dealt with their debtor on a separable basis with no regard to its relations with the group, consequently allowing for the distribution of the proceedings.

As pointed above, in many cases of integrated MCGs it will be evident that creditors knew they were dealing with a member of a group, and they actually had relations with other members of the group or with the debtor's parent. Yet, in certain other cases, it could be realized that creditors may have dealt separately with an autonomous subsidiary[13], even if this subsidiary was a part of a single unitary business integrated within a group. In those particular circumstances where local entities had significant degree of autonomy (which was reflected in the way creditors have dealt with it), it is

[11] Such beliefs may veritably be driven by creditors' interests regarding the forum - 'forum shopping' (see *infra* chapter 6 section 6.1).
[12] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2314.
[13] See Prototype B (*supra* chapter 1 section 1.6).

reasonable to assume that such creditors expect to have the main process against the particular entity in the country in which it operated. Hence, 'shifting' the proceedings to a different location can be regarded as unjustified in these scenarios. Nonetheless, as the entire MCG is still an integrated enterprise the creditors as a whole may benefit from the alternative sort of centralization, that is subjecting the entire process to a common direction.

5.1.3 Involvement and adequate representation in an MCG insolvency process

The actual course of insolvency within an MCG may be relevant not only to members directly under the proceedings but also to other affiliates which may be located in other states. It is very likely that the financial situation of one member may influence another, that there may be mutual claims or that there may be questions of group liability. These affiliates' insolvency proceedings may take place concurrently in different locations, or alternatively they may not be under insolvency at all at that time. In this type of cases it is particularly important that the wishes and views of creditors of affiliated companies will be heard. In this respect, a centralized approach that gives authority to a certain court to look at the group insolvency as a whole may ensure that creditors of related companies will be given a stage in which they will present their views and that it will be taken into account.

On the other hand, a centralized approach may present a risk of neglecting creditors and therefore compromising their involvement and representation rights. Apparently, handling the proceedings of each entity separately and locally is better suited to ensure the participation of creditors in the process of the subsidiary, to which they directly relate, in the most easiest and accessible manner. Conversely, if a subsidiary's insolvency is handled in some externally identified centre, certain creditors that might not have the sufficient means to embark on a multinational legal expedition (or from any other reason) may not be consulted even when a decision that pertains to them is made. It could involve, for instance, the decision of opening proceedings in a specific location as well as the ongoing handling of the proceedings once they were opened. In fact, it may also be the direct consequence of a central administration that lacking any explicit guidelines and directions is more likely to be concerned with a certain party's needs and expectations while forsaking those of other, perhaps more 'remote' creditors.

This scenario also poses the risk of culminating into a de facto substantive consolidation mostly for the sake of convenience of the administration rather than any substantial reason[14]. Thus, separate entities in essence may eventually be lumped together without giving full consideration to the interests of the entire multitude of creditors.

Furthermore, as was indicated with regard to single debtor cross- border insolvencies and the use of the EU Regulation, there are practical disadvantages for foreign creditors due to language, distance and the differences between procedural requirements imposed by states' insolvency laws[15]. Applying this notion to the case of insolvencies within MCGs suggests that there is a 'double' barrier to foreign creditors when they relate to a separate entity.

The problem of inadequate representation and the need for active involvement increases since there is a potential conflict of interest in supervising an MCG process in a unified manner. The appointee or appointees, if handling the whole proceedings together, may be representing different interests. This problem is surely more pronounced when a single appointee handles all the proceedings, but it is also quite prominent when there are several appointees handling the whole group. In such situations, the appointees are on the one hand operating for the benefit of the group as a whole (and the creditors in general) but on the other hand are dealing with separate entities that might have contradicting interests[16]. In any case, a single appointee or a closely tied group of appointees can result in an all too 'cozy' situation, with the potential of neglecting certain creditors' interests.

A global approach seems necessary in order to safeguard the rights of involvement and adequate representation, when we are dealing with an integrated MCG, as this requires for someone in this entire process to see and to hear all relevant voices and to be responsible to protect all interests. However, the inherent risks of a centralized system as introduced above are undeniably relevant to the application of a proper approach.

[14] As was proposed earlier (*supra* chapter 4 section 4.3) substantive consolidation will be justified only in the situation exemplified by Prototype C (*supra* chapter 1 section 1.6). Additional relevant factors and scenarios in which the corporate form may be ignored will be discussed in sections 5.2.2- 5.2.4 below.

[15] See I.F. Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL International, Cross-Border Insolvency, a Guide to Recognition and Enforcement 15, 41.

[16] Unless full substantive consolidation is applied (see *supra* chapter 4 section 4.3).

Hence, if a proposed approach is to be proved justified, it will need to provide mechanisms to overcome these potential flaws.

5.1.4 The threat to creditors rights under current regimes- examples on the international level

Recent cases of insolvencies within MCGs demonstrate the threat posed to the goal of fairness, in the lack of explicit means for dealing with MCGs' insolvencies. Examining the course of such processes shows either insufficient consideration to rights of all relevant creditors (pertaining to jurisdictional issues of the MCG insolvency process), or otherwise increased unwillingness on their part to support a unified process for the group (even though such approach would have been for the benefit of the group as a whole) as they fear to be forsaken in the foreign process handled in a 'group centre'.

Typically in these cases, parties and courts are driven to try and devise practical solutions, to enable efficient liquidations or restructurings of MCGs as it is only natural that these cases need an efficient mechanism to be able to reach a successful conclusion. However, lacking sufficient structured guidelines, courts are sometimes inclined towards the direction in which local creditors have pulled: either to protect creditors in the 'territory' sacrificing the global economic consequences it may have, or enforce control over foreign members of a group even in cases where it may not fit creditors' expectations. Creditors themselves have been on some occasions reluctant to accept any 'joint process' as they could not be certain that their rights will be preserved during this course of action.

The *Eurofood*[17] subsidiary company was incorporated in Ireland; however it was part of an Italian group that collapsed (*Parmalat*[18]). Hence, the Italian administrator appointed to restructure the Italian group wished to subject the Irish company to Italian jurisdiction in order to facilitate the operation[19]. However, creditors of the Irish subsidiary were reluctant to accept that. They feared the consequences of such an act

[17] See Eurofood IFSC Limited [2004] B.C.C. 383.
[18] Note 51 *supra* chapter 4.
[19] The Italian administrator asked the court in Parma to declare the company insolvent. The Parma court accepted the petition and placed the company under Italy's jurisdiction (see Eurofood IFSC, Re (Trib (I) 19 February 2004 [2004] I.L.Pr.14) even though provisional liquidators were previously appointed by the Irish court.

and could not be confident that their rights would be adequately safeguarded. They were concerned, for example, that the assets of the Irish subsidiary would be lumped together with those of the rest of the group[20]. They preferred to have control on the subsidiary's future and thus strove to place its proceedings in Ireland. Consequently, two main parallel proceedings were opened.

Indeed, the Irish court in its decision to approve the appointment of Irish provisional liquidators to the subsidiary[21] emphasized the Irish company's creditors' expectations and how they viewed the company's location. The court held that it was clearly Ireland in which the creditors expected a default to be handled as creditors were dealing with investments issued in Ireland and subject to Irish fiscal and regulatory provisions[22]. The Italian court, on the other hand, in its decision to open main proceedings in Italy (in relation to the same company)[23] seemed to have focused more on the entire group's operational structure and the Irish company's position within it. It pointed out the fact that the Irish company carried out activities instrumental to the Italian parent's group, that it was ancillary to the parent, that the parent guaranteed all transactions and that all operating and policy decisions were made from Italy[24]. Clearly, the courts lacked structured guidelines to follow in determining on the proper jurisdiction where it is a case of group of companies. Consequently, each pulled to the other direction to meet the interests of the local creditors or the local administrator.

The decision of the ECJ in the case has not resolved this difficulty. It has not provided means aimed at appreciating the benefits for the stakeholders of the group as a whole and clarifying how the various relevant interests can be safeguarded and taken into account. Rather, it entrenched the idea of ascertaining jurisdiction for each subsidiary separately[25], apparently focusing on the ascertainability to third parties of the particular company[26].

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[20] See "Italian and Irish courts clash over Parmalat", GLOBALTURNAROUND, April 2004, issue 51, p. 3.
[21] Eurofood IFSC Limited [2004] B.C.C. 383.
[22] *Id.* Moreover, it stated that no adequate notice was given to the company's creditors and to the Irish provisional liquidator on the Italian hearing.
[23] Eurofood IFSC, Re (Trib (I) 19 February 2004 [2004] I.L.Pr.14.
[24] *Id.*
[25] Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397, at paras. 26-37.
[26] *Id.* Though apparently the court has not excluded 'parental control' over a subsidiary as a relevant factor in determining the proper jurisdiction (see *supra* chapter 2 section 2.4.3.3).

The *Parmalat* case's complexities go beyond the EU Regulation's 'borders'. A Cayman Islands court's decision also in a matter related to the Parmalat group[27] reflects a similar consideration of that of the Irish court mentioned above. Cautious of not depriving creditors of the local subsidiary of their rights[28], the court refused to subject this company to the Italian administrator control, approving the appointment of separate representatives although conscious of the effect it might have on the cost-efficient operation of the whole process. The main reason for the court's decision was the fact that this was the wish of third party creditors (i.e., non-related creditors) - to have separate representatives and to conduct a local process- and because of severe concerns about the administrator's ability to act in the interest of the subsidiaries' stakeholders. Indeed, the way the Parmalat's administration was being handled has been criticized of being too nationalized, focusing on seeking 'an Italian solution', lacking a sufficient international perspective[29]. Creditor groups involved in the Parmalat process 'raised eyebrows' with regard to the sort of representation provided for such a large scale, international case[30]. However, such solution as was chosen by the Cayman Islands' court (segregation in handling the group's process) poses a threat on the chances to engineer a global rescue plan and in any case has probably increased costs and complicated the proceedings. Furthermore, it seems that the court (although stating that it was mainly concerned with the creditors' wishes) considered only part of the interests involved[31], and did not appreciate the fact that creditors who were not present at court and may have belonged to other members of the group may have had an interest in promoting a centrally based more efficient process, supervised by a single administration.

In the *Daisytek* case[32], an entire group (the European part) was placed under administration in one single place; however this resulted with much contest from the part of the 'local' subsidiaries. There was a strong debate regarding the reasoning

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[27] The Cayman Island's court decision (note 23 *supra* chapter 4).
[28] *Id.*, at p. 8-12, 21- 23.
[29] *See* GLOBALTURNAROUND, January 2004, issue 48, p. 3; GLOBALTURNAROUND, February 2004, issue 49, p.4.
[30] *Id.*
[31] The court considered the position of the Noteholders of the three Cayman Islands subsidiaries at stake (Parmalat Capital Finance Limited, Food Holdings Limited and Dairy Holdings Limited), while giving less weight to the views of related company creditors (The Cayman Islands court's decision, *supra* note 23, at p. 15). It seems that it did not take into account, though, potential views of other external creditors of other members of the group.
[32] Daisytek- ISA Ltd, Re [2003] B.C.C. 562 (Ch D).

given by the English court when it opened the proceedings against each member of the group, and with respect to the representation of the subsidiaries in this process[33]. It seems that a practical solution was imposed but with much confusion and discontent on the part of foreign members of the group[34]. Looking at the reasoning of the English court's decision it seems that creditors' expectations with regard to the local subsidiaries' place of main interests were considered[35]. Furthermore, as was noted earlier, prima facie the decision was grounded on finding COMI separately for each subsidiary[36]. Nevertheless, it appears that the decision was much influenced by the group situation. The court looked at the group's operational structure, and the way it was managed[37]. It also seems that the English administrator was mainly focused on devising an effective solution to the Pan-European group[38]. The French and German courts in first instances, on the other hand, considered the respective companies as locally situated, even though they were controlled by a parent company in the UK[39]. These contradicting views exemplify that an approach that would expressly address the situation of a group will make this issue much clearer, and enable the court to use the 'high road' to reach its decision. In addition, this de facto joint administration

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[33] See C. G. Paulos, "Zustandigkeitsfragen nach der Europaischen Insolvenzverodnung" International Insolvency Institute (http://www.iiiglobal.org/country/germany/insolvenzverordnung.pdf). See also Bob Wessels, "International Jurisdiction to Open Insolvency Proceedings in Europe, In Particular Against (Groups of) Companies" Working Papers Series, Institute for Law and Finance, Johann Wolfgang Goethe University, http://www.iiiglobal.org/country/european_union/InternJurisdictionCompanies.pdf.

[34] However, progress in this regard has been made. For instance, when the Munich Court in first instance decided in another case to place insolvency proceedings against an Austrian subsidiary in Germany (where the parent company was situated). The Munich court found that all the headquarters functions of the Austrian subsidiary were carried out at the premises of the parent in Germany. The court also expressly followed the decision of the English court in Daisytek, and in that contributed to the development of a consistent EU-wide interpertation of the EU Regulation (see Amtsgericht (Munich) Hettlage-Austria (Unreported, May 4, 2004) (Germany); G. Moss, "Daisytek followed in New German Case", Insolv. Int. 2004, 17(10), 141-142). Another step in this direction was recently taken by the Nanterre court (France), appointing French administrators for several subsidiaries of the Emtec MCG incorporated in different European countries (see note 75 *supra* chapter 4).

[35] Daisytek- ISA Ltd, Re [2003] B.C.C. 562 (Ch D), at p. 7-8.

[36] See *supra* chapter 4 section 4.1.3.8.

[37] The court stated for instance that: "the evidence shows that the trading companies in the group are managed to a large extent from Bradford and that they are managed and controlled as a group so that the activities of the group companies throughout Europe are co-ordinated by the head office in Bradford". It also indicated that the English parent, who performed the head office function for the group gave various guarantees to major suppliers and trade creditors of its subsidiaries (Daisytek- ISA Ltd, Re [2003] B.C.C. 562 (Ch D)., at p. 2).

[38] The English appointee attempted to facilitate a pan-European restructuring by opening proceedings for the different companies comprising the European division of the group at the same place (the UK). The idea was to administer the proceedings jointly, instead of having a 'patchwork of different cases in different countries' (see Stephen Taylor, "Daisytek chain reaction", *GLOBALTURNAROUND*, July 2003, issue 42, p. 10).

[39] In re Daisytek ISA Ltd (Tribunal de Commerce, Cergy-Pontoise, 1 July 2003); In re Daisytek ISA Ltd (Dusseldorf County Court, 19 May 2003; 10 July, 2003).

centralized in the UK with no clear guidelines as to its operation contained a potential danger of prejudicing creditors' rights, for example in progressing from a parallel administration to a sort of substantive consolidation.

A similar UK-based insolvency process for a European group of companies was commenced for the British car maker *MG Rover*[40]. Here as well, this was done taking into account the 'risk' of provoking resentment overseas by local insolvency practitioners or stakeholders claiming that the subsidiaries were national entities who would sell cars on to dealers in the countries concerned[41].

It is submitted thus that recent experience reinforces the need for an expressed authority within a model for cross border insolvency to centralize groups' proceedings while providing clear guidance (as to where such approach is appropriate) and sufficient rules that will accompany such authority and will be able to consider the interests of all relevant creditors.

5.1.5 The appropriateness of a global approach

It is evident that a global approach has the potential of promoting fairness (particularly upholding rights of due process and meeting expectations regarding the handling and the location of the international insolvency) in that it will enable a specific forum to consider all creditors' interests and expectations relevant to the group's insolvency. Having such a 'global look', taking into account the entire picture will result with the fairest outcome. In all, the advantage of such an approach is that in the appropriate cases (in the integrated MCG cases) it can better reflect the economic reality of the business. A global approach will be able to project the way the MCG operated and the way it had dealings with creditors in its ordinary course of business onto handling of its insolvency. Therefore, by mirroring the business activities prior to the collapse it will better accord with creditors' expectations. In its core, a global approach subjects the entire MCG insolvency process to a single direction. Furthermore though, it strives to handle all proceedings in a single location thus facilitating unification and an appropriate 'view from above' on the entire process.

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[40] See the administration proceedings in the Birmingham District Registry of the High Court (the judgment handed down on May 11, 2005 is available on the EIR Database at www.eir-database.com).
[41] See *GLOBALTURNAROUND,* "MG Rover, Europe's biggest COMI", May 2005, issue 64, p. 3.

Yet, as a global approach is expected to reflect the actual characteristics of the distressed MCG prior to its collapse and creditors' expectations regarding the location of the insolvency process, it must acknowledge the fact that even in the case of an integrated MCG, various operational structures may be involved[42]. Accordingly, in terms of fairness, it might not be appropriate in certain cases to place all the companies' proceedings in the identified centre for the entire group. This conclusion is in accord with our discussion regarding economic efficiency, as it refers here to the cases where local subsidiaries were significantly autonomous[43]. The approach should thus provide that if indeed a local subsidiary of an integrated MCG operated with a substantial autonomy which in turn was reflected in how creditors dealt with it[44], its proceedings should be handled separately and locally. However, it should still maintain that such local proceedings will be subjected to the process conducted in the MCG's centre. This flexible methodology will make it possible to contain both the cases in which all subsidiaries should be located at the MCG's centre and those other cases in which certain subsidiaries are in fact locally separated. Thus, it will overcome the short handedness of the 'black or white' solution imposed via the EU Regulation. Consequently, as was also provided where discussing economic efficiency considerations, in cases involving local proceedings of autonomous subsidiaries the designated venue should be given the supervisory role over the entire process[45].

As will be suggested below creditors of relevant affiliated companies should be notified about what is happening in the central process. In any case, bearing in mind the complex scenario of insolvency within an MCG, it should be provided within a global approach that creditors' wishes should be considered even if they are not physically present. The benefits or possible unfairness that will be the result of a decision to centralize the proceedings or rather to have separate processes should be examined with as much consideration as possible of the creditors in general. Thus, the consequences of judgments regarding a particular subsidiary upon stakeholders of other related companies should be taken into account. It should hence be examined what the majority of the subsidiary's stakeholders expected in terms of unification and

[42] See Prototypes A-D (*supra* chapter 1 section 1.6).
[43] As in Prototype B (*supra* chapter 1 section 1.6).
[44] See section 5.1.2 above.
[45] See *supra* chapter 4 section 4.1.3.8.

centralization, but also (as another relevant factor in determining on such mechanisms) the expectations of the majority of creditors as a whole.

A tool (of 'last resort') that local courts (of local affiliates) will be able to use is the public policy notion (in a broad sense, namely with respect to affiliate companies too). Thus, in cases of infringement of due process local courts can refuse to recognise the central proceedings[46].

In this process of evaluating creditors' wishes, a fair balance should be made between the various interests. The nature of claims is also relevant, namely whether third party creditors' wishes are at stake or those of creditors who are also shareholders or connected to the former management of the company, embracing the idea that related creditors should be entitled to less weight in the overall equation[47].

In addition, in order to diminish the problem of creditors' difficulties in ascertaining which corporate entity they were dealing with and where was its proper location (for the purpose of insolvency), a global approach should set up rules for transparent representation of a company's centre of gravity and its relationship with the rest of the group[48]. Namely, there should be an explicit reference within the company's documents as to whether it is a company which is integrated with other affiliates and (if indeed this is the case) where the centre of the MCG is located (in accordance with the definition of such location in the global model[49]). This should include a positive duty cast on each company (which is a member of an MCG) to proclaim this on its business documents. Furthermore, the company's auditors should be asked to validate the accuracy of those representations on an annual basis, and report whether indeed it matches the way the business is operating. Such representations can be also included

[46] See the ECJ decision in *Eurofood* which stated that the right to be notified of procedural documents and more generally the right to be heard (however- regarding proceedings held against the particular subsidiary) are considered as fundamental rights, thus Member States may refuse to recognize proceedings that were opened in breach of this rights on the grounds of the public policy exception provided in the EU Regulation (Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397, at paras 60-68).

[47] This was also the view expressed by the Cayman Islands' court considering Parmalat's members' wishes presented to it with regard to the appointment of provisional liquidators to the subsidiaries in the Cayman Islands (the Cayman Islands' court's decision (note 23 *supra* chapter 4), p. 9-10).

[48] Such rules can be regarded as a minimum requirement under national company or insolvency laws to ensure the information is available to creditors, ex-ante.

[49] See *infra* chapter 7.

in various transactions' documents in which the company is involved[50]. It may also incorporate statements and prohibitions on any actions taken by the company or its affiliates which may result in the alteration of the above location to another jurisdiction or the position of the company within the group. This will help in robustly protecting creditors and in avoiding the potential gap between 'impression' and 'reality' of the companies' operations and their effects on jurisdiction matters[51]. A lack of adequate representation regarding the MCG's centre's whereabouts or adequate notification regarding alterations in this location should result with the debtor being prevented from arguing that a certain place was indeed its proper centre[52]. Notwithstanding the above, it should be appreciated that ascertainability and creditors' expectations are not stand-alone factors justifying or denying unification between affiliates' insolvency proceedings. There are other relevant goals that should be considered[53]. As mentioned above, certain creditors (involuntary creditors in particular) are in any case unable to foresee the way the company or the MCG operated and could not ascertain its proper jurisdiction[54].

Even if the circumstances provide that a fully centralized process is compatible, it should still address the issue of representation and involvement of foreign creditors in the centralized process. Thus, a global approach should ensure that courts will be presented with the entire picture when considering the path an MCG insolvency process should take or with regard to other matters pertaining to the insolvency (this may include the decision on the location of proceedings, the administration and

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[50] For instance, in structured finance transactions involving special purpose vehicles (SPVs) (see *GLOBALTURNAROUND*, "Europe leads world in Forum Shopping", June 2003, issue 41, p. 2; see further on the issue of SPVs in the context of abuse within the MCG in section 5.2.4.3 below).

[51] In a similar way, with regard to international migration of the registered office of a company, the English Company Law Review (CLR, Completeing (note 32 *supra* chapter 1), paras 11.54-11.70 and CLR, Final Report I (note 32 *supra* chapter 1), Ch. 14) proposed that tranfer of the registered office should be permitted, but subject to adequate safeguards for shareholders and creditors, because the change in the jurisdiction in which the company has its registered office changes the internal company law to which the company is subject (according to English private international law). Inter alia, the directors would have to declare the company to be solvent and able to pay debts as they fall due for the twelve months after emigration, together with providing a detailed proposal for the alteration of the registered office. The entire proposal to permit the migration of the registered office was rejected on grounds of feared loss of tax revenues (Modernising Company Law, Cm. 5553-I, July 2002, p. 54-55); see also Davies, Gower company law (note 33 *supra* chapter 1), p. 118-119).

[52] See the decision in Ci4net.com in which the judge was not prepared to accept that the COMI moved inter alia since little or no contact was made by the companies to inform its creditors of the alleged change (Ci4Net.com. Inc [2005] B.C.C. 277 (Ch D); *GLOBALTURNAROUND,* "US company fails to escape Euro Regulation", July 2004, issue 54, p. 1).

[53] See the discussion in following sections of this chapter, as well as *supra* chapter 4 and *infra* chapter 6.

[54] See note 12 above and preceeding text.

supervision over the process or the decision on any sort of consolidation to be imposed, and so on). The court should be able to take into account interests of all creditors relevant to the process, appreciating the significant consequences of particular decisions on creditors' rights[55]. This should include foreign creditors, as well as creditors of affiliates who are relevant to the process (in the sense that they may be integrated within the group or have other claims that should be considered[56]) (hereinafter: relevant affiliates).

For that purpose, courts and administrators should be responsible for notifying creditors and other administrators of relevant affiliates about the opening of proceedings against a particular member within the group and of any relevant court hearings and orders[57]. The parties opening the case should provide full information and evidence in respect of the MCG scenario, its way of operation and the financial status of other relevant affiliates. Information should also include various matters pertaining to the insolvency that may affect other affiliates, such as decisions on the location of the proceedings and hearings that are going to take place regarding the application of a pooling or a contribution mechanism[58]. Creditors of relevant affiliates should also get access to proceedings being located in a foreign country and get equal treatment in terms of lodging claims to a joint administrator[59] and voting on a global plan or other sort of insolvency operation (if indeed any sort of consolidation was actually applied).

Finally, a global system should provide rules to ensure the objectivity of the administration supervising a group's process and its capability to represent a variety of interests relevant in the case of MCG. In this respect, an international firm with an international perspective may be more adequate to deal with MCG cases (than a

[55] See the case of TXU in which Mr Registrar Baister considered the possibility that there would be cases where the court would require evidence detailing extensively the circumstances in which the jurisdiction (in that case- the UK) has come to be or is said to be the centre of main interests of a foreign company in order to avoid prejudice of creditors' rights (TXU Europe German Finance BV, Re [2005] B.C.C. 90 (Ch D); see also G. Moss, "Creditors voluntary liquidation for foreign registered companies" Insol. Int. 2005, 18(1), 12-13).

[56] Such as claims pertaining to group liability issues (see section 5.2.4 below).

[57] Similar to the provisions in the EU Regulation with regard to foreign creditors of a single debtor (see Articles 40-42 of the EU Regulation, note 75 *supra* chapter 2), in the Model Law (note 143 *supra* chapter 2), Article 12) or in the ALI Principles (note 189 *supra* chapter 2), Procedural Principles 13 and 16.

[58] See *supra* chapter 4 section 4.3 and section 5.2.4 below.

[59] Similar to the provision in the EU Regulation with regard to foreign creditors of a single debtor (see Article 39 of the EU Regulation (note 75 *supra* chapter 2), in the Model Law (note 143 *supra* chapter 2), Article 11) or in the ALI Principles (note 189 *supra* chapter 2),Procedural Principle 13.

nationally oriented administrator), especially those involving large groups operating across the globe. Clearly, when the case involves separate entities that operated in different states with foreign creditors at stake, problems of potential conflicts of interest and inadequate representation of creditors may augment.

5.2 Protecting substantial rights of creditors in the context of MCG insolvency: the issues of equal distribution and group liability

5.2.1 Securing distribution rights during joint administration

Although we have concluded that centralization can fit with the idea of ensuring due process and meeting legitimate expectations with regard to the handling of the insolvency process, it may still pose risk to other fairness considerations, specifically distribution rights[60]. It should be reminded that centralizing the proceedings for procedural purposes should not hamper the separation between the entities[61].

Hence, the insolvency regime should pay attention to creditors of specific entities and compensate them if decisions (which are made for the benefit of the whole group) harm them in the sense that they will result in reducing the amount of dividend they would have got if no such joint process would have taken place. For instance, if a joint sale is the course in which a certain insolvency process has chosen to go along, but this will certainly reduce the gain a specific company (and its creditors) could have had through a local separate sale, they should be compensated accordingly[62].

The insolvency regime should also be aware of the danger of sliding on the 'slippery slope' from a joint administration to an actual pooling of assets and debts regime (where there is no justification for taking this path[63]).

Notwithstanding the above, it should be understood that when applying an idea of international jurisdiction and applicable law ('a centralized approach') some degree of

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[60] See *supra* chapter 3 section 3.3.

[61] Indeed, the distinction between the basis for assertion of jurisdiction and the assertion of substantive liability has contributed significantly to the acceptance of the 'enterprise view' in jurisdiction cases (see P.T. Muchlinski, "Corporations in International Litigation: Problems of Jurisdiction and the United Kingdom Asbestos Cases" [2001] 50 ICLQ I; Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 678).

[62] The ALI Principles (note 189 *supra* chapter 2, at p. 81) give an example of a subsidiary that holds domestic intellectual property and is offered a higher sum of money by a local competitor than it would have gained in a package sale, even though the global deal is better for the group as a whole. It is stated there that if the court is to decide that the local sale should be refused in favour of the overall package sale, it must protect the specific interests of the subsidiary.

[63] See *supra* chapter 4 section 4.3, and sections 5.2.2 and 5.2.3 below.

alteration in distribution rights may occur. Since presently there is no prospect of achieving unification of domestic insolvency laws[64] the application of a particular legal regime on the entire estate may affect legal rights of creditors. For instance, the ranking of a particular debt may be different. Thus, the relevant creditor may gain a lower (or higher) recovery from the estate of the company with which it dealt compared to what he would have gained under a 'separable' approach. This outcome diminishes with the option of having local proceedings for local subsidiaries in the relevant circumstances[65] or alternatively by using the mechanism of secondary (or non-main) proceedings that can be opened concurrently against the same entity[66]. In any case, in determining the proper venue, courts should take into account the severe effect such decision may have on creditors' distribution rights. And, if there is a potential prejudice of such rights, a careful examination of the facts should be done to ensure that the proceedings were not placed at a certain place as a consequence of mere forum shopping[67].

5.2.2 Dealing with alleged prejudice of creditors' distribution rights in the strongly integrated MCG scenario

5.2.2.1 The scenario

In some cases the MCG estate is integrated to such a degree that the separate businesses comprising the group are untraceable. We have previously suggested[68] that the strong integration between the entities[69] may demand the application of an interventionist approach (lumping all companies together) to achieve economically efficient results.

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[64] See *supra* chapter 2 section 2.4.1.
[65] See *supra* chapter 4 section 4.1.3.8 and section 5.1.5 above.
[66] As provided in existing models for cross-border insolvencies of single debtors (See *supra* chapter 2 section 2.4).
[67] See the case of TXU. Mr Registrar Baister pointed out the need in certain circumstances to require further evidence dealing with the question of the insolvency location and its effect on creditors' rights, for example whether any apparent forum shopping could undermine preferential rights of employees or some other class of creditors. See further on forum shopping in *infra* chapter 6 section 6.1.
[68] See *supra* chapter 4 section 4.3.
[69] Portrayed by Prototype C (*supra* chapter 1 section 1.6).

5.2.2.2 The fairness issue

In principle, ensuring equal distribution will demand for a similar solution, that is ignoring the corporate form and distributing dividends to creditors as if were all belonged to one single entity[70]. Even if the entanglement was not a result of strategic planning purposely designed to deceive creditors, but rather a result of negligent management or a de facto operation in which the affairs of the components were mixed to a significant extent creating in effect a single estate, the fact of the matter is that equality will not be fulfilled if certain creditors will be left to recover from the weaker entities (somewhat arbitrarily).

Nonetheless, there may be circumstances in which creditors may claim that they would have gained more in a separate distribution rather than under a pooling mechanism. This would be the case if it would be possible to show that particular assets of the estate could indeed be traced to a specific member of the group, although in general the assets are intermingled. Another possibility could be that creditors' claims are identified as belonging to a particular member of the group (although other claims are untraceable). If the recovery from this particular company separated from the group will be higher it may be claimed unfair to jointly distribute the entire group's estate. Similarly, with regard to inter-group claims, if there is evidence that in spite of the commingled way of affairs an explicit value could be ascribed to a particular claim it might not be fair to the particular creditor to pool all assets and debts together. A global approach should take into account this potential downside and provide responses as to how to deal with such situations.

5.2.2.3 Examples on the international level

Example for the potentially unfair application of substantive consolidation in strongly integrated MCGs could be demonstrated in the case of *BCCI*[71]. There, solvent companies were included in the pooling of assets imposed on the entire group[72]. As explained earlier[73], the parties in that case improvised a sort of consolidation in order

[70] Foreign creditors of foreign affiliates should accordingly be treated equally and should not be discriminated in the application of priorities in distribution from the joint pool (as long as it is full substantive consolidation (see *supra* chapter 4 section 4.3.6).
[71] Note 155 *supra* chapater 4.
[72] See *supra* chapter 4 section 4.3.2.
[73] See *supra* chapter 4 section 4.3.5.

to avoid massive costs and increase return to creditors. The outcome was certainly a success in terms of return[74]. Nonetheless, it is questionable whether it was indeed fair (in terms of securing distribution rights) to all the components that were part of this process and that participated in the pool. At least theoretically, it might be that for certain creditors, especially those that could have been identified as related to initially solvent members a better solution was to have a separate insolvency process. Such creditors might have gained (for instance) 100% of their debt instead of 70%.

Recently, in the case of *WorldCom*, the US court allowed substantive consolidation, although some note holders, that lent to MCI before WorldCom acquired it, stood in a position where due to the consolidation plan they were supposed to receive nothing, while creditors of the parent receive substantial distribution although were structurally junior to them[75]. Eventually, the parties reached an agreement under which the note holders position was modified (they were promised a substantially greater recovery than other unsecured WorldCom creditors) thus the decision was not contested[76].

5.2.2.4 The inability to ascertain separate claims and separate status of the members

Normally, if the situation is of a complete intertwined scenario in which assets and debts cannot be readily ascertained or the true financial position of each component can not be identified, then imposing a pooling concept would be favorable. It is true that a creditor may still claim that it was not aware of the intermingling way of affairs. It established credit to a certain company after due diligence and only now it finds out that its true risk has to be measured by reference to the financial health of the group as a whole. This would be even more pronounced if its claim is allegedly belonging to a

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[74] *Id.*

[75] In re Worldcom, 2003 WL 23861928. See also G. Douglas Baird, "Substantive Consolidation Today" [2005] 1 Bost. Col. L. Rev.5, 10-11.

[76] *Id.* See also David A. Skeel, "Groups of Companies: Substantive Consolidation in the U.S." in H. Peter, N. Jeandin, J. Kilborn (eds.), *The Challenges of Insolvency Law Reform in the 21st Century* (2006), 229, 233. See also the case of *Bramalea* (note 181 *supra* chapter 4) in which it has been argued that substantive consolidation was unfair to certain creditors, the US lenders that initially were exposed to US subsidiaries and found themselves, in the course of the joint insolvency, with exposures to the Bramalea group as a whole. This alleged unfairness was emphasized since, based on a balance sheet analysis, some of the subsidiaries were arguably not insolvent (see Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 719). Though Bramalea claimed that subsidiaries were highly dependent on the parent and were not financially viable as stand alone entities (see R. Gordon Marantz, "The Reorganization of a Complex Corporate Entity: The Bramalea Story" in Jacob S. Ziegel (ed.) *Case Studies in Recent Canadian Insolvency Reorganizations* (1997) 1, 6).

solvent entity that was put under the pooling proceedings. However, if the assets are now in fact intermingled then it would be difficult in any case to actually predict what option will gain more for the creditor. In this scenario it is impossible to determine which assets and debts belong to which company including the magnitude of inter company claims, so it will also be impossible to estimate with any degree of certainty the percentage distributions in each of the insolvency proceedings (of the companies comprising the group) in the absence of substantive consolidation. In addition, if the company is allegedly solvent but in fact is highly dependant on other insolvent components then the apparent worth of its assets may be unrealistic and the whole picture is actually unstable and about to change soon after the collapse of the group. Therefore, as a starting point, a pooling mechanism[77] would be the most adequate solution here in order to promote both a fair and efficient result. Yet, it should be examined whether indeed each of the relevant components is strongly integrated with the rest in a way that makes it significantly problematic to claim to be prejudiced by a consolidation.

Indeed, in *BCCI*, the businesses were so intermingled that a creditor could not have possibly shown that a certain company was by all means solvent or that he would gain more in a separate distribution. A prerequisite for such a claim would have been to conduct a long and expensive process of entangling the assets and debts to ascertain which assets and liabilities belonged to which component. Therefore, the representatives in this case concluded that a pooling concept was essential also in order to ensure an equal treatment to the creditors as a whole[78].

Even if particular claims were initially separated (as for instance creditors lent money to a company prior to its acquisition by the group), however at the time of insolvency the subsidiary at hand is strongly integrated with the rest, then it will be very difficult to prove the viability and ability of this entity to pay the debt from its own separate resources.

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[77] See *supra* chapter 4 sections 4.3.6- 4.3.7.

[78] See In re Bank of Credit and commerce International S.A. (District Court of Luxemburg, 3 January, 1992). The court indicated that the supervisory commisioner "is of the opinion that it is essential in order to ensure an equal treatment to all creditors of the group to coordinate the liquidation operations by means of cooperation agreements to be concluded with the liquidators of the different foreign entities, subsidiaries and branches, with a view to create a common pot and a common administration (Pooling Agreement) of all assets realised or to be realised by the different entities, in order to guarantee an equal distribution to creditors of those entities".

However, if creditors can show that their claim clearly belongs to a specific viable entity (at least to the extent needed to pay their debt or any part thereof), it would be required to provide an adequate fair solution. We will discuss these scenarios below.

5.2.2.5 National laws' approaches

National laws, under which substantive consolidation or pooling orders are available to domestic enterprises[79], suggest ways to deal with the problem of the different interests involved.

Under the US regime, the courts may place conditions on the consolidation in order to protect the interests of specific creditors or to affect an equitable remedy. For instance, the courts may order that higher percentages will be distributed to creditors that are prejudiced by the consolidation compared with those that are not prejudiced, or that certain claims will be recovered of assets of certain entities[80]. However, partial consolidation is rare and considered impractical[81]. As mentioned previously, in most large chapter 11 cases the court confirms only a single plan covering all of the debtor entities[82]. The court strikes a balance and aims to reach an equitable result for the creditors as a whole[83].

Under the New Zealand regime, it is not entirely clear whether a pooling order will always mean a merge of all liabilities and inter-company debts or whether courts should apply a sort of partial consolidation due to fairness reasons[84]. It has been commented in this regard, that a pooling order should principally mean a merge of assets and liabilities. However, the court may place conditions on the order[85].

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[79] See *supra* chapter 4 section 4.3.4.
[80] See In Re Continental Vending Machine Co, 517 F 2d 997 (2nd Circ 1975); In Re Parkway Calabasas Ltd. 89 Bankr. 832 (Bankr. CD Cal. 1988); Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 406-408.
[81] See Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 408.
[82] See note 106 *supra* chapter 4.
[83] In re Snider Bros., Inc. 18 B.R. 230, 234 (Bankr. D. Mass. 1982); Chemical Bank N.Y. Trust Co. v. Kheel 369 F.2d 845, 847 (2d Cir. 1966).
[84] See In Re Dalhoff & King (1991) 5 NZCLC 66, 959; In Re Stewart Timber & Hardware Ltd (Whangarei) Ltd (in liq.) and Stewart Timber & Hardware Ltd (in liq.) (1991) 5 N.Z.C.L.C. 67, 137.
[85] By its power in section 271(2) of the New Zealand Companies Act, 1993 (see Farrar, Corporate Governance (note 10 *supra* chapter 3), p. 247).

5.2.2.6 Addressing the issue within a global approach

A global approach should similarly adopt means to rightfully assess what would be most beneficial for the group as a whole if the ideal of 'fairness' in the sense of securing distribution rights is to be attained. On the international level, it would be even more crucial to carefully consider any contest for consolidation and even in the absence of opposition to thoroughly examine whether consolidation will result in prejudice. It should be appreciated that consolidation may not only redistribute substantial rights of creditors as a result of the pooling of all companies together, but also because the consolidation is being imposed by a particular court subjecting the entire estate to a specific legal regime. Moreover, as aforesaid[86], the ability to hear all creditors and to be aware of all potential objections is reduced. And here, it may influence substantial rights in the most direct way.

Accordingly, when considering a pooling order in an MCG insolvency case, all relevant interests should be taken into account. Decisions should not rely on ex-parte applications. Rather, the various stakeholders' wishes and the potential benefit or harm they may suffer should be considered. As aforesaid[87], this should be done even if certain stakeholders are not present and actually heard in a given application. As discussed with regard to the economic efficiency goal, a sort of partial consolidation can be applied in the sense that it would be possible to exclude certain companies from the consolidation or to pool only assets and not debts[88].

In other cases it should be permissible to compensate creditors that otherwise will be harmed in the course of the consolidation. For instance, certain claims could be paid although the company to which they relate is being consolidated (other conditions on the consolidation could also be applied). If the potential injustice is significantly lower comparing to the overwhelming advantage to the creditors in general a complete substantive consolidation could be justified. This way, an amount of flexibility can ensure that equity is done.

The result should be a balancing test as to whether the benefits of consolidation outweigh the harm that consolidation would cause to creditors. The balance may be between a specific creditor who wishes to recover from a specific asset and the rest of

[86] See section 5.1.3 above.
[87] See section 5.1.5 above.
[88] See *supra* chapter 4 section 4.3.6.

the creditors, or between two or more sets of creditors relating to different components of the group. It may also involve the striking of a balance between shareholders and creditors, if the former anticipate recovering from the insolvent estate, or if they have claims against other entities which they argue to be identifiable. In such circumstances, the rights of creditors should generally tend to weigh more heavily than those of shareholders[89].

In order to achieve a fair solution to the strongly integrated MCG, there is a necessity for global means that will ensure that the various interests pertaining to the case are taken into account and that a compatible solution is applied. Thus, a global model must provide predefined guidelines on the implementation of a pooling concept based on the above propositions. Without a set of accepted rules that accompanies the application of a pooling concept the outcome of any de facto or ad hoc solution could be such that may neglect, on the path to a compatible solution, certain 'voices'. These guidelines should be implemented by a specific court that supervises the case so that it is possible for a single body to see the entire picture and the different interests involved. Combined with the goal of achieving an economically efficient result, a single-supervised preferably centralized process for a strongly integrated MCG would benefit the creditors as a whole, providing an effective solution that appreciates the various interests involved.

5.2.3 Creditors' beliefs and the pooling mechanism

5.2.3.1 The scenario

There are also circumstances in which creditors of any of the companies comprising a group might have had the belief that they have dealt with one single enterprise rather than with an individual member of the group. In some cases this belief was encouraged by those in control of the group, so that the creditors were misled to think they were dealing with a greater entity[90]. Thus, in the event of a general collapse within such group the question of whether to apply a pooling mechanism arises.

[89] It accords with the general view that the interests of the creditors in the company's assets increases to the detriment of the shareholders in the event of insolvency (see note 22 *supra* chapter 3).
[90] See in section 5.2.4 below an elaboration on the issue of abuse within the MCG.

In this scenario, the various entities may have been strongly integrated operating veritably as a single entity, but it is also possible that in fact they have not been so inter-related. It may have been, for instance, that a certain component had identifiable separate business and was operating as a stand-alone component, however certain creditors (creditors of this component or creditors of other members of the group) were not aware of that and their impression was that the assets of this component were part of the entire estate.

The question is, whether and to what extent a global approach should take into account creditors' beliefs with regard to the pooling mechanism, bearing in mind the need to enhance fairness (in the sense of securing distribution rights).

5.2.3.2 National laws' approaches

Under 'pooling' regimes[91], courts are in a position to take into account a series of considerations in deciding whether to apply such mechanisms. These include factors pertaining to the creditors' reliance on a single unit or on a particular entity.

Under New Zealand pooling regime, one of the factors to be considered in deciding whether to make a pooling order is "the conduct of any of the companies towards the creditors of any of the other companies"[92].

Under the US bankruptcy regime, substantive consolidation apparently may be allowed not only where the financial affairs and businesses of the debtors are commingled, but also in cases where creditors of affiliate companies have dealt with these entities as a single economic unit, and have not relied on their separate identities when extending credit[93]. Substantive consolidation is regarded as an equitable tool and as a remedy for improper and misleading corporate behaviour[94].

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[91] See *supra* chapter 4 section 4.3.4.

[92] Section 272(2)(b) of the New Zealand Companies Act, 1993. This was interpreted as essentialy meaning the degree of confusion of the creditors of the companies as to which company they had been dealing with (see In Re Dalhoff & King Ltd (1991) 5 N.Z.C.L.C. 66 959).

[93] See e.g. Soviero v Franklin National Bank 328 F. 2d. 446 (2nd circ. 1964); Union Sav. Bank v. Augie/Restivo Baking Company (In re Augie/Restivo Baking Co) 860 F 2d 515 (2d Cir 1988); In re Owens Corning, 419 F.3d (3d Cir. 2005)).

[94] In re Snider Bros., Inc. 18 B.R. 230, 234 (Bankr. D. Mass. 1982); Chemical Bank N.Y. Trust Co. v. Kheel 369 F.2d 845, 847 (2d Cir. 1966)); Union Sav. Bank v. Augie/Restivo Baking Company (In re Augie/Restivo Baking Co) 860 F 2d 515 (2d Cir 1988). See also Eric A. Webber, "Concensual Substantive Consolidation: Comments on the Working Papers of Professor Skeel and Dr. Staehelin" in

As will be proposed in the following section, in the international scenario creditors' reliance should play only a limited role when considering substantive consolidation. The issue of improper behaviour will be dealt with separately, proposing additional adequate mechanisms to such scenarios[95].

5.2.3.3 The preferable approach for a global solution

Prima facie, it will serve justice if the international system could meet creditors' expectations regarding distribution rights and enable them to recover their debts from the entire estate if they genuinely thought they were dealing with the business as a whole. Furthermore, as was stated elsewhere[96], the lender's expectations are central to the calculation of interest rates and other terms of loans, and fulfilling those expectations is therefore important to the efficiency of credit markets.

Nevertheless, there are a number of problems in solely focusing on creditors' beliefs when determining whether to join the estates of two or more affiliates. These problems reflect on the ability of such approach to indeed promote the ideal of fairness of the creditors of the group as a whole. First of all, it is difficult to ascertain the credibility of individual creditors' claims which are subjective and relate to their viewpoint with regard to the group operation. Secondly, it often happens that some creditors would have dealt with the debtors as one economic unit, but others have not[97].

Indeed, the US experience demonstrates that where the creditors have relied on the separate credit standing of the group component with which they were dealing, and particularly where they were unaware that such component was affiliated with the corporate group, consolidation may be refused where it would result in prejudice. Some of these decisions involve previously independent companies that were subsequently acquired by the group and continued as subsidiaries, usually with the same management, particularly when it continues to conduct its previous business in

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H. Peter, N. Jeandin, J. Kilborn (eds.), *The Challenges of Insolvency Law Reform in the 21st Century* (2006), 235, 237.

[95] See section 5.2.4 below.

[96] In Re Augie (860 F. 2d. 515 (snd circ. 1988)).

[97] See Robert van Galen, "The European Insolvency Regulation and Groups of Companies" October 2003, http://www.iiiglobal.org/country/european_union/Cork_paper.pdf, arguing, with regard to European group of companies in default, that in the scenario of a single economic unit a substantive consolidation is not appropriate but rather filing separate suits, inter alia because of the conflicting views of creditors.

much the same way[98]. One of the ways to reconcile the problem of contradicting claims with regard to the way the corporate group was operated and the different expectation of creditors is the use of partial consolidation mentioned above. However, as aforesaid, the actual use of partial consolidation is rare[99].

It has been rightfully argued elsewhere[100] that an inherent problem to the dealing with insolvencies within corporate groups is the diversity of creditors' interests with regard to the distribution of the group's estate. The exemplary case is where one component apparently has sufficient assets to cover its debts while the debts of the other component vastly exceed its assets. In this case it is obvious that the latter company's creditors would wish to lump all assets and claims together whereas the former company's creditors would prefer to maintain the legal separation between the related companies.

Yet, this problem is reduced when substantive consolidation is grounded on 'objective' elements pertaining to the group; that is the way the enterprise was structured and operated. As explained above, when the MCG was actually strongly integrated the viability of one component is dependant on the other affiliates and vice versa, and the benefits for creditors from recovering their debts from a particular company are obscure.

The outcome is certainly more prone to injustice when a pooling order is based on creditors' subjective beliefs. It is then more difficult to determine which interests will outweigh the others and what would count as an equitable result. As mentioned earlier, this problem arises within national regimes; however, it becomes more pronounced on the international level, where competing legal systems are involved in the case and creditors are situated and had dealings with the group's entities in different countries and under different laws. In this case it is even harder to compound all interests together and reach the appropriate balance[101].

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[98] See Flora Mir Candy Corp. 432 F. 2d. (snd circ. 1970); Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 434-435.

[99] Note 81 above.

[100] See Robert K. Rasmussen, "The Problem of Corporate Groups, a Comment on Professor Ziegel" [2002] 7 Fordham J. Corp. & Fin. L. 395, 396.

[101] This may be the case even where substantive consolidation is consensual (reached through negotiations). It is possible that negotiations were not properly conducted with all parties heard and being adequately considered, especially in an international case (see the the concerns presented in Eric A. Webber, "Concensual Substantive Consolidation: Comments on the Working Papers of Professor

Notwithstanding the above, creditors' beliefs should be a relevant factor in this respect in order to fulfil the idea of meeting creditors' expectations regarding their distribution rights. A global approach that adopts a mechanism of pooling orders is suited to appreciate creditors' expectations in this regard and provide such an interventionist solution in the proper cases. Yet, the application of this idea on the global scenario should be done cautiously. On the international level it is significantly difficult to evaluate creditors' subjective beliefs with regard to the way a multinational operation was conducted. Therefore, the test should be more objective and reflect a composition of facts. Hence, creditors' beliefs may aid the final determination of whether consolidation is warranted, but will be neither a sufficient nor a conclusive factor. It may reinforce the need for a pooling order where the objective test suggests the same (see the scenario of strong integration[102]), or it may reveal a situation where the group actually misled creditors to think that they would be able to recover from a financially stronger entity[103].

5.2.4 Abuse and unfair behaviour within an MCG and the event of insolvency

5.2.4.1 Introduction

In order to deal with abuse and unfair behaviour within the MCG in the course of insolvency[104], there should be a way to evaluate and provide sufficient responses in the process of the insolvency within the MCG with regard to harmful actions made by affiliates. This would be specifically relevant when affiliates exerted their control over the group or their influence upon its affairs to abuse the corporate form or to unfairly defeat the interests of the stakeholders of a certain subsidiary. In such cases, where the privilege of incorporation was abused, a strict adherence to the limited liability doctrine would be deemed unfit. Similarly, a strict territorial approach in which each member of the group is treated separately within its own country offers little remedy in these situations. Conversely, a global approach will be much more suited here, as most importantly it will be able to link (for substantive purposes) between insolvent

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Skeel and Dr. Staehelin" in H. Peter, N. Jeandin, J. Kilborn (eds.), *The Challenges of Insolvency Law Reform in the 21st Century* (2006), 235-246 regarding consensual substantive consolidation in the U.S.).

[102] See *supra* chapter 4 section 4.3 and section 5.2.2 above.

[103] The latter scenario will be discussed in more details in the next section.

[104] See *supra* chapter 3 section 3.3. As was defined, one of the elements of fairness for our purposes is the protection of stakeholders from manipulation and abusive behaviour by those who controlled the company. Here, we are concerned particularly with the responsibility of the affiliated companies.

members and other affiliates for the purpose of increasing the estate of the failing companies available for distribution.

5.2.4.2 The 'actors' and scenarios

The basic scenario here is of a failing debtor company which is a component of an MCG[105]. Critically, an affiliate exploited its control over the debtor (in a manner as will be delineated below) resulting with the debtor's insolvency. Consequently, it will serve fairness that the affiliate will bear some responsibility to the financial situation of the debtor and be liable to a certain extent for the debtor's debts (the controlling affiliate will be referred to as the "contributory party") hence the need for a substantial linkage between the debtor and the contributory party. The contributory party is typically a parent company[106] and it is typically solvent[107]. Furthermore, it could either fully or partly own a subsidiary[108].

The contributory party could take the form of another type of related company (other than a parent company) or another connected entity that had similar influence on the company's affairs and is morally responsible for its condition (at least to some extent)[109]. Although, our discussion will be focused on unfairness within the group

[105] One of the options under Prototype D (*supra* chapter 1 section 1.6).

[106] Usually the immediate holding company, dependant on the way the group was operated and which was the entity that misbehaved. More often it will be the immediate holding company that exercised its control over the subsidiary, or otherwise was closely integrated with the subsidiary comprising together a single unit. Responsibility should be imposed on the entity that was actually acting in abuse or unfairness towards the other entity. This will also usually reflect the realities of the commercial division within the group and the enterprise notion of liability (see Muscat, The Liability (note 44 *supra* chapter 1), p. 443-444). However, in the oposite scenario, where the parent (or the controlling entity) is the insolvent entity (and not the subsidiary) there is no question of group liability since a solvent subsidiary should in no circumstance contribute to the debts of an insolvent holding company (see *Id.*, p. 456).

[107] Yet, a contributory party can be insolvent and still be exposed to liability with regard to its behaviour towards the other affiliate.

[108] In principle, whether the subsidiary is partly or fully owned is irrelevant to the liability question, which deals with the actual exercise of control over a subsidiary in an abusive way. However, complete ownership may suggest a higher risk of abusive control. In any case, courts are able to use their discretion to determine on the level of responsibility (and accordingly on the compatible remedy, as will be discussed below) to be imposed on the contributory entity according to its actual contribution to the debtor's situation (see Blumberg, The Multinational challenge (note 4 *supra* chapter 1), p. 142-143; Muscat, The Liability (note 44 *supra* chapter 1), p. 444-445, 462-463). It can also be a parent which is a partner in a joint venture that abused its control over the joint venture (see M. Lower, "Joint Ventures" in 241 *Regulating Enterprise* (D. Milman, ed., 1999) p. 258-262).

[109] Such as a sister company or a controlling entity linked to the company by contract. As explained earlier in this work (*supra* chapter 1 section 1.3) a global approach should not limit itself to the scenario of equity based 'hierarchical' group involving parent-subsidiary relationship. In fact, enterprises comprised of entities linked by contract may display similar systems of managerial control. Although the contract may include risk-shifting clauses in the form of exemptions of liability for the controlling

conducted by affiliated companies, it can also be a creditor which had significant influence on the business and acted in abuse[110] (typically while cooperating with another controlling affiliate) or alternatively, the group's officials who breached their duties, or individual shareholders[111]. However, the position of such parties is not within the scope of this work.

Pursuant to an event of assets' manipulation another type of linkage may be required. That is, a linkage between the debtor and another affiliate (not the contributory party) to whom funds or assets were diverted. This affiliate may or may not be solvent and may or may not be economically separate from the debtor (for instance, it could be conducting a different sort of business than that of the debtor's or the rest of the group). In fact, it may even belong to a different group with a common shareholder controlling both separate businesses (hereinafter: a remote affiliate).

In particular there are various scenarios and circumstances of corporate group behaviour that should result with at least some extent of disregard of the corporate form, in the sense that the contributory party or the remote affiliate should take part in the debtors' insolvency.

Imposing liability upon shareholders in exceptional scenarios represents a broad approach of existing laws[112]. Even in 'traditional' legal regimes, wedded to the entity

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entity, the issue of whether the 'contractual veil' should be lifted in cases where control was exercised in an abusive way arises (see on the issue of group liability in network enterprises: Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), p. 327, 330; G. Teubner, "Unitas multiplex: corporate Governance in group enterprises" in *Regulating Corporate Groups in Europe* 67, 87-92 (D. Sugarman and G. Teubner eds., 1990). See also Blumberg, The Multinational Challenge (note 4 *supra* chapter 1), p. 244-253 (explaining that contract may also provide one party with the ability to direct the business affairs of another party. This is particularly true where one party to the franchise contract, the license contract, or the loan agreement has dramatically stronger bargaining power, as is frequently the case).

[110] See Lundgren, "Liability of a creditor in a control relationship with its debtor" [1984] 67 Marq. L. Rev. 523; K. Hofstetter, "Multinational Enterprise Parent Liability: Efficient Legal Regimes in a World Market Environment" [1990] 15 North Carolina J. of Int. Law and Comm. Reg. 299; Also see Robert K. Rasmussen, "The Problem of Corporate Groups, A Comment on Professor Ziegel" [2002] 7 Fordham J. Corp. & Fin. L. 395, 397, asserting that sophisticated creditors are well aware of managerial decisions concerning the structuring of the group and the allocation of assets when they extend credit.

[111] Generally, in the case of the individual shareholders a strict adherence to the limited liability concept should be kept since it is the essential advantage and purpose of the principle of limited liability- to safeguard "natural" persons (see Muscat, The Liability (note 44 *supra* chapter 1), p. 194-195).

[112] By way of using the Anglo-American doctrine of 'lifting the corporate veil' or through concepts such as fraudulent corporate simulation, abuse of corporate personality, *actio Pauliana* (giving creditors powers over debtors who act in a manner prejudicial to the creditors' rights of execution) and *'abuse de droit'* (see Donson, ""Liefting the veil" in four countries: the law of Argentina, England, France and the United States" [1986] 35 ICLQ 839). See also Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), p. 330 (explaining that the broad approach of existing laws is to provide ad hoc exceptions to the limited liability concept, which deal with individual abuses); K. Hofstetter, "Multinational

doctrine[113] and the strict application of *Salomon*[114], the corporate form can be ignored. For instance, in cases in which the corporate personality is deliberately used as a cover for fraud or improper conduct[115] or where a company is a mere façade concealing the true facts[116] corporate form may be disregarded. In other words, most legal systems will enable imposition of liability upon a shareholder in some (even if rare) circumstances.

However, as was suggested elsewhere[117], traditional legal concepts fail to adequately deal with the complexities of the corporate group phenomenon and with the need to protect the legitimate interests of outside creditors. The exceptions to the concepts of separate personality and limited liability provided by the English law, for instance, are too narrow and too ill-defined to sufficiently remedy situations of unfairness within a corporate group[118]. There are a variety of scenarios of corporate group behaviour that should demand the imposition of liability and the linkage between the relevant affiliates to best implement equitable objectives which are in the core of insolvency law[119]. Indeed, as will be discussed hereafter[120], several legal regimes have developed more comprehensive approaches to address issues of inter-group liability.

When we initially described prototypical scenarios (Prototypes) in the first chapter of this work, one aspect that bears important relevance for the formulation of a

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Enterprise Parent Liability: Efficient Legal Regimes in a World Market Environment" [1990] 15 North Carolina J. of Int'l Law and Comm. Reg. 299, 313-314 (showing that in practically all intenational jurisdicions the abuse of a corporate entity by shareholders is recognized as a reason to disregard the corporate veil); Blumberg, Bankruptcy (note 43 *supra* chapter 1), chap. 17 (reviewing the approaches of various legal systems with respect to the liability of a parent corporation for the obligations of an insolvent subsidiary); OECD comparative findings (note 8 *supra* chapter 3), p. 8; Richard D. Kauzlarich, "The review of the 1976 OECD declaration on international investment and multinational enterprises" [1980-1981] 30 Am. U.L. Rev. 1009, 1021 (explaining with regard to the OECD comparative findings that OECD countries accept certain fairly consistent but limited exceptions to the limited liability concept).

[113] Such as the English corporate regime (see also *supra* chapter 4 section 4.3.4). For a review of other legal approaches that emphasize entity law see Blumberg, Bankruptcy (note 43 *supra* chapter 1), chap. 17.

[114] Salomon v Salomon and Co. Ltd [1897] AC 22.

[115] Re a Company [1985] B.C.L.C. 333 (C.A.); Creasey v. Breachwood Motors Ltd. [1992] B.C.C. 638.

[116] Adams v. Cape Industries plc [1990] B.C.L.C. 479 (C.A.). In addition, liability can be imposed in cases of wrongful trading on directors and "shadow" directors (Insolvency Act 1986, s. 214). See also Muscat, The Liability (note 44 *supra* chapter 1), p. 211-218.

[117] See Muscat, The Liability (note 44 *supra* chapter 1), p. 35, 38 (reviewing the calls for reforms with respect to the problem of inter-corporate liability). See also Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 6-8; Hugh Collins, "Ascription of Legal Responsibility to Groups in Complex Patterns of Economic Integration" [1990] 53 MLR 731, 744.

[118] See Muscat, The Liability (note 44 *supra* chapter 1), p. 112, 138. See also section 5.2.4.4 below.

[119] See *supra* chapter 3 section 3.3.

[120] See section 5.2.4.4 below.

comprehensive global approach (that is, how control was exercised within the MCG) was left aside for later consideration. However, we have now reached the point in our discussion where this aspect should be brought forward and serve an additional elaboration on our prototypical scenarios.

Dr. Muscat in his extensive analysis of the phenomenon of abuse and unfairness within corporate group[121] describes four main categories of corporate abuse and their characteristics[122]. We will adopt these categories in our discussion as well. They are comprised of well-defined circumstances of corporate groups' conduct which may prejudice the interests if external creditors or otherwise constitute an abuse of the corporate form. They embrace the notion that in some circumstances "entity law" should give way to "enterprise" analysis[123], although the principle of limited liability continues to be a fundamental concept of company law[124]. These practices occur and are relevant to both domestic corporate groups and transnational groups[125]. For the purpose of his proposal Dr. Muscat uses a definition according to which a 'group' is a holding company together with its subsidiaries[126]. However, it would be possible to extend the definition to include other types of MCGs in which a controlling party exercised control in an abusive way[127].

First such category is the subservient subsidiary[128], which entails the scenario of a subsidiary that is not acting as a real separate unit. This happens when a parent corporation dominates the subsidiary. Accordingly, its business is not conducted with the sole view of its own interests (rather possible interests of the parent, other affiliates, or of the group as a whole guide its operation). This may lead to group profit maximization, transfer pricing, diversion of corporate opportunities, manipulation of

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[121] See Muscat, the Liability (note 44 *supra* chapter 1), p. 298-305; 363-390; 413-415; 433-436. See also J. Landers, "A Unified Approach to Parent, subsidiary and Affiliated Questions in Bankruptcy" [1975] 42 U Chi L Rev 589; R. Posner, "The Legal Rights of Creditors of Affiliated corporations: An Economic Approach" [1976] 43 U Chi L Rev 499; R. Posner, "Another Word on Parents, Subsidiaries and Affiliates in Bankruptcy" [1976] 43 U Chi L Rev 572 (Landers identifies the dangers faced by creditors of a multicorporate enterprise to which law and economics fail to provide practical solutions) (the Landers-Posner debate regarding abuse and unfairness in the context of corporate groups is conveniently summarized in Muscat, The liability (note 44 *supra* chapter 1), p. 99-100).

[122] Muscat, the Liability (note 44 *supra* chapter 1), chap. 5, 6, 7 and 8. See also Farrar, Corporate Governance (note 10 *supra* chapter 3), p. 233-234.

[123] See *supra* chapter 3 section 3.2.

[124] Muscat, The Liability (note 44 *supra* chapter 1), p. 35.

[125] *Id.*, p. 98.

[126] *Id.*, p. 442-443.

[127] See note 109 above.

[128] Muscat, The Liability (note 44 *supra* chapter 1), chap. 5.

assets, allocation of financial support for the group and operation of the subsidiary without a profit motive.

A second category is that of the undercapitalized subsidiary situation[129]. In this case, the subsidiary is inadequately financed since the holding company fails to provide it with the reasonably required financing to enable it to undertake the business activity for which it was incorporated. As a result, the subsidiary is almost certainly doomed to failure and the risk is shifted to the creditors.

A third category involves the integrated economic enterprise[130]. In this scenario a unitary enterprise is artificially fragmented (for no functional reason) into several entities with the sole aim of insulating the enterprise from potential claims. In such circumstances this may amount to abusive integration and a manipulation of the privilege of incorporation[131].

The fourth category is the group persona situation[132], in which there is misrepresentation or holding out of a single entity, thus misleading creditors to believe they were dealing with a greater company. This may be done by indicating the subsidiary's membership of the group on its letter heading and advertising its membership on all documents and billings by showing a device or logo distinctive of the group[133]. These supposedly meaningless actions may in fact help the subsidiary to obtain substantial credit.

In these scenarios if the debtor becomes insolvent and goes into liquidation or reorganization, it seems unfair that the contributory party will decline all liability for its subsidiary's debts to external creditors. In other words, if the contributory party

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[129] *Id*, chap. 6.
[130] *Id.*, chap. 7.
[131] It should be noted that where integration was not a planned strategy designed purposely to deceive creditors or to shield the group from potential claims, or where the commingling of assets mentioned in the 'first type' of abuse was a result of reckless management or did not amount to 'abuse' or a 'wrongful commingling' (see Muscat, The Liability (note 44 *supra* chapter 1), p. 291. Dr. Muscat suggests that wrongful commingling is commingling without proper record keeping), still as was seen previously (see *supra* chapter 4), there may be other justifications (other than the need to redress abuse and unfairness) that would suggest to link between the components of the group in their insolvencies at least to some extent, essentially related to the economic reality of the situation. Dependant mainly on the degree of integration, a suitable linkage (either procedural or substantive) may be applied for the purpose of benefiting the creditors generally by reducing significantly administrative costs and increasing revenues.
[132] Muscat, The Liability (note 44 *supra* chapter 1), chap. 8.
[133] See the example given in the Cork Report (note 176 *supra* chapter 4), p. 435 with regard to the issue of making the parent liable to the subsidiary's external debts.

used the corporate form in a way detrimental to the debtor at hand then its creditors should not bear the outcome of such behaviour.

In addition, the group should not be able to enjoy the strength of a unified business in its 'good days' acting as if all the companies were fragments of a single entity and deny the connection between a fragment and the rest of the 'empire' in times of distress, leaving creditors of a certain component with no remedy or with less attractive assets[134]. A contributory party should bear consequences in such event, though, only if there is indeed an actual misrepresentation[135] (that is, if creditors were misled to think and relied upon the notion that they are dealing with the group as a unified entity or with an entity stronger than the debtor or otherwise if they were led to believe that the contributory party or another affiliate within the group will support the debtor financially).

Such abuses could also elicit highly unfair situations in the context of insolvency. For instance, if a contributing party has abused its influence on a subsidiary resulting with its collapse will eventually compete with other external creditors for the remains of the estate[136].

Similarly, it would be unfair to leave creditors of a certain subsidiary with valueless or even completely "empty" estate as a result of assets manipulations as described above. Assets manipulations can also be a result of fraud, diverting assets within or outside the group purposely to hide them from creditors.

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[134] In a similar way, the fundamental policy underlying the old "reputed ownership" clause (see s. 38(c) of the Bankruptcy Act, 1914), which provided that property belonging to another person (than the debtor) may be taken by the creditors, was to prevent the gaining of false credit by persons who conveyed the impression of wealth by means of property which they do not in fact own. This clause is no longer part of the English insolvency law and was criticized as 'verging upon the capricious', while its effectiveness was open to question. The outcome could have been quite devastating to the true owner who would have need to prove in the bankruptcy for the value of his lost property, along with the other ordinary creditors (see I.F. Fletcher, Law of Bankruptcy, 1st ed., 1978, at p. 168-175). In the case of a corporate group, however, the relationship between the debtor and its affiliate makes them 'closer' parties (compared to a debtor and a 'remote' true owner of the property) which reinforces the problem of reliance on the portrayed image of the debtor and justifies more strongly that the risk will be put on the affiliate and not on third party creditors.

[135] See Muscat, The Liability (note 44 *supra* chapter 1), p. 421-423. Dr. Muscat convincingly argues that liability should not be imposed merely because a 'group persona' policy is used as a marketing strategy. This by itself does not constitute prejudice to creditors. The participation of the debtor in a group persona can even strengthen its financial position if it is not abusively dominated or undercapitalized.

[136] See the example given in the Cork Report (note 176 *supra* chapter 4), at p. 436. It is submitted there that a law which permits such an outcome is a defective law.

There is another side to the coin, though, as creditors of the contributory party or the remote affiliate may have an opposite claim. That is, they may claim to have dealt with this particular component (the contributory party or the remote affiliate) relying on this company's separate assets when trading with it. They may reasonably argue that they should not be prejudiced because of that company's relationship with another company. Such prejudice may occur if that company will bear responsibility to the debtor's claims in any way that may threaten that company's insolvency (or if that company is already insolvent at the time when the question of responsibility arises). An approach that may demand from the company to bear any sort of consequences due to its relationship with the debtor may in effect penalize not only the holding company but its own creditors as well. These contradicting positions should be taken into account when searching for a solution for the abusive behaviour and the protection of creditors' rights.

5.2.4.3 Examples of abuse or unfair behaviour within MCGs

On the international level, companies and assets manipulations within groups may be overwhelming. It is not the purpose of this work to demonstrate the magnitude and frequency of corporate group abuse on the international level. Rather, our focus is to establish a suitable global framework to deal with such scenarios when they actually occur. Nevertheless, it should be appreciated that abuse and fraud may be able to thrive when a complex and large corporation is at stake operating under different legal regimes. Those who orchestrate manipulations can have a multitude of options as they may make use of the corporate structure, the geographical separation, the various regimes available on the global arena and the difficulties inherent to international control of corporate behaviour in realizing their abuse[137]. Conversely, it has been argued that it is in fact the smaller groups that are more affected with manipulations, since they are less exposed to monitoring by markets and regulatory authorities than larger corporate groups[138]. In addition, there are various factors that tend to limit the

[137] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2313. Westbrook gives the example of fraud as one of the scenarios that occur in multinational groups leading to a complicated mass of assets and liabilities sprawled across borders, as opposed to a situation of a neat territorial division of assets and debts.

[138] Farrar, Corporate Governance (note 10 *supra* chapter 3), p. 36. Farrar notes though that there is inadequate empirical research being done on the causes of corporate collapse; Muscat, The Liability (note 44 *supra* chapter 1), p. 97-98.

risk of abusive behaviour on the part of transnational groups[139]. However, recent experience on the international level with high profile cases such as the collapse of *WorldCom*[140], *Enron*[141] and *Parmalat*[142] have undoubtedly highlighted the serious threat and risk to creditors dealing with transnational corporations. It seems that regardless of the issue of what type of corporate group is more prone to abuse, the effect of an incident of a multinational nature is immense: considerably large enterprises are affected; sophisticated and big creditors are involved; substantial difficulties in getting access to assets that were diverted into different legal regimes etc.

An earlier example of fraud in the context of the insolvency of an entire MCG is the case of *BCCI*[143]. There, the close integration[144] was part of a severely fraudulent behaviour by those who controlled the group. Of the serious illegalities in which BCCI participated, the most significant was the formation of a "network" which involved an intricate money laundering arrangement[145]. When the group eventually collapsed, it was essential to find a way to fairly distribute the assets (that were available for distribution) amongst the creditors, taking into account the fact that assets were diverted and money was circulated prior to the insolvency amongst the different entities within the group.

In the case of *Parmalat*[146] the group executives were put under investigation for being accused of committing fraud, using a web of offshore holding companies and fictitious

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[139] For instance, allegedly they are probably more cautious in their activities than domestic firms in order to avoid upsetting host countries (Muchlinski, Mulinational Enterprises (note 9 *supra* chapter 1), p. 338; Muscat, The Liability (note 44 *supra* chapter 1), p. 98); Conversely, see Christopher Brown, "Report of the Board of Banking Supervision Inquiry into the Circumstances of the Collapse of Barings" J.I.B.L. 1995, 10(10), 446-452, commenting on the Barings Report, concluding that when institutions are trading globally, as was the case for Barings, rules become more difficult to implement and that if rules become more onerous in some jurisdictions it may deter business.

[140] Chapter 11 No. 02-13533 (AJG) (Bankr. S.D.N.Y.).

[141] Chapter 11 No. 01-16034 (AJG) (Bankr. S.D.N.Y.).

[142] See notes 51 *supra* chapter 4.

[143] Note 155 *supra* chapter 4. See also the cases of *Polly Peck International Plc* (Re A Company No. 009296 of 1990, 1992 B.C.C. 510 (Ch. 1992)) and the case of *Maxwell* (In re Maxwell Communications Corp., [1993] 1 W.L.R. 1402 (Ch. 1993); 170 B.R. 800 (Bankr. S.D.N.Y. 1994)).

[144] As was discussed in *supra* chapter 4 section 4.3.

[145] BCCI laundered drug money by transferring funds to its affiliates in the United States, and transferring funds to Luxemburg, and eventually London, where it was dispatched to one of its affiliates in another country in the form of a certificate of deposit.(see Thomas McInerney , "Towards the next stage in international banking regulation" [1994-1995] 7 DePaul Bus. L. J. 143, 144.; Daniel M. Laifer, "Putting the Super Bank in the Supervision of International Banking- Post BCCI" [1992] 60 Fordham L. Rev. 467, 484).

[146] Note 51 *supra* chapter 4.

revenues to keep Parmalat's losses secret for a decade[147]. Companies' assets were allegedly dispersed among this network of shell companies around the world and to other subsidiaries of the Parmalat group. An example of such a "diversion"[148] is the funds allegedly diverted from Parmalat Finanziaria SpA to Parmatour, the controlling family's tourism business. In addition, bank creditors of Parmalat were accused of allowing Parmalat to hide its losses and of being instrumental in helping Parmalat set up offshore vehicles[149]. This situation posed questions regarding the ability to reach hidden assets and the way Parmalat's creditors' claims will be treated. The accusations of fraud and abuse suggested uncertainty over the veracity and magnitude of inter-company claims, since fraudulent documents have been allegedly created and the reliability of the Parmalat group's accounting records and procedure was questionable[150]. Indeed, the Italian court, in adjudicating the validity of creditor claims against Parmalat, has excluded a substantial amount of creditors claims related to inter-company subordinated debt[151]. On the other hand, with regard to bank creditors' claims (who allegedly helped prolong the fraud) the Italian court took the approach that these creditors will have their claims honoured while damages suits and criminal investigations will take place on different tracks[152].

Other cases demonstrate abuse of the MCG structure where assets are diverted in a way that is detrimental to certain creditors, but without necessarily committing fraud. For instance, as a way to raise cash and enhance credit, a company can transfer assets it owns to a subsidiary, most often a special purpose vehicle (hereinafter: SPV) which pays in turn to the company for the assets it receives, by selling bonds secured by the assets. This transaction (called a securitization transaction) enables a company in financial difficulties to isolate its more attractive assets thus get higher interest and

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[147] Eric Sylvers, "Milan prosecutors try again on Parmalat" New York Times, May 27, 2004; Emily Backus, "Judge seizes assets of ex-Parmalat chiefs" Financial Times, September 30, 2004; REUTERS, "Judge Ready to Start Parmalat Hearings", New York Times, October 3, 2004.

[148] Given by Parmalat's officers during interrogations (see The Associated Press, "Ex - Parmalat CFO Reportedly Blames Tanzi", New York Times, October 3, 2004).

[149] See A. Galloni and Carrick Mollenkamp "Ex-Parmalat Banker Says He Misapropriated $27 Million, International Insolvency", DOWJONES Newsletters, March 2, 2004, p. 5; "Report says banks helped Parmalat hide Fraud", Blumberg News, July 22, 2004.

[150] See ,for instance, The Cayman Islands' court's decision (note 23 *supra* chapter 4), p. 10 (the intra-group claims were regarded by the Cayman Islands' court as ureliable as a result of the alledged fraud).

[151] See Adrian Michaels, "Citigroup and BofA on verge of Bondi win", Financial Times, 17 December, 2004.

[152] *Id.*; Adrian Michaels, "BofA is set to rally Parmalat banks against Bondi lawsuits", Financial Times, 20 January 2005; Adrian Michaels, "Judge deals blow to BofA over Parmalat", Financial Times, 25 January 2005.

raise capital. As a result, the SPV becomes a separate stand alone entity. Indeed, many corporate groups use SPVs to issue bonds, notes and other financial instruments in the global market for a variety of reasons; these range from taxation to insolvency remoteness issues[153]. This may indeed be legitimate[154], however in an asset securitization transaction if creditors are misled to believe that the assets that were diverted to the SPV are part of the entire estate on which they relied for its financial strength (not aware of the fact that all the 'good assets' were in fact removed) then it is not fair to leave these creditors with all the bad[155]. Indeed, other creditors (those who wish to recover separately from the SPV assets) may claim to have a legitimate transaction according to which they were assured that the SPV will stay out of any bankruptcy event, however an examination of their share in orchestrating the transaction or actual 'innocence' and the inter-relations between the SPV and the rest of the group may lead to the conclusion that separateness should be avoided.

In the above examples the necessity to connect between the various components within the group in the course of an entire group's insolvency does not necessarily involve the perpetrator of the abuse (which may in fact be an individual). Yet, the remedy for this situation would still be a substantive linkage between the various components of the MCG although none was responsible for the abuse.

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[153] See Denis Petkovic, "(Case Comment) Piercing the Corporate Veil in Capital Markets Transactions", I.B.F.L. 1996, 15(4), 41-43, discussing the implication of the decision in Polly Peck International Plc (In administration) (No. 3), Re [1996] 1 B.C.L.C. 428 (Ch D) with regard inter alia to the use of SPVs by corporate groups; Robert K. Rasmussen, "The Problem of Corporate Groups, A Comment on Proffessor Ziegel" [2002] 7 Fordham J. Corp. & Fin. L. 395, 398, indicating implications of the use of SPVs on bankruptcies within corporate groups. For explanations of securitized tranactions including SPVs, see generally Steven Schwarcz, *Structured Finance: A Guide to the Principles of Asset Securitization* (2d ed. 1993); Steven Schwarcz, "The Alchemy of Asset Securitization" [1994] 1 Stan. J. L. Bus. & Fin., 133, 135, 150-51; Calir Hill, "Securitization: A Low Cost Sweetener for Lemons" [1996] 74 Wash U. L.Q. 1061.

[154] In the case of *Polly Peck International Plc* (In Administration) (No. 3), Re [1996] 1 B.C.L.C. 428 (Ch D) the English court confirmed the respecting of the separate corporate personality of companies in the context of using SPVs and insolvency (where it was not a fraudulent transaction). In refusing to confuse the offshore special purpose vehicle with the parent company, the judge took into acount the commercial practice of using SPVs for this type of transaction (see Gabriel Moss, "(Case Comment) Recent Developments in Cross-Border Insolvency Issues" Insolv. Int. 1997, 10(8), 57-58; Denis Petkovic, "(Case Comment) Piercing the Corporate Veil in Capital Markets Transactions", I.B.F.L. 1996, 15(4), 41-43; Chizu Nakajima, "Lifting The Veil", Comp. Law. 1996, 17(6), 187-188).

[155] Thus, for instance, in re Buckhead America Corporation (161 B.R. 11 (Bankr. D. Del. 1993) ("Days Inn case") the court did not accept the claim that one of the entities comprising the group, a solvent SPV should stay out of a substantive consolidation order, reaching the conclusion that creditors were relying upon the unified assets of all of the debtors when doing business with each of the individual debtors (see further on the Days Inn case and on its implications on structured finance transactions in Jeffrey E. Bjork, "Notes & Comments, Seeking predictability in bankruptcy: an alternative to judicial recharacterization in structured financing" [1997-1998] 14 Bankr. Dev. J. 119).

In other examples a particular contributory party (or the group as a whole) may have abused a foreign failing member and should therefore bear responsibility for its debts. This may involve a collapse of all relevant components or only that of the specific subsidiary (the failing debtor). An example for a total collapse could entail a parent situated in country X and a subsidiary in country Y for which the parent was deeply involved in obtaining credit. In the course of that the parent misrepresented the legal status of the subsidiary and its financial situation, misleading creditors to believe that they are dealing with a greater company, and that the subsidiary is actually an integral part of the parent. Following the group collapse, the parent, although insolvent, is in a better financial state than that of the subsidiary. A fair distribution in this case, would mean having the assets of the foreign parent available for distribution to the subsidiary's creditors as well. Yet, the fact that the group had dealings in more than one country would suggest that conflicting national insolvency rules may be involved, barricading any appropriate and effective solution to the matter.

Cases such as *Deltec*[156] demonstrate the problems that may arise when the collapse involves an insolvent subsidiary and a solvent parent (within an MCG)[157]. It was claimed there that the entire multinational group (including U.S. and Canadian affiliates) should bear responsibility for the debts of the Argentinean subsidiary, basing this assertion on 'enterprise law' rationales. The Argentinean court concluded that the group was a "unified socio-economic entity" and referred generally to the abuses of multinational enterprises[158]. However, the legitimacy of the decision was highly debatable and it was commented elsewhere[159] that the case did not present simply a legal question, but rather grave national interests. This case shows the difficulties in giving effect to a conclusion that a certain affiliate located abroad is indeed responsible for creditors' losses as the enforceability of the local decisions in

[156] Compania Swift de la Plata, S.A. Frigorifica s/convocatoria de acreedores, 19 J.A. 579, 151 La Ley 516 (1973) [hereinafter: the decision of the Argentinian court in Deltec]. The decision is translated in Gordon, "Argentine jurisprudence: The Parke Davis and Deltec cases" [1974] 6 Law. Am. 320. See also the case of Bhopal (see the judgment of the High Court of Jablapur, on appeal from the order of the Bhopal District court (Union Carbide Corporation Gas Plant disaster at Bhopal India in December 1984 634 F. Supp 842 (SDNY 1986)). See also Symposium, [1985] 20 Tex. Int'l L.J. 267-340; K. Hofstetter, "Multinational Enterprise Parent Liability: Efficient Legal Regimes in a World Market Invoironment" [1990] 15 North Carolina J. of Int. Law and Comm. Reg. 299 (approaching the multinational enterpise parent liability topic exemplified by the Bophal case, from an efficient perspective); Muchlinski, "The Bhopal case: controlling ultrahazadous industrial activities undertaken by foreign investors", [1987] 50 MLR 545).

[157] See Prototype D (*supra* chapter 1 section 1.6, in particular note 152).

[158] The decision of the Argentinian court in Deltec (note 156 above).

[159] See Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 664.

the foreign states was not trivial[160]. In addition, it demonstrates the problem of having conflicting laws, where one state presumes abuse while the other regards the decision as violating most basic notions of morality and fairness, and views it as possible "confiscation of property"[161].

5.2.4.4 National laws' approaches

National laws provide certain remedies to situations of corporate group abuse in the course of insolvency. It has been mentioned in the beginning of this discussion[162], that even in legal systems wedded to the strict application of the entity doctrine (e.g., the English legal regime) it is possible to use doctrines such as the 'wrongful trading' and 'shadow directors' in order to impose liability upon a group member as well as piercing the corporate veil in exceptional cases. Apparently, the term 'shadow director' may include a parent company. Thus, a parent company can be held liable on the basis of its involvement in the management of the subsidiary, and where it had been negligent with regard to the solvency of the subsidiary[163].

However, English courts have resisted attempts to lift the veil and treat a closely integrated group of companies as a single economic unit on the basis of perceived injustice, and emphasized the greater importance in respecting the separate legal existence of such companies once they became insolvent[164]. It is also unclear how willing will courts be to use the statutory 'lifting of the veil' (the wrongful trading provision and the concept of a 'shadow director') to make a parent company liable for a subsidiary's debts, and in which circumstances this will be possible[165]. Indeed, the

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[160] After the Deletc decision, further litigation developed both in Argentina and in New York, involving inter alia questions of the enforceability in New York of the Argentine decree (see Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 667-668).

[161] Rosenn, "Expropriation in Argentina and Brazil: Theory and Practice" [1975] 15 Va. J. Int'l L. 277, 314.

[162] See section 5.2.4.2 above.

[163] See s.214 of the English Insolvency Act, 1986; see generally on wrongful trading and the shadow director concept in Davies, Gower Company Law (note 33 *supra* chapter 1), p. 196-198.

[164] The strict adherence to entity law with regard to corporate groups was expressed in Adams v. Cape Industries plc [1990] B.C.L.C. 479 (C.A.). See also Polly Peck International Plc (In Administration) (No. 3), Re [1996] 1 B.C.L.C. 428 (Ch D); Ord v Belhaven Pubs Ltd [1998] B.C.C. 607; Gabriel Moss, "(Case Comment) Recent Developments in Cross-Border Insolvency Issues",Insolv. Int. 1997, 10(8), 57-58; Denis Petkovic, "(Case Comment) Piercing the Corporate Veil in Capital Markets Transactions", I.B.F.L. 1996, 15(4), 41-43; Chizu Nakajima, "Lifting The Veil", Comp. Law. 1996, 17(6), 187-188).

[165] See Davies, Gower Company Law (note 33 *supra* chapter 1), p. 197-198 (asserting that it remains to be seen whether the courts will take the opportunity afforded by the wrongful trading provisions to rationalise the legal position of groups of companies).

Cork Committee (mentioned earlier[166]) recognized the potential for the abuse of the corporate group and observed that, even with the introduction of wrongful trading, the law would remain in an unsatisfactory state[167].

More comprehensive solutions to the above scenarios can be found in the New Zealand and the American regimes referred to previously in this work[168]. Under New Zealand legislation it is possible to impose liability upon a related company for the debts of a company being wound up. This is done by using the 'contribution order' in circumstances of involvement or misconduct towards the debtor at stake[169]. It is at the court's discretion to order that the related company pay the debtor's liquidator the whole or part of its debts. As aforementioned, it is alternatively possible, in the appropriate circumstances, that the assets and debts of a related company will be pooled together with the debtor, winding up both companies as if they were one[170]. The court must consider whether the extension of the subsidiary's bankruptcy is just and equitable, and desirable for the protection of creditors, while taking into account the set of factors delineated in the Act. That is, the extent to which the related company took part in the management of the company being wound up, its conduct towards the creditors, and the extent to which the winding up is attributable to the actions of the related company. The court is also authorised to consider such other matters as it thinks fit[171].

There is no equivalent of contribution orders under American bankruptcy regime. However, substantive consolidation provided in the U.S. regime is also available between a debtor and a non-debtor[172]. Other remedies are available such as voidable preference provisions[173] and the doctrine of fraudulent transfers[174].

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[166] *Supra* chapter 4 section 4.3.4.
[167] Chapter 51 of the Cork Report (note 176 *supra* chapter 4).
[168] See *supra* chapter 4 sections 4.1.3.3 and 4.3.4 , and sections 5.2.2.5, 5.2.3.2 above.
[169] Section 271(1)(a) of the New Zealand's Companies Act 1993.
[170] *Supra* chapter 4 section 4.3.4.
[171] Section 272(1) of the New Zealand's Companies Act 1993.
[172] See In re 1438 Meridian Place, N.W., Inc., 15 Bankr. 89 (Bankr. D.D.C. 1981); In re Crabtree 39 Bankr. 718 (Bankr. E.D. Tenn. 1984); Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 439-440.
[173] Blumberg, Bankruptcy (note 43 *supra* chapter 1), chap. 9.
[174] *Id.*, chap. 7.

With regard to inter-company claims, some national regimes allow to differ in priority intra group claims[175]. For instance, American courts have been using their powers under the Bankruptcy Code to impose subordination of claims on equitable grounds[176]. Thus, courts are allowed to inquire into the conduct of the parties and the nature of the financial arrangement which gave rise to the debt and defer the debt to the claims of the external creditors. Subordination is discretionary and may be ordered in a wide variety of circumstances where equitable principles so require, that is where the conduct of the parent has been in some way unscrupulous[177].

5.2.4.5 The need to address the issue of abuse within a global approach

Evidently, unfairness and abuse may exist in the context of insolvencies within MCGs. As some of the affiliated companies are located in different states the conflicting laws and the jurisdiction issues undermine the ability to provide an adequate and just solution by putting additional barriers to getting access or to enforcing judgments against contributory parties[178].

In addition, in the case of assets manipulation within a global context, the ability to get hold of all the group's resources is jeopardized since assets are located in various states, with different approaches to the issue of separate personality and limited liability. This may lead as well, to prejudice of creditors dealing with the group and incapability to eventually distribute the MCG's assets equally amongst all parties involved. Indeed, in the case of *BCCI* (where money was circulated among the various entities), the elements of abuse and fraud led parties and courts to agree on a global concept of a joint pool of assets[179].

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[175] See UNCITRAL Legislative Guide (note 58 *supra* chapter 2), p. 279. Under some insolvency laws that provide for consolidation, intra-group obligations are terminated by the consolidation order (see *supra* chapter 4 section 4.3.4).

[176] 11 U.S.C. s 510(c). See e.g. US v. Noland, 517 U.S 535 (1996).

[177] On subordiantion in the U.S. see Blumberg, Bankruptcy (note 43 *supra* chapter 1), chap. 3.

[178] Foreign courts may deny jurisdiction using doctrines such as the forum non convenience or the public interest factor, thus disallowing the choice of jurisdiction from claimants as weaker parties (see e.g. In re Union Carbide Corporation Gas Plant disaster at Bhopal India in December 1984 634 F. Supp 842 (S.D.N.Y. 1986). See also K. Hofstetter, "Multinational Enterprise Parent Liability: Efficient Legal Regimes in a world Market Environment" [1990] 15 North Carolina J. of Int'l Law and Comm. Reg. 299; P. Muchlinski, "Corporations in International Litigation: Problems of Jurisdiction and the United Kingdom Asbestos Cases" [2001] 50 ICLQ I).

[179] See *supra* chapter 4 section 4.3.5.

This vulnerability of the MCG to abuse and fraud and the additional inherent obstacles to the provision of remedy in these cases suggest that it is most desirable to bridge over gaps in national laws converging the wide differences in bankruptcy and company law regimes specifically with regard to the effect of a corporate group abuse in the event of insolvency. Furthermore, it would be beneficial to provide a solution and guidelines on the international level which would precipitate linking the fragments of the group that are spread between the states on national levels.

Also, a global approach that can hold related companies responsible for the faults of others in the state of insolvency may create an 'incentive' for MCGs to continuously monitor and supervise the activities of companies within the group, and to take early measures in the case of financial difficulties of one of its members[180]. Thus, it can reduce manipulations from an early stage of the distressed business. It can be provided alongside other guidelines and principles designed to enhance good behaviour ('corporate governance') within multinational enterprises (such as provided by the OECD[181]). Naturally, an insolvency regime will deal with the MCG behaviour only after the harm was done to make ex-post controls through liability rules and other mechanisms available on the international level to control corporate group behaviour.

Existing models to cross-border insolvencies do not deal with the issue of group liability[182]. The UNCITRAL Legislative Guide provides a review of possible approaches to the treatment of corporate groups[183]. This is an important aspect of an international tool which may improve harmonization between national laws. In any case, the Guidelines do not provide recommendations regarding a preferable approach in this regard.

It is submitted that, the issue of group liability should indeed be addressed on the international level (in the sense that a universal view to the matter should be taken), and within the scope of insolvency. Such mode of operation is a fundamental cornerstone for just and fair multinational insolvency regime. It would enable equitable consideration of the entire bulk of parties involved and their interests and will deter those in control of MCG from abusing or manipulating the corporate form. It is clearly one of the strengths a global approach may present, that it can better deal

[180] See UNCITRAL Legislative Guide (note 58 *supra* chapter 2), p. 277.
[181] See OECD guidelines (note 33 *supra* chapter 1).
[182] See *supra* chapter 2 sections 2.4.3.3, 2.4.4.3 and 2.4.5.3.
[183] Note 58 *supra* chapter 2, at p. 276-279.

with strategic manipulation compared to a 'component' based approach that considers each component of the group separately, always 'dividing' the group between the countries within which they operate.

5.2.4.6 Adequate tools

A variety of tools- contribution orders, pooling and the subordination doctrine, can amply protect stakeholders affected by abuse and unfairness within MCGs. As was suggested elsewhere[184], the 'contribution order' mechanism is the most effective one and may promote fair results in situations of abuse within a group in the course of insolvency. The rational here being that creditors are not to be granted an independent cause of action. Rather, liability should be imposed by paying of a contribution to the subsidiary's assets. This would reduce litigation and associated costs[185] and would eliminate entirely the risk of a double recovery[186]. Most notably, by avoiding separate action by individual creditors, the approach will help to maintain the fundamental principle of Pari Passu, and will preserve the procedural unity of liquidation proceedings and the collective regime of insolvency. The amount of contribution to be granted may differ according to the circumstances. That is, the degree of abuse performed by the contributory party and the effect this had on the financial condition of the subsidiary should be taken into account[187].

Notwithstanding the above, a contribution mechanism should be cautiously applied in a global approach. The fact that we deal with foreign entities may entail difficulties in obtaining all relevant information and more importantly clear and truthful account of the events that preceded the failure[188]. This is especially relevant with regard to the

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[184] Muscat, The Liabiliy (note 44 *supra* chapter 1), p. 302-303.
[185] See *supra* chapter 4 section 4.2.1.
[186] Otherwise, if the holding company's behaviour also constitutes a breach of duty to the creditors, both the creditors and the subsidiary may be able to sue (see Muscat, The Liability (note 44 *supra* chapter 1), p. 302).
[187] See Muscat (*Id.*), p. 303-305, 389-390, 415, 435-436, and note 2 p. 304, explaining that liability need not necessarily be co-terminus with the subsidiary's inability to settle its debts, and that the concept of giving discretion to courts in this regard goes along with the application of statutory provisions allowing English courts discretion when providing remedies in the course of insolvency, such as the fraudulent and wrongful trading provisions. In addition, it accords with the way U.S. courts exercise discretion when they provide a remedy in the 'piercing the veil' cases, and with the New Zealand approach providing the contribution mechanism that may be applied in order to pay the whole or part of the debts of a related company, according to the courts' discretion (see *Id.*, note 1 and 3, p. 304. See also section 5.2.4.4 above).
[188] See section 5.1.3 above.

interests of stakeholders related to the contributory party. In addition, as the approach aims at applying to as many legal regimes as possible it should provide clear boundaries and safeguards for the implementation of such a mechanism. It should appreciate the fact that it is a matter of substantive law and that imposing liability on affiliates may be regarded as rather drastic. Accordingly, a global approach should adopt a set of clear and well defined guidelines to accompany a contribution tool[189]. These guidelines may be counted as exceptions to the limited liability rule, in the context of insolvency within an MCG.

In this respect the guidelines provided in the New Zealand Companies Act[190] combined with more specified factors to assist in identifying circumstances in which group liability should be imposed can delineate proper substantive group liability standards within an international approach. For that purpose, an integration of the factors extracted from the types of abuse we have considered above with the broader guidelines of the New Zealand's Act would be suitable. Thus, for instance, courts will be directed to take into account "the conduct of the related company towards the creditors of the company in liquidation"[191], while in exercising their discretion they would take into account factors such as whether such conduct involved misrepresentation of the group to creditors in a serious and consistent manner, or whether liabilities were purposely insulated into separate entities. Or, in evaluating "the extent to which the related company took part in the management of the debtor"[192] they will look at circumstances such as intrusive domination of the parent in the subsidiary[193]. Ultimately, an overall view of the contributory party's conduct and involvement in the insolvent subsidiary should be taken.

This way, the court will be given discretion to evaluate the circumstances and interests involved for the purpose of achieving an equitable result, yet it will be guided by specified factors, ultimately resulting in greater certainty.

Furthermore, in the context of abuse within the MCG, a global approach may also adopt the option of pooling assets and debts together (as was already suggested with

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[189] On the issue of certainty and predictability see further in *infra* chapter 6 section 6.2.
[190] See section 5.2.4.4 above.
[191] Section 272(1) of the New Zeland's Companies Act, 1993.
[192] *Id.*
[193] See Muscat, The Liability (note 44 *supra* chapter 1), p. 304-305, 389-390, 415, 436 proposing the specific factors that can be used in exercising of the court's discretion.

regard to the strongly integrated case scenario[194]). Similarly, such a dramatic mechanism should be carefully applied. Clearly, the circumstances should be examined meticulously concluding whether a joint pool or otherwise contribution order is more suitable to address the abuse within the group, in the event of insolvency (of any part of the group). In essence, where the abuse was part of a strategy aimed at disregarding the corporate form (including for instance the circulation of money between affiliates) resulting in strong integration between the affiliates, this should lead to a pooling order rather than contribution. It will then converge with the goal of economic efficiency as was discussed above[195].

A relevant factor will also be whether the contributory party is insolvent. However, this should not be a decisive one[196]. It may be that at the particular time of opening insolvency proceedings against the subsidiary the contributory party is allegedly insolvent, however in fact the group was closely integrated and this affiliate is either deemed to fall into insolvency shortly or it might be that its insolvency cannot be ascertained. Hence, once again, the approach should avoid a 'black or white' rule. It should depend on the situation. If it is a matter of a truly stable entity it might be inadequate to drag an affiliate into the insolvency, and then a contribution concept may be more adequate. Conversely, there may be cases in which it will be more adequate to order contribution where the contributory party is insolvent, since for instance the companies were not integrated or the contribution was only partial and there is no sense in pooling all proceedings together. In this case the debtor will compete in the liquidation of the affiliate claiming that the latter should be liable to pay any of its debts.

Another issue to consider is how to address the conflict of interests between creditors and shareholders of the contributory party and the subsidiary's creditors. If the contributory party is insolvent or if a contribution order sought from the company threatens that company's solvency then the contribution order prejudices bona fide creditors and shareholders. A similar question emerges with regard to a pooling order when certain creditors have dealt with the contributory party on a separate basis (as

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[194] See *supra* chapter 4 sections 4.3.5- 4.3.7.
[195] See *supra* chapter 4 section 4.3.
[196] Conversly, Muscat argues that substantive consolidation would be proper only in the event of the insolvency of the holding company and should then only affect those affiliates which have become insolvent. As long as the holding company remains solvent, a rule regarding the holding company's liability should provide an adequate remedy (Muscat, The Liability (note 44 *supra* chapter 1), p. 462).

was previously discussed[197]). It has been argued[198] that it is more reasonable to prefer the equally "innocent" creditors of an abused subsidiary rather than the creditors of the defaulting affiliate. However, it is arguable whether the position of bona fide creditors and shareholders of the affiliate should be undermined. It seems more adequate that all interests will be taken into account in a decision, striking the balance between the two sets of stakeholders[199]. In this regard the integration between the companies, the way the affiliate was represented to its own creditors and their point of view will all be relevant factors. In certain circumstances a court can reach the conclusion that a separate claim against the affiliate rather than a contribution order or a pooling mechanism is more suitable. It may also be the case that the interests of the rest of the group's creditors (when there are other affiliates and creditors as well) would conclusively tilt the scale.

A pooling mechanism should be also apt to deal with the manipulations involving assets diversion or the use of affiliates to manipulate the group's financial resources, as it should be able to include remote affiliates as well. For instance, a finance unit, allegedly operationally separate from the group, but in fact an instrument for diverting assets may also be included in the pooling. Such an affiliate could be financially sound, even purposely structured to be 'insolvency remote' (for instance, an SPV to whom assets were shifted, while misleading creditors to believe the assets were part of the group's estate). However, the circumstances of the case should still be thoroughly examined and a proper balance should be struck between the interests of the insolvent group at stake and the interests of the operationally or insolvency remote affiliate and its creditors. If, for instance the creditors of the remote affiliate did not take part in the manipulation and were dealing with the affiliate separately from the group, or if the affiliate is solvent and has a separate business going on and critically the assets that were diverted can be reasonably identified, then presumably it will be more justified to file separate claims against such affiliates to recapture assets rather than throw all assets together.

Finally, the equitable subordination doctrine should also be available in the cross-border case involving a corporate group, modifying the pari passu principle to enable

[197] See sections 5.2.2 and 5.2.3 above.
[198] See Muscat, The Liability (note 44 *supra* chapter 1), p. 457.
[199] See Farrar, Corporate Governance (note 10 *supra* chapter 3), p. 246-247 and the New Zealand's case laws cited there, clearly stating that such equities will have significant input to the court's decision to make an order but will not necessarily be decisive.

to defer a contributory party's claims (as long as there are such claims) to those of external creditors. Similarly to our previous discussions, it is suggested that clear guidelines will state the circumstances in which subordination should be imposed, based on the factors that were considered above.

5.2.4.7 The implementation of the tools in the international scenario

As was suggested above[200], the implementation of joint administration in the international case, and in particular substantive consolidation, will be most effective if the operation is 'centralized'. This concept will be appropriate for the scenario of abuse as well. Accordingly, the court which deals with the group's insolvency should be able to extend its jurisdiction over remote affiliates to the extent that such affiliates were involved in a manipulation scenario.

Where pooling will be appropriate due to reasons of abuse, it will be even more critical to have enforceable legal rules to enable this mechanism, rather than using ad-hoc tools[201]. The difficulties in achieving a consensual agreement in these sorts of cases might be even more prominent. Here, it may be that the entities' businesses can in fact be identified and thus addressed separately (so that it will not be a matter of impracticality that will drive the parties to agree on a 'single choice' solution, assumingly beneficial to all stakeholders). In considering linkage between affiliates in the situation of abuse very different interests may be involved, including completely opposite wishes on the part of creditors of separate companies. The need in such instances for one authorized body to be able to impose an adequate solution, while considering all relevant circumstances and balancing between the interests is clear[202].

The implementation of contribution and subordination mechanisms, in the scenario where the contributory party (or the remote affiliate) is solvent, does not involve means of coordination, since there is no administrator involved in the part of that entity (as it is not under insolvency proceedings). Rather, the court handling the insolvency case should be given the authority to give orders directed at the affiliate,

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[200] See *supra* chapter 4 sections 4.1.3.6 and 4.3.7.
[201] See *supra* chapter 2 section 2.4.2, and *supra* chapter 4 section 4.1.3.4.
[202] See in this regard Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2313-2314. Prof. Westbrook convincingly explains that universalism's single court and single law are transparently better suited to sorting out the liability of various elements in a worldwide corporate group in such circumstances.

imposing either a contribution to the debtor (or debtors) debts or the subordination of the contributor's party's claims to those of external creditors. These mechanisms as delineated above should be embraced by the global approach and be available universally.

The notion of international jurisdiction (already proposed) would then be extended to provide that the court who handles the proceedings (those of the subsidiary or any part of the group that is jointly placed under insolvency) will be empowered to decide not only on the way to handle the proceedings but also on questions relating to the protection of creditors from other affiliates' manipulations. Judgments given in this respect should then be internationally recognized and enforceable in other states where contributory parties or remote affiliates are located. This concept will be rooted in a combination of two concepts. One is the above-mentioned idea of international jurisdiction applied to the case of insolvencies within MCGs (that is, having one particular court that is entitled to handle the insolvency proceedings of an MCG member or a group of members). The other is the idea that the court of a host country in which a subsidiary was located (here the subsidiary in insolvency or a number of subsidiaries subjected to a joint process) should be authorized to decide on the issue of an affiliate's liability for the subsidiary's debts[203]. As a result, the court handling the insolvency of the MCG (or of any member within it) should be given authority to handle all insolvency related matters, including group liability and subordination. Where it is impossible to assert the place in which supervision should be held, it was suggested to have alternative solutions[204]. If a supervisory court could not be agreed upon (in cases where there is more than one entity collapsing) close coordination should be applied[205]. For the purpose of imposing liability, such claims will be handled separaelty by the courts of each subsidiary with maximum cooperation among the various proceedings.

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[203] See K. Hofstetter, "Multinational Enterprise Parent Liability: Efficient Legal Regimes in a World Market Environment" [1990] 15 North Carolina J. of Int'l. Law and Comm. Reg. 299, 327-328, claiming that efficiency calculus favors host country jurisdiction over both host country subsidiary and the multinational enterprise's parent company for matters of abuse. The host country courts have, inter alia, better access to evidence and witnesses with regard to the actions subject to adjudication (which primarily occur in the host county). It also allows a consolidation of the often similar liability actions brought against a subsidiary and its parent.

[204] See *supra* chapter 4 section 4.1.3.8.

[205] *Id.* See also *infra* chapter 7 section 7.4.

5.3 Summary

Exploring the goal of fairness in the context of insolvency regimes reinforced what was established earlier regarding economic efficiency. That is, a global approach can offer a range of important tools and prove advantageous over and above other systems. Essentially, a global model embracing a centralized approach will be able to project the way the MCG operated and the way it had dealings with creditors in its ordinary course of business onto handling of its insolvency. Therefore, by mirroring the business activities prior to the collapse it will better accord with creditors' expectations. It will also enable a 'view from above' on the entire process. However, such approach should be applied carefully, providing protective measures to ensure that creditors' voices are heard, adequate representation is given to all stakeholders, and that a solution which is compatible to the specific scenario is imposed.

Furthermore, a global approach should take into account creditors' views and their reliance on a specific entity or rather the group as a whole, when considering the more interventionist mechanisms. Yet, this should only serve as a supporting measure to the objective test based on the economic realities of the case. Finally, it was proposed how a global approach can deal with unfair behaviour and abuse of the corporate form in the context of an international insolvency.

Chapter 6

Forum Shopping, Predictability and State Sovereignty

6.1 Preventing transnational forum shopping

6.1.1 Introduction

There is widespread consensus that forum shopping should be prevented[1]. It increases uncertainty, it erodes the principle of finality, it diminishes predictability of the application of the law to particular facts, it destroys 'decisional harmony' and it puts a premium on legal inventiveness in invoking jurisdictions[2]. The EU Regulation in devising an international model for insolvencies involving Member States explicitly states that "It is necessary for the proper functioning of the internal market to avoid incentives for the parties to transfer assets or judicial proceedings from one Member State to another, seeking to obtain a more favourable legal position (forum shopping)"[3].

The question is hence whether and how a global approach can avoid or at least reduce the phenomenon of creditors' and debtors' forum manipulations in relation to insolvencies within MCGs.

6.1.2 Illustrating the forum shopping phenomenon in several cases of insolvencies within MCGs

In the case of *Eurofood*, mentioned previously in this work[4], concurrent proceedings were opened against the company - in Italy (by the Italian administrator), as well as in Ireland (by creditors of this subsidiary)[5]. The Italian administrator's incentive in challenging the Irish appointment was presumably to facilitate the restructuring of the

[1] See *supra* chapter 3 section 3.3. Though it has been observed in the past in English case law that forum shopping should not be a matter for indignation and that it is merely the prerogative of a plaintiff (see The Atlantic Star [1974] A.C. 436, 471), recent cases have made it clear that the privilege of a party to bring proceedings in a different jurisdiction should be controlled (see Bell, Forum Shopping (note 45 *supra* chapter 1), p. 18; HIB v Guardian Insurance [1997] 1 Lloyd's Rep 414, 417; Meridien BIAO v Bank of New York [1997] 1 Lloyd's Rep 437, 442, 446).

[2] See Bell (*Id*).

[3] Recital 4 of the EU Regulation (note 75 *supra* chapter 2).

[4] See mainly *supra* chapter 2 section 2.4.3.3, note 54 *supra* chapter 4 and section 4.1.3.8 and *supra* chapter 5 section 5.1.4.

[5] Eurofood IFSC, Re (Trib (I) 19 February 2004 [2004] I.L.Pr.14); Eurofood IFSC Limited [2004] B.C.C. 383.

remaining operations of Parmalat[6]. The creditors' motivation was to preserve their control over the subsidiary, to ensure that a representative will protect the interests of the creditors of the subsidiary itself separately from the rest of the group and to make sure that all Eurofood's assets will be subjected to the Irish jurisdiction[7]. Apparently, the fact that the group had presence in more than one place, and that the parties had competing interests relevant to the subsidiary's insolvency and the future of the group as a whole, increased the likelihood of forum shopping and cross-border insolvency jurisdiction battles. Each of the parties presented to the corresponding court a 'story' showing evidence why the COMI of the subsidiary was located in the particular location, convincing the court that it should assert jurisdiction over that company's insolvency[8].

Similarly, in *DaisyTek* MCG[9], there were attempts to commence proceedings against subsidiaries of the group in particular forums (France and Germany)[10], while at the same time administration orders were given against these subsidiaries in the UK[11] with the motivation of facilitating a unified restructuring of the entire group (thus attempting to place all proceedings under a single forum)[12]. At a certain point, concurrent proceedings took place with regard to the same companies, belonging to a single group[13].

The case of *Cenargo* MCG[14] was described as "an example of unsuccessful forum shopping"[15]. The English parent (Cenargo International Plc) and various subsidiaries

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[6] However, it has been commented that this motivation is rather inconvencing since Eurofood IFSC was not an operational unit, merely a financing vehicle with no part to play in any restructuring (apart from providing additional funds for the admnistration) (see *GLOBALTURNAROUND,* "Italian and Irish courts clash over Parmalat", April 2004, issue 51, p. 3).

[7] See *supra* chapter 5 section 5.1.4.

[8] Eurofood IFSC Limited [2004] B.C.C. 383; Eurofood IFSC, Re (Trib (I) 19 February 2004 [2004] I.L.Pr.14).

[9] See mainely *supra* chapter 4 sections 4.1.3.7 and 4.1.3.8, and *supra* chapter 5 section 5.1.4.

[10] In re Daisytek ISA Ltd (Tribunal de Commerce, Cergy-Pontoise, 1 July 2003); In re Daisytek ISA Ltd (Dusseldorf County Court, 19 May 2003; 10 July, 2003).

[11] Daisytek- ISA Ltd [2003] B.C.C. 562 (Ch D).

[12] See *supra* chapter 4 section 4.1.3.7.

[13] See *supra* chapter 5 section 5.1.4.

[14] Re Norse Irish Ferries & Cenargo Navigation Limited (unreported, 20 February, 2003); In re Cenargo International Plc, 294 B.R. 571 (Bankr. SD.N.Y. 2003).

[15] Susan Moore, "Global Crossing versus Cenargo The right way and the wrong way, *GLOBALTURNAROUND,* January 2004, issue 48, p. 8; LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 189, 191-193, 204,-205. See also the attempt of Yukos, the Russian oil company to seek chapter 11 protection in the US. Yukos had no business interests in the US apart of bank accounts established in the eve of filing the bankruptcy petition. Eventually, the US court dismissed the case on the grounds that the company did not have enough of a presence there (*GLOBALTURNAROUND,*

presented Chapter 11 petition in the U.S., even though the only connection the group had to this country were bank accounts opened shortly prior to the opening of proceedings and the fact that certain creditors (a group of bondholders) were based in the US. However, the group was essentially European[16]. Subsequently, a major leasing creditor presented a winding up petition in England and the English court appointed provisional liquidators over Cenargo. Each of the relevant courts restricted the other party from pursuing proceedings in the other jurisdiction. It appeared that Cenargo (the debtor) foreseeing its collapse was forum shopping and preferring the US proceeding (as it enables the directors to remain in control through the 'debtor in possession' notion[17]). Eventually, the US court suspended the Chapter 11 proceedings finding that the "centre of gravity" of the cases was in the UK but reserved jurisdiction over the US litigation. The 'battle' was solved by the respective judges holding a conference call in which they agreed a number of key jurisdictional differences[18]. Ultimately, a joint administration took place in the UK enabling successful rehabilitation of many companies in the group[19]. Absent such an initiative, the conflict could have been continued with greater costs, inefficiency and potential unfairness to creditors. A-priori the group could have commenced bankruptcy proceedings anywhere as long as it satisfied a particular forum that it had some assets or business in that location according to this forum's point of view and legal policy.

In cases involving U.S and Canadian affiliates, plaintiffs very often shop for the US forum, where parent's responsibility to the debt of its insolvent subsidiary is sought. The reason for this is that Canadian courts are more wedded to the entity doctrine, while the U.S. legal regime provides more tools to deal with such situations[20]. Namely, creditors of affiliates in these jurisdictions forum shop for the country which provides more profitable results for them.

"Yukos court battle over chapter 11", February 2005, issue 61, p. 1,3; *GLOBALTURNAROUND*, "Yukos abandons Chapter 11"", April 2005, issue 68, p. 7).

[16] See Susan Moore, "Cenargo: A Tale of two courts, comity and (aleged!) comtempt!", January 2004 (http://www.iiiglobal.org/members/committee_c/cenargo.PDF); Shando, Sandy and Tett, Richard, "The Cenargo Case: A Tale of Conflict, Greed Contempt, comity and Costs", Insol World- Fourth Quarter 2003, 33-35.

[17] *Id.*

[18] Insolv. Int. 2003, 16 (6), 47-48 (NOTICEBOARD- Co-operation Between Courts); Susan Moore, "Cenargo: A Tale of two courts, comity and (aleged!) comtempt!", January 2004 (http://www.iiiglobal.org/members/committee_c/cenargo.PDF).

[19] See *supra* chapter 4 section 4.1.3.7.

[20] Jacob S. Ziegel, "Corporate Groups and Crossborder Insolvencies: A Canada- United States Perspective" [2002] 7 Fordham J. Corp. & Fin. L. 367, 388-391.

The above examples demonstrate that a complex structure of enterprises with a presence in various legal regimes coupled with a variety of interests pertaining to issues related to the insolvency of the group (or any of its components) may increase the likelihood and facilitate considerably forum shopping by debtors as well as creditors.

6.1.3 The need to identify the 'most appropriate' forum to handle the insolvency process and to have standard means to deal with issues pertaining to the MCG insolvency

Certain international models to cross-border insolvencies attempted to tackle the problem of forum shopping (with regard to single debtors), by embracing the concept of identifying a single place which represents the centre of main interests of the debtor[21]. Under the EU Regulation, concurrent proceedings can be opened or should be recognized only in well defined circumstances, and they only have limited effects[22]. Also, the COMI is defined according to 'real' connections to the place rather than pure formalistic factors. Thus, it is not accepted under this approach that proceedings will be opened where there is only a thin nexus between the debtor and the jurisdiction[23].

However, this concept is applied to single debtors as separate entities. There is no consideration in this regard to the group as a whole and the effect of the economic truth and inter relations within a group on the 'proper' location of the group's insolvency or that of any of its members[24].

An MCG can then engage in preplanning of its insolvency and therefore produce, for instance, a formal organizational structure that only remotely reflects the actual state of affairs. With a careful planning an MCG may succeed in avoiding unfavourable jurisdictions or otherwise subject certain subsidiaries to particular insolvency regimes, albeit these subsidiaries being in reality closely connected to the rest of the group and operating elsewhere. When the system provides for an easy separation of related companies within an MCG, debtors and creditors will be bound to engage extensively in jurisdictional quarrels regarding the appropriate location. As was noted in another

[21] See the idea of identifying the COMI of the debtor in *supra* chapter 2 sections 2.4.3.2.
[22] *Id.*
[23] Though the presumption is in favour of the registered office of the company (*Id.*).
[24] *Supra* chapter 2 section 2.4.3.3.

EU Regulation case involving an MCG[25], EU courts should avoid motivating parties to take artificial actions and to take advantage of formal corporate structures in order to arrange for a relevant corporate body to be subjected to the 'proper forum'.

Incentives to forum shop could be diminished by the harmonization of substantial laws relating to insolvency and corporate groups[26]. Indeed, when the case involves comparable insolvency laws the factor of forum shopping will be less pronounced[27]. Therefore, the global system should aspire to promote harmonization of the rules pertaining to MCGs' insolvencies, providing adequate means to deal with situations of abuse or intermingling of assets and debts[28], thus producing equivalent protections across countries. The fact that such a solution is applied or proposed from the international level to the national regimes enables it to override national differences and maintain a standard rule. It will thus be able to prevent more effectively situations where legal regimes provide entirely different solutions to the same scenarios. As a consequence, forum shopping could be reduced.

However, even if substantial laws will be the same, still parties may find other motivations in choosing one forum over the other, such as the geographic location, the character of the judicial institution and so on[29].

Under these circumstances, it seems that forum shopping considerations (as were other goals discussed previously) lead to the conclusion that a direct international jurisdiction rule should be applied to cases of groups. That is, the centralized approach proposed that will provide which forum should handle the group process is needed. It should rely on the organizational structure of the group[30] in distinguishing between cases that call for handling vs. supervising the process from one single place as well as identify those circumstances in which no unification or centralization are needed[31].

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[25] Brac Rent-A-Car Inc, Re [2003] B.C.C. 248.

[26] See Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), p. 112, explaining that "incentives for MNEs to exploit differences in national regulations could be removed by the harmonization of tax laws, disclosure standards, labour regulations and corporate liability regimes".

[27] See, for instance, Robert K. Rasmussen, "The Problem of Corporate Groups, a Comment on Professor Ziegel" [2002] 7 Fordham J. Corp. & Fin. L. 395, 403-404, indicating that the matter of parties structuring corporate groups' operations as to ensure that each entity is handled by the 'appropriate' legal system may be less significant in Canada-US cases whose laws are functionally similar. But, see text preceeding note 20 above.

[28] See *supra* chpater 4 section 4.3, and *supra* chapter 5 section 5.2.

[29] Note 47 *supra* chapter 3.

[30] See *supra* chapter 1.

[31] See *supra* chapter 4 sections 4.1.3.6- 4.1.3.8, and *supra* chapter 5 section 5.1.5.

The strength of a global approach in this respect is that it can disregard "pure" formalities that may obscure the 'real' state of affairs of the group at stake (for example, where the group was fragmented into separate entities yet all operated a single business directed and managed from a single location). By definition, manipulations can be done more easily under a 'formal' regime. If the 'economic truth' is disregarded and no weight is given to the real connections between the companies at hand unjust outcomes are more probable, and the difficulties to 'control' manipulations augment. Obviously, when the system being used strives to reflect the state of affairs prior to the onset of the proceedings and makes use for this end of a broader evaluation of the MCG as a whole, debtors and creditors' manipulation will be reduced.

Furthermore, in order to truly overcome forum shopping, the method applied should designate the place to which the group has the strongest connection as the appropriate forum for the handling the MCG's insolvency process. That is, a centre of gravity of the entire enterprise[32]. This way parties will find it more difficult to 'elude' the proper jurisdiction and to choose a different but more favourable one when commencing insolvency proceedings.

It has been argued elsewhere[33] that a 'universalist' system of any sort to cross-border insolvency is, especially in the context of corporate groups, too vulnerable to strategic manipulations since it makes use of a vague notion of "home country" [34]. Accordingly, this argument continues, a 'territorial' regime (in which each country has jurisdiction over the portion of the insolvent multinational firm within its borders[35]) is more suitable to this problem since it disregards the debtor's home country and focuses on the resident assets.

Certainly, any global approach may be subjected to debtors' manipulations, especially in the corporate group case, in which the affairs of the enterprise could be much more scattered in different places and different entities. However, as will be suggested herewith[36], a global approach has the potential of devising measures to deal with this

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[32] In *infra* chapter 7 the identifiaction of the locus of the MCG's centre will be discussed.
[33] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 720-723. See also Lynn M. LoPucki, "Universalism Unravels" [2005] 79 Am. Bankr. L. J. 143.
[34] See *supra* chapter 2 section 2.2.
[35] *Id.*
[36] Section 6.1.4 below.

weakness and at the same time provide the advantage of being compatible with the economic realities. Conversely, a territorial and separable approach leaves to debtors to manipulate with assets location and subsidiaries operations knowing that no consideration will be given for the purpose of jurisdiction to the connections between the constituent companies.

6.1.4 Overcoming manipulations targeted at the location of the centre of the group[37]

A rule of international jurisdiction that identifies a single place as the centre of the entire group may also be susceptible to manipulations. Debtors, anticipating a collapse (and knowing that a single location will be designated as the centre from which subsequent proceedings will be handled) may displace the group's centre to a different location with a preferable jurisdiction. Alternatively, they may use successive filings. Namely, manipulating the order in which the group members file insolvency petitions. For instance, by sequencing the filings of the MCG's members in a way that the parent will come last, debtors can promote the chances of having the entire process already running in a location different than the group's centre (if the rule provides that the parent is the centre of the group)[38]. The complex structure of a corporate group could assist debtors to cherry pick those jurisdictions which are debtor-friendly[39]. This sort of manipulations has been demonstrated in recent cases. In the case of *Cenargo*, the companies opened bank accounts in the U.S. at the eve of bankruptcy[40]. In *Eurofood* proceedings were opened in Ireland in an attempt to prevent the company's centre of main interests being moved by its parent to Italy[41]. In the case of *BCCI*[42] the group's headquarters were moved from London to Abu Dhabi shortly before filing bankruptcy[43].

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[37] The identification of the proper place to handle the MCG's insolvency process will be discussed in *infra* chapter 7.

[38] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 722-723. See also LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 226-230.

[39] See *GLOBALTURNAROUND*, "The new European pastime", March 2004, issue 50, p. 6.

[40] Note 16 above, and accompanying text.

[41] Eurofood IFSC Limited [2004] B.C.C. 383.

[42] Note 155 *supra* chapter 4.

[43] See Richard Donkin, "Troubled BCCI Shifts Base to Abi Dhabi", Financial Times (London), Sept. 20, 1990, p. 34. See also examples of manipulations of the forum given in LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 226-230.

Furthermore, both creditors and debtors can attempt manipulating the forum by presenting a biased account to the courts[44] regarding the issues pertaining to the identification of the group's centre. A rule of immediate recognition as provided in the EU Regulation arguably increases the problem since the first to open proceedings captures the entire process into his insolvency[45]. It might be hence that a court opening a process relies on incomplete information taking a certain view which could sometimes be completely in the wrong direction. Eventually, the case will be dealt in an improper place while failing to achieve the goal of having the insolvency handled in the proper jurisdiction[46]. The Models we have discussed[47] do not offer solutions to such scenarios, not even for the single debtor whose venue was changed prior to the opening of the insolvency proceeding[48].

In order to overcome such manipulations regarding the MCG's centre, a global model should draw a distinction between a cynical attempt to move the centre shortly before insolvency proceedings are commenced and a restructuring of the enterprise for sound commercial reasons before insolvency proceedings. As was stated in the case of Ci4net.com[49] (an EU Regulation case) with regard to alteration of a debtor's COMI, an 'artificial' change of the company's centre would not be regarded as altering the COMI for the purpose of the Regulation, whereas a real move of the centre could[50]. Hence, the place identified as the proper jurisdiction to handle the MCG insolvency process should be the centre of the group for a set amount of time prior to the

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[44] See the debate regarding the facts presented to the English court in the case of *Daisytek* (*supra* chapter 5 section 5.1.4).

[45] Once COMI is established, all other jurisdictions are bound by it, and any challenge can only be made via the original court. It has been pointed out that this could prove to be an Achilles' heel of the entire EU Regulation (see I.F.Flecther, "The Challenge of Change: First Experience of Life under the EC Regulation on Insolvency Proceedings in the UK", Annual Review of Insolvency Law, 2003 (Toronto, Carswell, 2004), 431, 454); see also *GLOBALTURNAROUND*, "Forum Shopping in Europe "is here to stay"", December 2004, issue 59, p. 5).

[46] See the ECJ judgment in *Eurofood* stating that main insolvency proceedings opened by a court of a Member State must be recognised by the courts of other Member States, without the latter being able to review the jurisdiction of the court of the opening State (Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397, at paras. 38-44).

[47] See *supra* chapter 2.

[48] As was observed elswhere the criteria set by the ECJ in the case of *Eurofood* can be also exploited to manipulate the forum. A group can move its COMI to a convenient location while making sure the place is widely known (thus ascertainable) to third party creditors (see C. Rapinet & I. Tucker, "European Court of Justice resolves Parmalat jurisdictional battle under EC Insolvency Proceedings Regulation" Sweet & Maxwell's Company Law Newsletter issue 10/ 2006, p. 2).

[49] Ci4net.com Inc & Anor [2005] B.C.C. 277

[50] See also Richard Tett, Nicola Spence, "COMI: PRESUMPTION, WHAT PRESUMPTION" Insolv. Int. 2004, 17(9), 139-141.

insolvency[51]. In this regard, in order to resolve situations where there was more than one such place within this period of time a model should presume that the venue in which the centre was residing longer is the COMI[52]. However, the reasons for the change should be closely examined and if it is apparent that the centre was genuinely placed at the new jurisdiction (though this was for a shorter period, as the company entered insolvency) this place should be designated as the proper venue.

This will add to the demands that should be set upon debtors with regard to notifications and representations towards creditors on the whereabouts of the centre of the group, as was previously proposed[53], and to the burden that should be set upon both parties and courts to carefully examine all evidence and the various potential interests involved[54].

A global model should also take into account in this respect the entire group situation and preferably place all affiliates under one insolvency regime while determining the proper forum for the entire group. Thus, it could avoid the downsides of successive filings by debtors as mentioned above.

However, the model should allow for some modifications in the designated venue, in order to accommodate the dynamics of the MCG's insolvency's process. And, it should be possible to challenge in real time the decision regarding jurisdiction. Indeed, when the proceedings are lawfully but inappropriately located it should be possible to ask for a transfer of the insolvency proceedings to be conducted from the

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[51] In Ci4net.com mentioned above (note 49) the judge stressed that the COMI must have some degree of permanence (it should not move around with the location of the directors). Certainly, moving the centre of main interests after lodging a request to open insolvency proceedings (but before the proceedings are opened) should not affect the decision regarding the appropriate jurisdiction. As was explained by the ECJ in the case of Staubitz-Schreiber, a transfer of jurisdiction from the court originally seised to a court of another Member State on the basis of the debtor moving its centre after submitting the request would be contrary to the objectives persued by the Regulation, mainely the intention to avoid incentives for the parties to transfer assets or judicial proceedings from one Member State to another, seeking to obtain a more favourable legal position (Staubitz-Schreiber (Case C-1/04) [2006] (http://curia.eu.int).

[52] Resembling the English rule that resolves a jurisdictional dilema which arises when the debtor's residential address or business address (or for a company- the 'registered office') has changed from one insolvency district to another within a 6 months period prior to the presentation of insolvency petition. The insolvency rules provide that the court within whose jurisdiction the debtor has been resident for the longest time prevails even if it is not the current address at the time of filing (Insolvency Rules 1986, rr.6.9(4), 6.40(2)(c); see also Fletcher, The Law of Insolvency (note 148 *supra* chapter 2), p. 131-132).

[53] See *supra* chapter 5 section 5.1.5.

[54] See *Id.*

proper jurisdiction[55]. Thus, the model will incorporate a useful mechanism that will provide the needed flexibility in the jurisdictional rule to overcome manipulations and to accommodate the changes in the insolvency scenario[56]. It will enable to remedy situations in which it can be shown that the court was presented with incomplete information in the first place as mentioned above. However, this power given to the insolvency courts should be carefully used bearing in mind that if proceedings are passed on to another state it would implicate on the legal regime applied to the case[57], and that it may involve significant additional costs.

Finally, another device that should be used in order to quickly and efficiently resolve jurisdictional battles once they have started is communicating directly between parties and courts. This tool was used to resolve the jurisdictional battle in *Cenargo* mentioned above[58]. It should be explicitly provided that in cases of connected affiliates, each having proceedings commenced or heard in a different court, communication should be used as a fast track to prevent forum shopping and prolonged battles.

6.2 Predictability and Certainty

6.2.1 The vulnerability of a global approach

As was suggested throughout this study so far[59] a suitable and comprehensive global approach demands a certain degree of flexibility and should provide a variety of alternative solutions that can be well matched to different cases. For instance, certain circumstances will require an interventionist approach to regard separate entities as if they were one single enterprise, while in other scenarios a simpler joint administration will be needed[60]. In the relevant cases the insolvency process of an entire group should be handled from a single location and in other cases separate proceedings are more

[55] Similar to the power given to English courts in domestic bankruptcy cases. The courts have a general power of transfer that may be used to relocate proceedings in the court in which they can be most suitably and conveniently administered and a specific power to transfer proceedings in cases where it transpires that the proceedings have commenced in the wrong court (see Fletcher, The Law of Insolvency (note 148 *supra* chapter 2), p. 133-135, 582-583).

[56] For instance, certain entities may join the process at a later stage despite efforts to place the entire group under insolvency at once.

[57] See *supra* chapter 5 section 5.2.1. This is not the case in a domestic setting.

[58] Section 6.1.2 abvoe. Communication is a method provided within the Model Law and the ALI Principles (see *supra* chapter 2 section 2.4.4 and 2.4.5).

[59] See *supra* chapters 4 and 5.

[60] *Id.*

suitable[61]. Naturally, flexibility has its toll on certainty and predictability. If a highly flexible approach is being implemented, such that it can accommodate differently every slightly distinct scenario, there is a good chance that even the most proficient of practitioners will find himself in the muddle regarding the outcome of a particular insolvency. Moreover, the fact that decisions related to the MCG insolvency (such as responsibility for affiliated companies' debts) are made by the courts after the event of insolvency may undermine predictability and introduce some amount of uncertainty[62].

In addition, prima facie, any approach that suggests a mechanism which attempts to unify insolvency proceedings of separate entities may possibly be less predictable compared to a 'segregating' approach that regards each company as the separate entity it was designed to be at the first place. It may be reasonable to assume that lenders know which entities are indebted to them[63]. Hence, they can predict where and how they will be able to claim their debts should the company they were involved with face insolvency. Typically, they would not expect, for example, to be mingled with other creditors from other companies.

Finally, an approach that may involve some changes to the current practices regarding insolvencies within MCGs will presumably produce more uncertainty and decrease predictability as it modifies a familiar mode of operation.

6.2.2 A need for a solution to improve predictability

Indeed, the above potential drawbacks should veritably be taken into account when proposing a global approach. Nevertheless, it is argued herewith that a global approach wili ultimately improve certainty and predictability.

The system as it currently is cannot be truly considered as a stable and predictable one. In fact, parties as well as appointees and courts are presently quite 'confused' as to the approach they should exercise in relevant cases. Indeed, in recent cases involving MCGs we are faced with different and sometimes contradicting results and approaches. For example, in a number of cases involving pan-European corporate

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[61] *Id.*
[62] See Uncitral Legislative Guide (note 58 *supra* chapter 2), p. 277.
[63] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 751 (thus arguing that a territorial regime offers greater predictability to lenders).

groups we see the court promoting a sort of global approach, trying to 'collect' all the group's components together and handle the proceeding in one country under a single administrator[64]. Other cases revealed the court's sensitivity to the problem of forum shopping and manipulations in relation to the 'appropriate forum' in cases involving affiliated multinational companies[65]. In a rather different approach, national insolvency courts dealing with insolvency of corporate groups' members have resisted the jurisdiction of another member state's court demonstrating confusion as to the application of the EU Regulation in cases of corporate groups. The French court in Cergy Pontoise in the case of *Daisytek*[66], for instance, while trying to look after the domestic creditors, appointed its own administrators and permitted the selling of the French assets separately[67]. The French jurisdiction was eventually overruled[68], however at a certain point the question of the subsidiaries' COMI was given different and contradicting results[69]. In the recent decision of the ECJ in *Eurofood* the court apparently took an 'entity' line of approach, however, leaving it rather vague and unpredictable as to the particular factors that will suffice in order to rebut the presumption that a subsidiary's COMI is in the country of its registered office. Evidently, as for this time the EU Regulation does not provide reliable and clear means to deal with MCGs[70].

In many other cases involving MCGs the courts and the parties designed ad-hoc solutions in the lack of appropriate tools for these particular cases[71]. Faced with the need to prevent jurisdiction battles and lower realizations as a result of the breaking up of insolvent (related) companies, administrators and courts used various means to enhance cooperation and to actually link between affiliates applying a de facto unified

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[64] See e.g. cases mentioned in notes 60-75 *supra* chapter 4 and accompanying text.
[65] See, for instance, *In re* Brac Rent-A-Car Inc [2003] EWHC (Ch) 128; [2003] B.C.C. 248, and TXU Europe German Finance BV, Re [2005] B.C.C. 90 (Ch D).
[66] In re Daisytek ISA Ltd (Tribunal de Commerce, Cergy-Pontoise, 1 July 2003).
[67] See also the contradicting decisions with regard to the issue of jurisdiction over insolvent members of a corporate group in the case of Eurofood (Eurofood IFSC Limited [2004] BCC 383; Eurofood IFSC, Re (Trib (I) 19 February 2004 [2004] I.L.Pr.14).
[68] In re Daisytek-ISA Ltd (Cour d'Appel, Versaille, 4 September 2003). The decision is pending in the French Court de Cassation.
[69] The French and German courts in first instance opening local insolvency proceedings against the relevant subsidiaries, and the UK courts subjecting the same entities to English jurisdiction (Daisytek-ISA Ltd [2003] B.C.C. 562 (Ch D)); In re Daisytek ISA Ltd (Tribunal de Commerce, Cergy-Pontoise, 1 July 2003); In re Daisytek ISA Ltd (Dusseldorf County Court, 19 May 2003; 10 July, 2003)).
[70] See also *supra* chapter 2 section 2.4.3.3.
[71] See *supra* chapter 2 section 2.4.2.

solution to such cases. Yet, ad-hoc solutions are, by definition, less predictable than pre-designed tools applicable to all similar future cases.

The practical necessities, therefore, lead parties to apply 'global methods' to the MCG cases. However, with the lack of available model that clearly outlines the rules relevant to the particular case of an MCG, the solutions applied are more informal and unplanned, resulting with a significant degree of uncertainty and unpredictability. Thus, currently parties are not in a position to predict whether a future MCG's insolvency will be handled co-ordinately, where the proceedings of each of the companies will be handled and which laws will apply. The business may be one that was coordinated and headquartered from a specific country, yet separate proceedings will be taking place in several states with no cooperation between the courts and administrators, in the lack of any successful initiative to promote coordination. Or, it may be handled with close cooperation. The outcome is hard to predict.

In addition to the above, the diversity in national laws' treatment of corporate groups' insolvencies result with uncertainty regarding the substantial rules that will apply to the case. Even within a specific national regime there may be significant degree of ambiguity with respect to questions of insolvency law in the context of corporate groups[72].

Therefore, in order to achieve predictability a global approach is needed. It can offer specific solutions to the cases of MCGs' insolvencies, precisely expressing what will be the applicable rules to these cases, when a unified solution should be imposed, in what ways and in which circumstances. This way, participant parties can know in advance, in a sufficient degree of clarity, what to expect if a future failure of an MCG occur[73]. Furthermore, courts will be able to achieve consistent outcomes and thus more rapidly develop a body of precedents eventually building up to a reliable and steady system.

[72] See *supra* chapter 3 section 3.2, *supra* chapter 4 section 4.3.4 and *supra* chapter 5 section 5.2.4.4.

[73] As stated in the UNCITRAL Legislative Guide, it is important that an insolvency regime address matters concerning corporate groups (although the issues pertaining to groups are very complex) in sufficient procedural detail to provide certainty for all parties concerned in commercial transactions with corporate groups (UNCITRAL Legislative Guide (note 58 *supra* chapter 2), p. 277).

6.2.3 Overcoming the flaws and providing adequate tools

Evidently, the current legal situation regarding MCG insolvencies is rather unclear. It is suggested, though, that constructing a specific method to cope with insolvencies within MCGs in a unified and universal manner would eventually be more predictable than other possible methods.

For this purpose, a global approach should first be careful not to become too flexible or vague 'on account' of promoting predictability. With too many potential scenarios to which a model should provide compatible solutions, the outcome will be total case-by-case approach, thus defeating predictability. However, as was suggested earlier in this work, several key factors pertaining to the MCG insolvency can be used in order to classify a number of main representative classes. We have accordingly described the variety of relevant MCG insolvency scenes by identifying prototypical organizational structures and the corresponding insolvency scenarios. Hence, we have enabled some measure of generalization across cases and scenarios[74] and we have built upon these Prototypes the proposed characteristics of a global approach[75]. Using such Prototypes, a global approach can offer on the one hand a reasonable range of alternative combinations, and on the other hand can narrow this to a small number of typical cases to hence, reduce vagueness. This can serve here as a measure for enabling predictability in determining on the appropriate solution to be imposed on a particular case.

In any case, a global approach will entail some amount of uncertainty, since it does not suggest a 'one size fits all' kind of solution. It seems, though, that it is more of the type of 'predicted uncertainty', which could still be taken into consideration by the various relevant parties.

Second, the approach should go along with creditors' legitimate expectations[76]. As was demonstrated[77], in the relevant circumstances, linking between affiliates in the course of insolvency will better reflect the enterprise's true way of operation, ultimately, enhancing predictability. The companies' places of incorporation and the way the enterprise constructed its operations in terms of components' formation may be misleading in many cases and reflect an altered 'reality' of the way the group

[74] See *supra* chapter 1.
[75] See *supra* chapters 4 and 5.
[76] As was also suggested in *supra* chapter 5.
[77] See *supra* chapter 5 sections 5.1 and 5.2.

operated its businesses. If for example, a group operated in its ordinary course of business as an integrated business and represented itself (e.g., to the public, to customers, to creditors, etc.) as such, it will be more predictable for the parties involved in the group's insolvency that the proceedings will be handled in an integrative way even though separate entities are involved. It will also reflect more accurately the creditors' expectations. A system that aims to depict as accurate an image as possible of the MCG at hand can thus be compatible to creditors' expectations rather than contradict them, thus promote certainty and predictability.

Evidently, though, the EU Regulation that has provided a rule of international jurisdiction and a uniform code of choice of law rules (for the cases of single debtors' cross border insolvencies), in order to promote certainty and predictability[78], actually left a significant degree of vagueness concerning the assertion of the principal jurisdiction. How one decides the location of the main court is not well defined, leaving a lot of discretion to local judges. Thus it results with confusion and undermines predictability[79]. A lesson should be learned from this experience and a clearer definition of what will be regarded as the group's insolvency proper venue should be provided[80]. This, together with adequate rules to facilitate the ascertaining by creditors of which corporate entity they were dealing with and where was its proper location (for the purpose of insolvency)[81] will promote predictability and certainty as to where the insolvency process will take place and the laws that will apply to these cases.

Increasing harmonization of laws via the application of standardized rules to matters relating to the MCG insolvency provided by a global approach, as was mentioned

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[78] See I.F.Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL CROSS-BORDER INSOLVENCY A Guide to Recognition and Enforcemnt, 15, 30-31.

[79] See *GLOBALTURNAROUND*, "French breakthrough for Euro Regulation", October 2003, issue 45, p. 9.

[80] The importance of assigning jurisdiction in a certain and predictable way was emphasized, for example, with regard to the Brussels Convention on Jurisdiction and Judgments in Civil and Commercial Matters, now translated into European Council Regulation 44/2001 [hereinafter: The Brussels Regulation]. The ECJ stressed this goal as a major concern of the convention (see in Case 241/83, Rosler v Rottwinkel [1985] ECR 99, 127). It was noted that 'a plaintiff must be sure which court has jurisdiction. He should not have to waste his time and money risking that the court concerned may consider itself less competent than another' (Schlosser Report [1979] OJ C59/71, 97.; see also Bell, Forum Shopping (note 45 *supra* chapter 1), p. 53-54). The identification ohf the MCG COMI will be discussed in *infra* chapter 7.

[81] See *supra* chapter 5 section 5.1.5 and *infra* chapter 7.

above[82], will serve predictability as well, since creditors will be able to assess what means could be applied in the case of the MCG failure, regardless of the location in which the proceedings will actually take place.

6.3 State sovereignty and differences in national regimes

6.3.1 Introduction

As was indicated previously in this work, inconsistency (of an international system) with domestic regimes may present both practical and theoretical problems[83]. Essentially, the question posed for our particular concern was whether a global approach can offer rules that will be both justifiable (although interventionist to some extent), and widely accepted. It is argued herewith that a well designed global model that is based on the set of propositions outlined in the conclusions chapter of this work that derive from the above discussion of the insolvency goals[84] can be indeed practically feasible and theoretically justifiable. In fact, it is the most adequate solution to the treatment of insolvencies within MCGs that operate within a diversified scene of national policies. This is the way to overcome national differences and hence offer a more effective and fair system in the insolvency context.

6.3.2 The practical issue

It is certainly a fact that current local insolvency laws differ[85]. In the scope of MCGs' insolvencies (as opposed to single companies) the gaps between national laws are even wider. While, in the case of a single debtor there is a rather broad consensus about the basic fundamentals of the conduct of its insolvency proceedings[86], there are considerable differences among national laws in their dealings with group matters in

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[82] See section 6.1.3 above.
[83] See *supra* chapter 3 section 3.3.
[84] See propositions summerized in the conclusions chapter (*infra*).
[85] See *supra* chapter 2 section 2.4.1, and *supra* chapter 3 section 3.2.
[86] The imposition of collective proceedings which stops individual creditors' collection efforts and attempt to preserve whatever going concern value the firm (the debtor) may have for the benefit of all interested parties. However, even with regard to single debtors there are still differences even within the European community as to which of the founding principles should be predominent and the extent to which the insolvency system should adhere to any of these fundamentals (see Wessels, Bob, "International Jurisdiction to Open Insolvency Proceedings in Europe, In Particular Against (Groups of) Companies" Working Papers Series, Institute for Law and Finance, Johann Wolfgang Goethe University (http://www.iiiglobal.org/country/european_union/InternJurisdictionCompanies.pdf); see also *supra* chapter 3 section 3.3).

the context of insolvency. This is attributed to the lack of conformity in the views regarding the basic issues of limited liability and separate entity[87]. With a single debtor, international approaches could at the least impose models that provide with compromised frameworks for cross-border insolvency. These models can refrain from attempting to harmonize laws either by setting complementary provisions (such as, easy access, recognition, assistance and ways of cooperation[88]) or by employing more comprehensive regimes which include direct jurisdiction and choice of law rules[89]. For the group scenario merely agreeing upon a basic system for addressing the MCG case on the international level (even in its 'compromised' forms) may be deemed very difficult.

Nation states may be reluctant to subject local companies (that are in fact members of MCGs) to any global mechanism that will regard such companies as fragments of some greater body (a group). They may not wish to be in the position where local courts or representatives must cooperate with other foreign authorities, for instance in providing them information or a standing in court with regard to the future of the (local) debtor company.

The problem augments if the model adopts direct international jurisdiction (and applicable law) rules. Namely, a centralized approach as was suggested above[90] has more chances of collision with national regimes. In general, a regime that affects the jurisdiction of the courts may be seen as a direct challenge of state authority. This may be even more emphasized in the group scenario (compared with the single debtor situation) since the reason and justification for the altering in the designated forum (to handle the MCG insolvency process) will stem from the inter-relations among separate entities rather than the operations of a single company. As was proposed previously[91] it is the economic truth of the enterprise as a whole that will ultimately point out to the proper venue for the MCG insolvency. It will not originate solely from a separate consideration of each company as a stand alone. Thus, even if a specific company is considered as situated in a certain country it may be subjected to the

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[87] *Supra* chapter 3 section 3.2.
[88] As is the concept underlying the Model Law (note 143 *supra* chapter 2). See also Fletcher, Insolvency (note 4 *supra* chapter 2), p. 497-498, explaining the idea of the Model Law as a procedural framwork to cross-border insolvencies.
[89] See the EU Regulation's approach (*supra* chapter 2 section 2.4.3).
[90] See *supra* chapter 4 sections 4.1.3.6- 4.1.3.8.
[91] See *Id.*, and *supra* chapter 5 section 5.1.

supervision of another court in a different country to which the group as a whole has the strongest connection. States may regard this as significantly interfering with sovereignty power and courts' jurisdiction over domestic companies.

Moreover, a model that includes rules which directly intervene with the corporate separate personality device, as are the rules dealing with 'group liability'[92], obviously presents the highest difficulty when these rules contradict with substantive national laws. This is where the issue extends beyond mere administration of the insolvency process and enters the zone of examining shareholders' behaviour, imposing (in the relevant circumstances) responsibility upon affiliates in the course of the insolvency process. Here, a wider or relatively flexible approach with regard to group liability may directly collide with those national approaches that more strictly adhere to the entity doctrine[93].

Furthermore, competition among nations for foreign investment might spur 'a race for the bottom' among states[94] thus aggravating the disinclination to accept a global approach. Some countries may firmly protect the 'corporate form' within their domestic legal regimes in order to attract new investors[95], and thus be unwilling to participate in a global model affecting corporate groups. Most probably, they would be reluctant to agree on a system that on occasions let creditors get access to related companies' assets or receive contribution to the debtor's assets from another entity within a group, or participate in any model that in a given case may demand the transfer of proceeds to a common pool of assets.

However, adhering to the limited liability concept might only be part of the problem. Some countries (not necessarily particularly regarded as limited liability friendly) may also demonstrate a sort of tendency to adhere to their national laws and protect local stakeholders, especially where they are related to separate entities (that operated within national borders). Such inclination may pose a threat on the acceptance and

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[92] See *supra* chpater 5 section 5.2.4.

[93] See *supra* chapter 3 section 3.2 and supra chapter 5 section 5.2.4.4.

[94] See K. Hofstetter, "Multinational Enterprise Parent Liability: Efficient Legal Regimes in a World Market environment" [1990] 15 North Carolina J. of Int. Law and Comm. Reg. 299, 323-324.

[95] It was obsereved that if a jurisdiction were to introduce a regime that was hostile to groups (for example by making a parent company liable for the obligations of subsidiaries) that might deter multinationals from investing in certain jurisdictions (Milman, D., "Groups of Companies: The Path towards Discrete Regulation" in Milman, D. (ed.), *Regulating Enterprise* (1999), p. 236; The DTI Consultative Document, Modern Company Law For a Competitive Economy (March 1998), ch. 4). See also, Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), p. 45-46. Muchlinski describes the current business environment as geared towards investment promotion and economic deregulation.

viability of applying a global model. Indeed, in certain occasions, courts 'ring fenced' assets belonging to local subsidiaries located within their jurisdictions refraining from transferring such resources to a joint administration appointed by a foreign regime[96]. It happened even in a case of a strongly intertwined group, where it was unreasonable to treat the constituent companies separately. In the *BCCI* case[97], some countries within which subsidiaries or branches of the group were situated, adopted such 'grab rule' approach allowing local assets to be used to satisfy local creditors in local proceedings with little regard for proceedings or parties elsewhere[98].

All this may undeniably affect the feasibility of imposing a global approach that will be widely accepted.

6.3.3 The theoretical issue

An argument that goes against the legitimacy of a global approach may be that an attempt to impose a sort of universalist approach[99] (applied to the case of MCGs' insolvencies) will undermine and suppress domestic laws, which are still accepted to be necessary and significant on the international commercial arena[100]. Mainly, the idea of having a single insolvency system applied to cases of international insolvencies of MCGs may be regarded as a detriment to national regimes' role.

In particular, an attempt of a global approach to include means for consolidating proceedings of related companies substantially (in the appropriate circumstances)[101], or impose inter-group liability in the relevant scenarios[102] can be regarded as severely interfering with national policies.

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[96] See the decision of the French court in first instance in the case of Daisytek. The court had resisted the jurisdiction of the UK court, appointing its own administrators to the French subsidiary and selling the French assets separately (In re Daisytek ISA Ltd (Tribunal de Commerce, Cergy-Pontoise, 1 July 2003).

[97] Note 155 *supra* chapter 4.

[98] A substantial number of countries, including the United States, insisted on giving priority to local claims against local assets despite the fact that the group's funds were extensively commingeled (see Jay Lawrence Westbrook and Jacob S. Ziegel, NAFTA Insolvency Project, [1997-1998] 23 Brook. J. Int'l L. 8).

[99] See *supra* chapter 2 section 2.2.

[100] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2298- 2299.

[101] See *supra* chapter 4 section 4.3.

[102] See *supra* chapter 5 section 5.2.4.

Providing a framework for cooperation and coordination between affiliated companies' proceedings while the law applied to the insolvency case continues to be national law is less problematic in this regard. National laws still have a major role in applying their rules within the international framework. However, imposing additional legal means that are not currently available in every legal system (which may be a potential candidate for participating in a global model) is naturally more challenging, since it directly overrides the domestic systems.

6.3.4 The ability of a global model to be acceptable within nation states and to leave sufficient room for domestic policies

It should be accepted within a global approach that the corporate form and limited liability notions are rather sensitive and obtain varied solutions in different legal regimes[103]. Accordingly, the approach should be prudent in this regard and respect the corporate form as its basic position. It should clearly make the distinction between the scenarios in which only minor means of unification between affiliated companies proceedings will suffice, and the cases in which an interventionist approach will be needed. Countries will then know the boundaries of a global approach and the specific circumstances and justifications for applying the more intrusive tools in a given international insolvency case involving an MCG.

In addition, as was demonstrated[104], a systematic examination of typical scenarios deriving from actual cases and data of insolvencies within MCGs (i.e., their unique circumstances and problems, the particular solutions that have been applied and the outcomes accomplished) enables to locate some sort of conventional 'common ground' of necessary steps and frameworks that need to be imposed on the particular situations. These cases and scenarios showed that a global approach is in fact for the benefit of stakeholders, if applied prudently and embrace certain characteristics and tools to reflect the economic truth and the specific needs of the group at hand. If aimed to reflect truthfully the real needs and issues ought to be solved for all parties' interests, a global approach may presumably reduce countries opposition to surrender control.

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[103] See *supra* chapter 3 section 3.2.
[104] See in *supra* chapters 4 and 5 (for instance section 4.1.3.7 and 5.1.4).

Ultimately, national regimes should have little problem with accepting an approach that provides international framework for handling MCGs' insolvencies if it imposes its solutions only to the appropriate sorts of MCGs that really demand global insolvency means. More often than not the 'minor' global means for cooperation will suffice. In these cases, the group's members although jointly administered will not be lumped together and will not be treated as a single entity[105]. Cooperation will be granted only for the benefit of the group as a whole and of each member thereof without compromising the specific interests of each member's stakeholders. National policies and views with regard to the fundamental issue of limited liability remain 'untouched'.

The more interventionist means will be provided in order to give solutions to the exceptional cases where the economic truth or behaviour within the group demand the disregard of the corporate veil at least to some extent. We have demonstrated that even with regard to group liability there are some common grounds among national laws[106]. Most legal systems will enable imposition of liability upon a shareholder in some (even if rare) circumstances[107]. Nevertheless, we have suggested extending this basic approach to a range of circumstances in which group liability should be imposed[108]. In addition, it was proposed to include within a global approach methods for adequately dealing with situations of strong integration in the course of the insolvency process[109]. Such methods are in their essence based on particular relatively advanced legal systems (in these aspects)[110]. However, the idea is that such rules and mechanisms will promote the integrity of the international insolvency system. The global model will be then comprehensive and will be well-equipped to address the various aspects pertaining to the MCG insolvency, providing effective protection to the different stakeholders that were involved with the MCG and enabling its fair and efficient administration in the event of a general default.

The fact that national regimes might be unmotivated to improve domestic laws' solutions to the special case of insolvency within a corporate group if anything suggests that the initiative should come "from the top" and not "from the bottom". In

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[105] See *supra* chapter 5 section 5.2.1.
[106] See *supra* chapter 5 section 5.2.4.2.
[107] *Id.*
[108] *Supra* chapter 5 section 5.2.4.
[109] See *supra* chapter 4 section 4.3.
[110] See mainly *supra* chapter 4 section 4.3.4 and *supra* chapter 5 section 5.2.4.4.

other words, we should not rely solely on the legal situation as it is now, but rather strive to improve it universally, with a view of harmonizing systems[111]. In addition, in order to provide sufficient solutions for maximum cooperation among states, an international regime is essential. Solutions within national regimes will offer inconsistency and thus ineffectiveness and unfairness in the treatment of the MCG default[112].

It has also been noted elsewhere[113] that, local policies are in any case difficult to apply to multinational companies[114]. Consequently, little surrender of local control will be needed by international governance of multinationals[115]. Allegedly, though, in the case of an MCG it may be that local subsidiaries operated separately and possessed local assets. Countries are asked then not to apply local policies upon a specific member of an international group although this member is in itself a local autonomous company. However, since the proposed approach provides solutions matched to the specific organizational structure of the MCG, those companies that were actually operating separately and were not integrated with the group will indeed be subjected to local laws. Only in integrated groups where the local companies are part of multinational enterprises national laws are restricted to some extent[116]. It is in these cases that there

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[111] See D. Milman, "Groups of Companies: The Path towards Discrete Regulation" in Milman, D. (ed.), *Regulating Enterprise* (1999), p. 236, suggesting that the solution to national legislators' reluctance to regulate the peculiar legal problems posed by the group enterprise lie in regulation beyond the purely national level so as to eliminate potential economic disadvantage. See also Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), p. 45-46, arguing that the development of international law of foreign direct investment would serve to reduce the conflict caused by uncoordinated unilateral state policies. Harmonization of state policies will diminish misuse of internationalization advantages by multinational enterprises deriving from the diversity in national regulations (see further on the theories beyond multinational enterprises' expansion in *supra* chapter 1 section 1.2).

[112] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, 2310-2311, arguing that a universalist system to multinational bankruptcies is essential in order to protect the various stakeholders involved with the company. A territorial regime, under which local policies will apply to the case of the multinational company, is incapable to deal with the way multinational companies actually operate and manage their business. See also *supra* chapter 2 section 2.4.1.

[113] See Jay Lawrence Westbrook, "A Global Solution to Multinational Default" [2000] 98 Mich. L. Rev. 2276, p. 2298- 2299.

[114] Since, for example, the multinational company may have transferred assets out of nation states (*Id.*, p. 2298-2299, 2310-2311).

[115] It has also been proposed there that an international bankruptcy regime can be applied only to companies of a certain size or a certain level of international activity and it can be focused on commercial entities rather than on consumers. This way, interference with domestic regimes in this regard will be minimized (*Id.*, p. 2298- 2299). As has been suggested previously in this work, the aim of the proposed model is to be applicable to all variety of MCGs (see *supra* chapter 1 section 1.3). However, narrowing the model to certain MCGs is a possibility as a second best approach in cases of reluctancy to accept a more comprehensive model.

[116] See *supra* chapter 4.

are less significant implications on local policies applied to local entities (as the entities at stake are not entirely 'local' in essence).

All in all, the idea is to facilitate MCG's insolvency proceedings and promote fairness while 'proceeding with caution' and respecting the corporate identity as a starting point, thus not severely interfering with local traditional corporate theory ideas. In addition, as the approach aims to reflect the economic truth and the specific needs of the group at hand it will not be reckless to predict that it has the potential to be accepted by domestic regimes. Indeed, in some circumstances it is justifiable to restrict some degree of state sovereignty in order to provide adequate solutions to the multinational enterprise in distress, which in turn may convince countries to participate in such a model.

6.4 Summary

The first two issues discussed in this chapter reinforced the need for a global approach, and the advantages it will bring to an insolvency system. It was suggested that it will better deal with forum manipulations (than a territorial separable approach applied to these cases)[117], and that it can provide clearer and more predictable rules, if embracing certain crucial characteristics as proposed[118]. The last issue discussed showed that it will not be reckless to predict that states will be willing to embrace a global approach that cautiously applies its linking mechanisms and respects the corporate form. It was argued, that a global approach is thus both feasible and justifiable to be embraced globally. These assertions add to our previous conclusions regarding our discussion of other insolvency goals, each of which showed the merits of a global approach for insolvencies within MCGs[119].

Throughout the examination of the insolvency goals (in this and the previous chapters[120]) the characteristics of a suitable comprehensive global approach emerged. In the final concluding part of this work these characteristics will be summarised into a structured set of propositions that can guide the construction of a proper global

[117] See section 6.1 above.
[118] See section 6.2 above.
[119] See *supra* chapters 4 and 5.
[120] *Id.*

model. However, before reaching this ultimate point[121] we will address one last critical issue, namely the question of the proper venue[122].

[121] See the conclusions chapter (*infra*).
[122] See *infra* chapter 7.

Chapter 7

Determining the proper venue

7.1 Introduction- the sort of venue we are looking for

Clearly, the crux of a global model that invokes a centralized approach as one of its main features[1] would be the identification of the one location within which proceedings could be centralized (or the location from which they can be supervised). One important derivative of this notion would be the identification of those particular circumstances in which a single venue for the MCG insolvency can not be located. Hence, a valid centralized approach to MCGs will have to provide criteria for identifying this potential locus. Thus far, cross-border insolvency models have not provided an answer for the question of proper jurisdiction to an integrated corporate group[2]. The ALI Principles do allow for a subsidiary to open insolvency proceedings in the parent's jurisdiction, yet this place does not necessarily reflect the centre of main interests of the group as a whole, and it is only provided as an option for the subsidiary[3]. This 'indeterminacy' of the group's 'home country' is in fact one of the major critiques against universalism[4].

While we consider in the next two sections the various options of places to handle or supervise the MCG's insolvency process it will be worthy to bear in mind the main features that are expected to be present in such a place. The test for the chosen forum should obviously be of a kind that will promote the underlying ideas of a global approach and the objectives and advantages it is designated to achieve[5]. Thus, it should lead to the place with the strongest connection to the MCG; namely, there should be a real nexus between the group and the proper venue to handle the joint process (therefore encumbering forum shopping[6]). For that, it should take into account the group's operation as a whole (as opposed to looking for a proper venue for every company separately). Moreover, it is important that the designated venue would be a place easy to identify and to predict, so that it would accord with creditors' expectations regarding the insolvency process' location as well as with the goals of

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[1] See chapters 4-6, passim.
[2] See *supra* chapter 2 sections 2.4.3.3 and 2.4.4.3.
[3] See *supra* chapter 2 section 2.4.5.3. See also text preceding note 41 below.
[4] See *supra* chapter 2 section 2.3.
[5] As were discussed in previous chapters (see *supra* chapters 4-6).

certainty and predictability[7]. In order to comply with creditors' expectations (therefore promote fairness) the chosen place should also reflect the actual way the group was managed and the way creditors have dealt with it[8].

7.2 Alternatives for a proper venue

Thus far, three main factors (or tests) were proposed and used in cases of international insolvency of single debtors to determine issues of international jurisdiction. That is, the debtor's place of incorporation[9], the debtor's centre of main interests (COMI)[10] and the location of "principal assets"[11]. The COMI test seems to be the most prominent as is apparent from its inclusion in existing models for cross-border insolvencies[12].

However, the place of incorporation still retains a role in issues related to cross-border insolvency. Thus, under English law, for instance, a foreign dissolution of a company is recognized when the dissolution has taken place under the law of the country of incorporation[13]. Under the EU Regulation it is presumed that the company's place of registered office is the COMI (which is the test for determining the proper jurisdiction)[14]. Similarly, the Model Law adopts this presumption when designating the country of "main proceedings"[15]. However, the presumption can be rebutted under the EU regulation if there is a proof that the COMI is located in some other Member

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[7] See *supra* chapter 5 section 5.1, and *supra* chapter 6 section 6.1.
[8] See *supra* chapter 5 section 5.1.
[9] Or the 'registered office' (this term is used, for instance, in the EU Regulation (note 75 *supra* chapter 2) Article 3(1)) and in the Model Law (note 143 *supra* chapter 2, Article 16(3)).
[10] The concept originated in the EU Regulation as the test for ascertaining international jurisdiction. The Model Law and the ALI Principles followed and adopted this concept. This already means a widespread use of the COMI concept, within and outside Europe, as the Model Law has already been recognised by a substantial number of countries around the world, and recently was included in the reformed US Bankruptcy Code (see *supra* chapter 2 section 2.4.4.1).
[11] For a summary and explanation of each of these factors see LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 217-221. As explained there each of these tests has been considered in various times and places as the most appropriate basis for international jurisdiction (Prof. LoPucki also distinguishes between "headquarters" and "administrative employees and operations". We will consider these as part of the 'centre of main interests' test).
[12] See note 10 above. However, COMI does not escape from its own inherent difficulties of definition and application (see notes 30-33 below and accompanying text, and *supra* chapter 6 section 6.1.4).
[13] Fletcher, The Law of Insolvency (note 148 *supra* chapter 2), p. 811. See also LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 196; Liza Perkins, A Defence of Pure Universalism in Cross-Border Corporate Insolvencies [2000] 32 N.Y.U. J. INT'L. L. & Pol. 787, 815 (proposing place of incorporation to determine debtors' home countries).
[14] See *supra* chapter 2 section 2.4.3.2.
[15] See *supra* chapter 2 section 2.4.4.2.

State[16]. Thus, it is accepted under these regimes that such formalities as the place of incorporation are not determinative in ascertaining the venue for the insolvency process, but rather functional realities are key factors[17]. Basing the decision regarding jurisdiction merely on these criteria is regarded as insufficient and it is recognized that it can encourage forum shopping by parties initiating insolvency proceedings[18]. Nevertheless, it was recently emphasized by the ECJ in the *Eurofood* case, that substantial evidence is needed in order to rebut the presumption of incorporation[19]. Prior EU Regulation cases showed that judges tend to give lesser weight to the incorporation presumption. For instance, in the case of *Ci4net.com*[20] incorporation was only one of many factors that were considered. It was not regarded as a decisive or predominant factor in determining the COMI[21]. In any case, as has been commented by professor LoPucki[22] 'bankruptcy havens'[23], in which companies chose to incorporate but hold no significant business, still play a role in multinational insolvencies[24]. Indeed, this was criticized as encouraging forum shopping, using these 'bankruptcy havens' as 'rubber stamps' to confirm foreign plans or to take control over bankruptcy cases although there is at the most a nominal headquarters in the

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[16] See *supra* chapter 2 section 2.4.3.2.

[17] See also I.F. Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL CROSS-BORDER INSOLVENCY A Guide to Recognition and Enforcemnt, 15, 25.

[18] The American National Bankruptcy Review Commission, for instance, recommended deleting place of incorporation as a sufficient basis for venue in domestic bankruptcy cases (National Bankr. Rev. Comm'n, Bankruptcy: The Next Twenty Years [1997], 770, 783; see also LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 80). With regard to international insolvencies it was commented that it make little sense to subject an insolvency process to the laws of a particular country (merely because the company registered there) even though the actual commercial life of the company was centred elsewhere (see Jay L. Westbrook, "Theory and Pragmatism in Global Insolvencies: Choice of Law and Choice of Forum" [1991] 65 Am. Bankr. L.J. 457, 486). Under the EU Regulation and the Model Law the fact of incorporation is also not a relevant link for the purpose of opening a secondary or "non main" proceedings (see I.F.Flecther, "The Challenge of Change: First Experience of Life under the EC Regulation on Insolvency Proceedings in the UK", Annual Review of Insolvency Law, 2003 (Toronto, Carswell, 2004), 431, 443).

[19] The exemplifying scenario given is that of a 'letterbox' company not carrying out any business in the country of the registered office (see Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397, para 34-35; see also *supra* chapter 2 section 2.4.3.2).

[20] Ci4Net.com. Inc [2005] B.C.C. 277 (Ch D).

[21] See also Richard Tett, Nicola Spence, "COMI: PRESUMPTION, WHAT PRESUMPTION" Insolv. Int. 2004, 17(9), 139-141. See also the case of Enron Directo (Enron Directo SA, Re (England Ch D, 4 July, 2002) (unreported)) and the case of Re Brac (Brac Rent-A-Car Inc [2003] B.C.C. 248) in which proceedings where opened in the UK for non-UK companies.

[22] LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 193-200.

[23] Such as Bermuda and the Cayman Islands.

[24] Thus, it is explained, in the case of *ICO Global Communications*, for instance, the English court recognized a US reorganization plan of an essentially English corporation although it had little presence in the US, mainly because the plan was also approved by the Cayman Islands and Bermudan courts in

'haven'[25]. It is certainly expected that bankruptcy heavens will gradually lose their practical value, as the 'new' functional test for ascertaining jurisdiction will be embraced by more and more states. To summarize, incorporation is still being used, to a certain extent, as a basis for ascertaining jurisdiction over insolvency cases, yet this factor may often only reflect a legal fiction. As such it enables manipulation of the venue and clearly should not be a proper basis in its own merit.

An even weaker basis for determining jurisdiction (the principal jurisdiction for the insolvent company) is the assets-based test (or any test based on amount of activities). Assets and activities may be spread among countries with none of them having a clear majority. In addition, as was indicated elsewhere[26] some assets could be of mobile nature and even be outside the boundaries of any country[27]. The need to measure and weigh between quantities entails high level of complexity which makes the test a lot less predicted and prone to manipulations. It will be difficult to identify the place in which most of the assets reside, and to predict in advance what will be the evaluation of a future court in this regard. Hence, this test can not accord with the need to meet creditors' expectations and avoid manipulations of creditors and debtors in choosing a preferable forum to open insolvency proceedings[28].

So far we have considered those tests in the context of a single debtor. However, when dealing with a group scenario applying either the incorporation test or the assets-based test to determine the proper venue is even more problematic. The place of incorporation may be different for each entity comprising the group, since we are dealing with a multinational enterprise whose entities are spread among various countries. Keep in mind that our goal here is to find a single focus-point of the entire

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which several companies of the ICO group were incorporated (LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 197-199).

[25] *Id.*, P. 198-199.

[26] See Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 716.

[27] *Id.*, and see the example given there of assets which were leases in satellites orbiting the earth.

[28] Also the more so, it is an insufficient basis for asserting worldwide jurisdiction if the debtor has only some assets in the country, even though it is only a small portion of the debtor's estate. Indeed, the attitude of the American bankruptcy court in the case of Cenargo (In re Cenargo International Plc 294 B.R. 571 (Bankr. S.D.N.Y. 2003)) agreeing to open proceedings against this essentialy English group based on the fact that the debtor had only a bank account in the country was much criticized (see Susan Moore, "Cenargo: A Tale of two courts, comity and (alleged!) contempt!", January 2004 (http://www.iiiglobal.org/members/committee_c/cenargo.PDF); Shandro, Sandy and Tett, Richard, "The Cenargo Case: A Tale of Conflict, Greed Contempt, comity and Costs", Insol World- Fourth Quarter 2003, 33-35; LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 189, 191-193, 204-205).

group. Hence, not only that the place of incorporation test is a formalistic one and is deemed insufficient in determining the jurisdiction for cross-border insolvency cases of single debtors (as explained above), it also prevents the identification of a single venue for the entire group. As aforesaid, a major feature of a desirable venue for handling a group's insolvency is that it will have the strongest connection to the group as a whole. However, MCGs are not incorporated as such in a particular country so there is no single country that can be identified as the place of incorporation of the group[29]. A possible adaptation of the incorporation test to the group scenario could suggest the place of incorporation of the parent of the MCG as the proper venue for the proceedings. However, this could clearly be rejected as it may lead to a completely preposterous situation in which for instance a number of European companies in default are supervised by a Cayman Island court due only to the fact that the parent holding company was incorporated there.

Similarly, group's members may each have its own principal asset or operation location so that no one single location can be identified for the group as a whole. Alternatively, trying to identify a single place as the centre of gravity by summing up the entire group's assets or operations and the proportionate part located within the various entities is also very problematic. It will be difficult to do such a calculation of quantity or value of assets or operations where for instance the entities comprising the group were handling a variety of different operations (e.g., a group of companies that develop IT security mechanism and include both software developing for consumers, software development for industries and hardware development) and accordingly owned different sorts of assets or had different kinds of activities. The need to evaluate very different types of operations makes the process even more prone to uncertainty.

As mentioned in the beginning of this section, the COMI test is the concept underlying major existing models[30]. It is based on the idea that the proposed place for opening

[29] It is possible though to create a supranational entity formed under laws adopted by regional organizations of states, such as the SE and the EEIG (forms adopted by the European Community) as described previously in this work (see *supra* chapter 1 section 1.3). Such supranational entities may be the lead or the head company of a European group; however each entity comprising the group may be registered in a different state. Consequently, there will not be a specific place in which all group members should be incorporated (see Davies, Gower Company Law (note 33 *supra* chapter 1), p. 23-26).

[30] See note 10 above.

proceedings should be the one to which the debtor is substantially linked[31]. Hence, as aforesaid, incorporation is only a presumption, and the mere presence of assets in a particular country is insufficient[32]. In essence, this suggests that courts should look for the centre of the actual main interests of the debtor; however, the definition of such a centre is somewhat vague. Indeed, the EU Regulation does not define what the COMI of a company is[33]. Prima facie, a COMI could be identified according to operations (or assets) or otherwise it could be based on aspects of management.

However, both the Report Virgos/Schmit (1996)[34] and the Recitals to the EU Regulation[35] stress that the COMI should be the place where the debtor conducts the administration of his business on a regular basis and that it should be ascertainable by third parties[36]. Interpretations of the COMI concept embedded in the Model Law have also suggested that it directs courts to consider the country where the debtor's headquarters are located as the country of main insolvency proceedings[37]. The rationale underlying the incorporation presumption discussed above is also derived from the (not necessarily correct) assumption that normally the registered office of the company will accord with the actual head-office[38]. However, as the idea is to look for actual place of main interests and not to be satisfied with a place of incorporation, if

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[31] See I.F. Fletcher, "The European Union Regulation on Insolvency Proceedings" [2003] INSOL INTERNATIONAL CROSS-BORDER INSOLVENCY A Guide to Recognition and Enforcemnt, 15, 25-26.

[32] It is also not enough in order to open a secondary process (see Report Vigros/Schmit (1996) (note 94 *supra* chapter 2) which indicates that an 'establishment' requires a certain amount of organisation and stability. Hence, few assets in the country will not suffice for an international jurisdiction; see also I.F. Fletcher, "The Challenge of Change: First Experience of Life under the EC Regulation on Insolvency Proceedings in the UK", Annual Review of Insolvency Law, 2003 (Toronto, Carswell, 2004), 431, 441).

[33] See *supra* chapter 2 section 2.4.3.2.

[34] Note 94 *supra* chapter 2.

[35] Note 75 *supra* chapter 2. These are the two main instruments for interpreting the EU Regulation.

[36] Report Virgos/Schmit (note 94 *supra* chapter 2); Recital 13 of the EU Regulation (note 75 *supra* chapter 2). See also Virgos, The 1995 European Community Convention on Insolvency Proceedings: an Insider's View, in: Forum International, no. 25, March 1998, p. 13, noting with regard to the need that the place will be ascertainable to third parties that 'the place where the debtor conducts the administration of his business and centralizes the management of his affairs (e.g., contractual and economic activities with third parties) satisfies this requirement; not the place where the assets, whatever their value, are located, not the place where the goods are manufactured (e.g., the place of industrial establishment, etc.)'. See also Fletcher, Insolvency (note 4 *supra* chapter 2), p. 366-368, and *supra* chapter 2 section 2.4.3.2.

[37] See Memorandum from Jay L. Westbrook to the National Bankruptcy Review Commission (July 29, 1997, in National Bankr. Rev. Comm'n, Bankruptcy: The Next Twenty Years [1997], app. E-1 at 7, referring to "the centre of its main interests" as "a concept taken from the European Union Convention on Insolvency and akin to concepts like 'principal place of business' or 'chief executive office'". Professor Westbrook was co-leader of the U.S. delegation that negotiated the Model Law). See also LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 218.

the actual headquarters are located in a different place than the registered office then the former will prevail[39]. Therefore, it seems that in essence, these models seek to look for the real place from which the business of the debtor was managed- an operational headquarters rather than a façade of headquarters, such that can be ascertainable by third parties. A real top-tier management is supposed to be in the chosen venue along with the central administration of the debtor.

It will be suggested herewith that the idea of identifying a COMI for a single debtor- in its interpretation as referring to the operational headquarters of the company being the key connecting factor- could be extrapolated to identifying a COMI for the entire integrated MCG. As will be argued, such an approach will direct the proceedings to the most proper venue when dealing with an MCG, and thus will facilitate the achievement of the main insolvency goals.

Prior to explaining this approach, another option to solve the jurisdiction issue when dealing with MCGs should be mentioned. That is, to look for the COMI of each of the group's members separately, handle the proceedings of each member locally while linking between them via a supervisory mechanism[40]. However, such a solution still requires the designation of a proper supervisory court and therefore will not solve the question of the 'proper venue' (for the principal process). To propose that the parent's proceedings should always be given the supervisory authority means that the principal or coordinating proceedings would not necessarily be handled in the real centre of the group as a whole thus will not achieve the insolvency goals, such as creditors' expectations[41]. The difference from the approach proposed within this study is that the COMI is considered separately with no consideration to the group concept. Hence, it encourages courts to focus on more local interests rather than on the group as a whole and the entire bulk of stakeholders. As such it does not comply with the conclusions drawn from our discussion regarding the benefits of a global approach to these cases[42].

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[38] See Report Virgos/Schmit (note 94 *supra* chapter 2).

[39] See e.g. the decision in Enron Directo (Enron Directo SA, Re (England Ch D, 4 July, 2002) (unreported)). The English court in this case asserted jurisdiction upon a Spanish incorporated company since the actual head office of the company was in England. As appeared from the evidence provided, the entire principal executive, strategic and administrative decisions in relation to the financials and activities of the company were conducted in London.

[40] See Robert Van Galen, "The European Insolvency Regulation and Groups of Companies" October 2003, http://www.iiiglobal.org/country/european_union/Cork_paper.pdf.

[41] See section 7.3 below (particularly text accompanying notes 47-49).

[42] See section 7.1 above.

Furthermore, it falls into the pit of a 'one size fits all' solution which is quite clearly a 'crooked' sort of key to unlocking the problems raised by the diversified scene of MCGs[43].

7.3 The location of the group's operational headquarters as the preferred criterion for determining the proper venue

Since our aim is to identify a single location and preferably place all proceedings of the group's members (which are under insolvency) there, it is suggested to use the concept of a COMI for a debtor in the MCG scenario as well, that is identify the COMI for the group as a whole.

This will accord with the concept of applying a vigorous use of the "doing of business" or "presence" criteria of jurisdiction for the purpose of opening insolvency proceedings in the context of an MCG[44]. Indeed, it has been suggested, with regard to jurisdiction over holding companies in countries where their subsidiaries operate and vice versa (whether creditors of a subsidiary can sue in the home country of the parent) that referring to each company separately or relying on a pure agency relationship might not be the ideal solution[45]. Similarly, a more flexible test should be

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[43] See *supra* chapter 1.

[44] The traditional view of the "doing of business" test with regard to bankruptcy proceedings (of an individual debtor) was expressed in Re Brauch ([1978] CH 316, [1978] 1 ALL E.R. 1004, [1977] 3 W.L.R. 354. It has been held there, that in order to establish that the debtor had 'carried on business in England', within S 4(1) of the English Bankruptcy Act 1914 (now repealed), it was not sufficient to show that he had been running his company's business in England, even if he was the sole beneficial shareholder and in complete control. Rather, the court needs to find that he had been carrying on personally a business of his own in England independently of that of the companies (albeit his modus operandi involved the use of the companies as vehichles for achieving his business objectives).

[45] See P.T. Muchlinski, "Corporations in International Litigation: Problems of Jurisdiction and the United Kingdom Asbestos Cases" [2001] 50 ICLQ I; Muscat, The Liabiliy (note 44 *supra* chapter 1), p. 23; Lawrence P. Kessel "Trends in the Approach to the Corporate Entity Problem in Civil Litigation" [1953] 41 Georgetown L.J. 525, 526-532; J.J. Fawcett, "Jurisdiction and Subsidiaries" [1985] J.B.L. 16; John K. Rothpletz, "Ownership of a Subsidiary as a basis for jurisdiction" [1965] 20 New York University Intramural Law Review 127; Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), chap. 5 and chap. 9 p. 328-329. Certain legal systems have asserted the right to extend their law exterritorialy on the basis of the economic unity of the MCG (see for example Article 10 of the Argentinean Draft Code of Private International Law. The full text of the Code can be found in 24 ILM 269 [1985]; see also Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), p. 138-139). In American law there is a strong tendency towards the application of enterprise law to the problem of jurisdiction over foreign components (see Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 678; Blumberg, The Law of Corporate Groups: Procedural Problems in the Law of Parent and Subsidiary Corporations (1983 supp. 1992), at chs. 3 to 5). This is consistent with the assertion of 'long arm' jurisdiction in the United States and the constitutional guarantee of 'due process' which requires only certain 'minimum contacts' with the forum (International Shoe Co v Washington 326 US 310 (1945); see also Bell, Forum Shopping (note 45 *supra* chapter 1), p. 6, 7 and 11).

applied to the case of relationship between affiliate companies in the context of handling insolvency of an MCG. The focus here should be on the economic reality of the relationship between the parent and subsidiaries rather than looking at each company separately.

Using the 'headquarters criterion' (or the main place of administration of the debtor's affairs) as the key connecting factor for determining jurisdiction in cross-border insolvency in the group case will enable identification of the place of command and control of the entire integrated centralized group[46]. In 'centralized integrated groups' we refer to those cases where the entire enterprise was actually controlled from a single place. Since this situation was influenced inter alia by how creditors dealt with the entities comprising the group[47], it is also plausible to assume that using this definition the group's COMI can be ascertainable by stakeholders that dealt with this sort of enterprise. Accordingly, it is proposed that the COMI of an MCG should be at the place where the high level decision making with regard to the enterprise was performed, namely at the state from which the business (as a whole) was actually controlled and managed. Subsidiaries are generally directed and managed from headquarters of the group enterprise. Headquarters is the brain and nerve centre, while the subsidiaries are the limbs[48]. The headquarters thus reflect the 'meeting point' for the various entities.

Senior decision-takers may typically be concentrated around the parent (the holding company)[49], though this is not always the case. The parent can be situated in one place while the operational headquarters of the group are located elsewhere[50]. Moreover, the parent entity may be in fact just a holding company with no significant operations or workforce. In such cases it will make no sense to see the centre of this specific entity

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[46] See Prototype A (*supra* chapter 1 section 1.6). This is subject though to consideration of situation where national entities had significant independence and other specific circumstances that may suggest a different approach in terms of jurisdiction. These scenarios will be discussed hereafter (see section 7.4 below).

[47] See *supra* chapter 5 section 5.1.

[48] See C. Tugendhat, *The Multinationals* (1971) p. 22, 23.

[49] See Muchlinski, Multinational Enterprises (note 9 *supra* chapter 1), p. 60; Muscat, The Liability (note 44 *supra* chapter 1), p. 56-57.

[50] In the case of *Crisscross* for instance, the actual headquarters of the group were in London at the place of incorporation of one of the group's subsidiaries but not of the parent company (Crisscross Telecommunications Group, Re (unreported, 20 May 2003) (Ch D)). In the case of *BCCI* (note 155 *supra* chapter 4) the parent company was situated in Luxemburg whereas the actual headquarters were apparently in London (see note 55 below and accompanies text).

as having the strongest connection to the entire group[51]. It should be also emphasized that the headquarters we are looking for are not necessarily those located at an ultimate parent company. The first step is to identify the 'integrated and centralized collapsing MCG' and only then locate the COMI of this specific group (that may have on top of it other entities not integrated with it or not under insolvency)[52].

Relevant circumstantial pieces may assist in locating the operational headquarters of the group. This includes, the whereabouts of principal top executives (in the ordinary course of business of the group); whether this management indeed directed the employees and had the authority to direct or coordinate the global business (the various activities of the group companies throughout the world); whether the registered office or another head office is actually the address of principal executive offices or whether it is only a "post box", and whether the majority of the administration functions of the companies were conducted from this place; whether the group represented to creditors a certain venue as the head office of the group; the location where executive meetings were taking place, and where the financial affairs were directed. This is by no means an exhaustive list, but it presents several aspects that can usually hold in the identification of place of central control over an integrated group.

In addition, the other tests for venue mentioned above[53] may reinforce a decision to locate an insolvency process of a group in a particular place. Thus, if the bulk of assets of the various constituent companies of a group (and/or the subsidiaries themselves) are also located where the headquarters are, and/or the parent or other companies were incorporated in that country- these should be relevant factors for a decision on the proper venue, although they will be 'lower level' tests, inferior to the operational headquarters criterion. In case the tests contradict one another the 'operational headquarters' should prevail. Thus, in a case such as *BCCI*[54], where factors point out to different directions (in BCCI the parent company was incorporated in Luxemburg with a 'brass plate' headquarters there, the group's assets were spread

[51] In this regard, the ALI Principles' recommendation that subsidiaries will be allowed to file for insolvency in the parent's home country is insufficient to tackle the 'home country' issue (see *supra* chapter 2 section 2.4.5.3). See also LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 230 compellingly arguing that the ALI recommendation in this regard will enhance forum shopping.
[52] See examples in *supra* chapter 4 section 4.1.3.8.
[53] See section 7.2 above.
[54] Note 155 *supra* chapter 4.

around the world and operational headquarters were based in London) the country of principal proceedings should be that in which the actual headquarters were located[55]. It would not be accurate to assert then that the *BCCI* case demonstrates the impossibility to identify a single 'home country' for a distressed corporate group[56], but rather it shows that there should be a clear and distinct standard for an acceptable centre. In most cases, once adopting a clear criterion a single centre will indeed be revealed[57].

Indeed, it can be seen in recent cases involving MCGs that proceedings of the various entities comprising the group at hand were actually placed in the jurisdiction in which the management and control of the group was situated. In *Crisscross*[58], for instance, the actual headquarters of the group were located in England. The English High Court placed all the companies under insolvency in England based on the finding that each of the separate companies had its COMI there, although subsidiaries were incorporated in different countries [59]. In *Re Parmalat Hungary/Slovakia*[60] the Hungarian court based his decision to open main proceedings against the Slovakian subsidiary of the Hungarian parent company in Hungary mainly on the fact that the financial affairs of the subsidiary were directed from Hungary and the main decisions were taken from there[61]. In the case of *Bramalea*, a United States- Canadian group of companies[62], Canada was the jurisdiction supervising the reorganization. Although the day-to-day operations of U.S. affiliates were carried out and managed locally, large

[55] Indeed, regarding *BCCI*, although the main proceedings against the group took place in Luxembourg, commentators expressed the opinion that England was the actual centre of interests of the transnational group (see I. F. Fletcher, "The European Union Convention on Insolvency Proceedings: An Overview and Comment, with U.S. Interest in Mind" [1997] 23 Brook. J. Int'l L. 25, 37).

[56] An opinion expressed in Lynn M. LoPucki, "Cooperation in International Bankruptcy: A Post-Universalist Approach" [1999] 84 Cornell L. Rev. 696, 713-715.

[57] Except for certain specific scenarios as will be discussed in the next section.

[58] Re Crisscross Telecommunications Group, Re (unreported, 20 May 2003), Ch.D.

[59] On the use of the EU Regulation for centralizing group proceedings see *supra* chapter 4 section 4.1.3.7.

[60] Re Parmalat Hungary/Slovakia, Municipality Court of Fejer, 14 June, 2004.

[61] It also examined whether the designated forum was ascertainable by third parties (see in Re Parmalat Hungary/Slovakia, Municipality Court of Fejer, 14 June, 2004). Proceedings of affiliated companies were also placed at the location of main decision making in other EU Regulation cases, such as Daisytek (Daisytek- ISA Ltd, Re [2003] B.C.C. 562 (Ch D)); Cirio Del Monte (Cirio del Monte (Italian court of Rome, August, 2003) (unreported)); Hettlage-Austraia (Amtsgericht (Munich) (Hettlage-Austria) (Unreported, May 4, 2004) (Germany)); Collins & Aikman corporation group [2005] EWHC 1754 (Ch).

[62] Note 181 *supra* chapter 4.

strategic decisions were likely dealt in Toronto, where the group's head office was located[63].

This experience shows a tendency of courts to place insolvency proceedings of related companies at the state in which they were all ultimately managed. It correlates with the idea of looking for the centre of main administration of a debtor and it provides the opportunity to place all the proceedings of the group's members in one place which reflects a connection to the group as a whole.

On the other hand, the recent ECJ judgment in *Eurofood* implies a different approach. As was already indicated, the ECJ was more concerned at looking at factors relating to the particular subsidiary than at locating a place common for the entire group at the place of main decision making. It seems that at the core of this decision lies an 'entity' approach, thus the interrelations among group members receive little consideration (though, the fact that a parent controlled the decision of the subsidiary could be a contributory factor)[64].

In any case, as was established throughout this work, there are substantial advantages in applying a global approach to these cases, since such a method will enhance the insolvency goals of legal systems[65]. Accordingly, in the cases where unification will be beneficial, searching for a common place for handling or supervising the proceedings is essential[66], which takes us back to the idea of actual headquarters as the meeting point and suitable criterion. Nevertheless, it should be reminded that the approach is not of the 'one size fitting all' type and alternative solutions are needed to answer the demands of the scenario. Thus, for instance, not always should the headquarters' location be the place in which all proceedings of all subsidiaries are to be handled, as will be elaborated in the next section[67].

We have indicated that the test suggested can be ascertainable by stakeholders that dealt with the sort of enterprise that will be the subject of the centralized process. Indeed, the goal of fairness can be achieved using this criterion (particularly meeting

[63] See R. Gordon Marantz, "The Reorganization of a Complex Corporate Entity: The Bramalea Story" in *Case Studies in Recent Canadian Insolvency Reorganizations* 1, 17-18 (Jacob S. Ziegel ed., 1997).
[64] See *supra* chapter 2 section 2.4.3.3.
[65] See *supra* chapters 3-6.
[66] See section 7.1 above.

creditors' expectations regarding the jurisdiction) as it is a rather simple and objective test[68]. It will also render the outcome regarding jurisdiction relatively certain and predictable[69]. First, the place of main decision making is relatively easy to identify. It does not involve the need to quantitatively 'weigh' between amounts of operations or assets in different states (as is the case if adopting a 'place of principal operations' test)[70]. It would be easier hence first for the companies themselves (comprising a group) to recognize this location and indicate it in their business documents[71], since the companies naturally are aware of the location of the group's real headquarters. Parties that dealt with the group in its ordinary course of business are also likely to know the whereabouts of the group's headquarters either because they negotiated with the management or as a general knowledge reasonable to have when dealing with integrated centralized entities[72]. Conversely, creditors or other stakeholders of the corporate group are less likely to know where the various companies comprising it were incorporated or to evaluate where the main activities or assets of the group are located. Finally, when courts are determining the venue issue they can make use of simple evidence related to the organizational structure of the group to identify the place of command and control over the group[73].

An additional merit of the 'head-office criterion' is that it is not formalistic (as is the registered office or incorporation test[74]), but rather based on functional realities of the business. It can disregard strategic planning (incorporating group members in different states to avoid or to purposely subject them to specific jurisdictions) by looking for the place from which the business was actually managed. Hence, it can prevent many of the more overt techniques of forum shopping[75]. However, as was concluded when discussing the issue of forum shopping, any test for the proper venue is susceptible to

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[67] Section 7.4 below. See also *supra* chapter 4 section 4.1.3.8 in which *Eurofood* and the *Prototype* it seems to represent is discussed.

[68] Hence, it will actually fulfil the norm established by the ECJ in *Eurofood* that the COMI should be grounded on factors which are both objective and ascertainable by third parties (Eurofood IFSC Ltd (Case C-341/04) [2006] B.C.C. 397, para. 34).

[69] This was identified as a crucial merit of the designated forum (see section 7.1 above).

[70] See section 7.2 above.

[71] As was suggested earlier this should be a duty cast upon the companies and its auditors, thus ensuring this information is available to creditors ex ante (see *supra* chapter 5 section 5.1.5).

[72] And the requirement to indicate this in business documents (*Id.*) will also assist in ensuring that stakeholders would possess this knowledge.

[73] This too will be facilitated by casting duty upon companies to provide such information in business documents (*Id.*).

[74] See section 7.2 above.

[75] See *supra* chapter 6 section 6.1.3.

manipulations, even if it is based on substantial factors (looking for a strong and true connection to the jurisdiction)[76]. Hence, it was proposed to look for the centre of the group for a substantial amount of time, and to disregard artificial actions being taken with regard to the group centre[77]. Applying this idea to the 'head-office test' will emphasize the idea of actual operating headquarters (the real centre of control) residing for a set amount of time, rather than a façade of headquarters. Finally, our model should also incorporate means of correcting error. That is, it should be possible to transfer the proceedings to another more appropriate forum as new facts and evidence may reveal[78].

In sum, the place from which the group affairs were managed and controlled reflects most suitably the heart and core of the enterprise, its centre and meeting point. Hence, it can be regarded as the place of strongest connection to the group as such. It would also be the easiest to identify (and most importantly to predict) as the future jurisdiction for insolvency proceedings of the integrated group. It would also accord with the true way in which the business has been operated prior to its fall. Therefore, this is an efficacious test that can fulfil the various goals of a global approach[79].

7.4 Limitations to the 'head-office' criterion

As was consistently noted throughout this work, it is ill advised to treat the MCG as a single and unique scenario. Rather, it may take many forms and shapes. Thus, it is necessary for any comprehensive approach that deals with MCGs to be able to ascertain when the tools and tests it incorporates are appropriate (and when they are less so). The 'head-office' criterion is no exception.

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[76] See *supra* chapter 6 section 6.1.4.
[77] In addition, the COMI should be examined taking into account the situation at the time of lodging a request to open insolvency proceeding, disregarding moving of the centre at any time afterwards (Staubitz-Schreiber (Case C-1/04) [2006] (http://curia.eu.int). See further *supra* chapter 6 section 6.1.4.
[78] See *supra* chapter 6 section 6.1.4.
[79] See section 7.1 above.

A.' balance of connections'

There may be a particular scenario in which although the head office of an MCG is in a certain country and it is real and operational, all other connecting factors point out to a single and different place than that of the headquarters. In this situation the nexus to each of the relevant countries may be actually equal, even when looking at the group and its stakeholders as a whole.

In such scenarios, discretion should be given to the relevant courts to either defer to the proximate jurisdiction to which the group has many connections and transfer the process there[80], or decide on a parallel process, conducting insolvency proceedings in both countries (if there is no agreement providing one court with the authority)[81].

To illustrate, if all the subsidiaries of a group are incorporated in France, the bulk of assets is there and all creditors are there, however the operational headquarters is in Germany, then there is a case to look at France as an appropriate venue for the group's insolvency as well, as the German headquarters are in fact 'isolated' (although not a façade) and as all other factors lead to France. It is a scenario very different than the cases where the constituent companies are spread in a number of countries; assets are located in various places and so on. Then, the headquarters, as aforesaid, are the best factor connecting the group to a single venue.

The case of *Maxwell*[82] may demonstrate a scenario of such a 'balance of connecting factors'. There, the group had most of its important subsidiaries located and managed in the U.S. but on the other hand the parent company was incorporated in the U.K. and the U.K. was the financial and governance centre of the entire group[83]. Indeed, from the point of view of the relevant courts, both the American and the U.K. court believed they had an interest in handling the case[84]. Although it can be convincingly argued that

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[80] This would be especially beneficial if in addition most of the creditors are in that second country and it is thus more convenient to handle proceedings there. See also *supra* chapter 6 section 6.1.4 on the transfer of proceedings mechanism.

[81] However linking between the proceedings to gain the advantages of a joined process (see *supra* chapter 4 section 4.1.3.8).

[82] Maxwell Communication Corp., 170 B.R. 800 (Bankr. S.D.N.Y. 1994); Maxwell Communication Corp., [1993] 1 W.L.R. 1402 (Ch. 1993).

[83] *Id.* See also Jacob S. Ziegel, "Corporate Groups and Crossborder Insolvencies: A Canada- United States Perspective" [2002] 7 Fordham J. Corp. & Fin. L. 367, 379.

[84] See Jacob S. Ziegel, "Corporate Groups and Crossborder Insolvencies: A Canada- United States Perspective" [2002] 7 Fordham J. Corp. & Fin. L. 367, 379.

the English court should have been the designated venue[85] there is also a strong case in favour of the U.S. jurisdiction[86]. What happened eventually in the case indeed provides a useful paradigm for the running of a 'parallel' process, in terms of inter-court collaboration[87].

In such instances the idea of direct communication can also assist in preventing jurisdictional 'battles' and jointly agree on the suitable way to administer the case[88].

B. Coordinated groups

In considering the economic efficiency and fairness goals we have pointed to the scenarios in which it would not be advantageous or fair to have all proceedings handled in the same place[89]. Where the enterprise was decentralized to a certain degree (although integrated), with self-standing units of decision-takers, cost efficiency and fairness reasons suggested that it is sensible to have local proceedings against subsidiaries[90]. It has been accordingly proposed that the model should be flexible in that it should enable to have an MCG's insolvency process supervised by a single court (to gain the advantages of a unified process to an integrated enterprise) although separate proceedings are opened in various other countries[91].

It is suggested here that the headquarters criterion can be adapted to these scenarios[92] however it should be given a different role. Looking at the head-office's location now as the centre of coordination (rather than centre of control) the principal insolvency process should be located there. Local insolvency proceedings against local subsidiaries can then be opened in the place of the regional head-office or main management of the particular subsidiary (the subsidiary's separate COMIs). As explained previously, in the 'coordinated groups' the head office coordinates the entire operation (whereas in the centralized MCGs the head-office is the ultimate policy-

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[85] See Jay Lawrence Westbrook, "The Lessons of Maxwell Communication" [1996] 64 Fordham L. Rev. 2531, 2538.
[86] Note 83 above. See also LoPucki, Courting Failure (note 26 *supra* chapter 2), p. 219.
[87] See note 84 above.
[88] See *supra* chapter 6 section 6.1.4.
[89] See *supra* chapter 4 section 4.1.3.8 and *supra* chapter 5 section 5.1.
[90] See *Id.*
[91] See *Id.*
[92] Exemplified by Prototype B- the integrated and coordinated MCGs (supra chapter 1 section 1.6).

maker and directing 'brain')[93]. Hence, though the role of the headquarters is operationally different it still reflects the meeting point of the various companies and the most significant connection the group as a whole has to a particular place. Here as well, the headquarters test (in its specific characteristic as coordinator and supervisor) will accord with the way the business was actually operating and thus will correspond with creditors' expectations regarding the venue[94]. As a result it will achieve the goals of certainty and predictability and assist in preventing forum shopping[95].

In the non-integrated MCGs, where the companies were completely autonomous and the group as a whole was largely decentralized[96] a holding company will typically not control or coordinate the group (or a particular member of the group which operated on a separate autonomous basis). However, in these types of cases global means (such as designating a single venue for a group's insolvency process) will not be necessary and appropriate to begin with[97].

C. Where there is no single centre of control

In certain scenarios that were discussed earlier in this work and are depicted by Prototypes A'[98] and D1-D3[99], a single centre of control for the entire group is missing at the time of insolvency. For instance, if subsidiaries (a bundle of sister companies) are under insolvency; however the parent who controlled the group is truly solvent and not part of the process (or it is an individual shareholder who controlled the group)[100] the centre of command and control may be actually 'outside' the insolvency process. Similarly, in organizational structures where the integrated group is divided between two sub-groups (as demonstrated in Prototype A'[101]) those who control the group chose to operate it via two centres located in two different states. Thus, instead of having one 'head' and 'brain' controlling the entire group (in its ordinary course of

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[93] See *supra* chapter 1 section 1.5.3.
[94] See *supra* chapter 5 section 5.1.5.
[95] Similarly to the centralized groups scenarios (see section 7.3 above).
[96] See Prototype E (*supra* chapter 1 section 1.6).
[97] See *supra* chapter 4 section 4.1.2
[98] The 'twin holding' structure (*supra* chapter 1 section 1.6).
[99] Insolvent subsidiaries and solvent controller within an integrated MCG (*supra* chapter 1 section 1.6).
[100] As in Prototypes D1-D3 in *supra* chapter 1 section 1.6.
[101] Note 98 above.

business), there are in fact two heads for the enterprise[102]. This 'twin holding' structure suggests that there is no single operational headquarters controlling or coordinating the group but rather two. Hence, in these scenarios, the headquarters criterion may not be useful for locating the appropriate venue to handle the insolvency proceedings against the group.

Nevertheless, if such groups were integrated, a unified approach will be beneficial and it will be advantageous to place the related companies' insolvencies in a single place or to have them all coordinated by a supervisory authority. Since it may be impossible to locate a single head office for this purpose, the model should provide 'second best' tests to locate a centre for such MCGs. Here the other tests for venue mentioned above may become of merit. That is, the location of the group's main assets and operations and the place of incorporation of the various subsidiaries[103]. It might be possible to point to one of the affiliate's locations as the place with the major volume of assets and activities and/or a place where most companies are incorporated. However, as these are problematic tests especially when applied to the group case[104], it might be impossible to locate a centre in such cases and the advantages of a unified process will need to be achieved in other manners[105].

7.5 Summary

The question of the 'appropriate venue' is essential to a global model which strives to fulfil insolvency goals by linking between the allegedly disjointed. Thus, it should provide with an appropriate test for ascertaining the locus of control of an MCG from which proceedings should be handled or supervised. Although several such tests were suggested previously in consideration of a single multinational debtor it is increasingly accepted that the idea of Centre of Main Interest is the most appropriate one for the single debtor case. Implementing the concept of COMI to the MCG scenario through the use of the 'head-office' test as the embodiment of COMI we can end up with the best efficacious test for identifying the proper venue. However, we must also realise its limitations and accommodate those specific cases when this test might not be

[102] See note 52 in *supra* chapter 1.
[103] See section 7.2 above.
[104] See *Id.*
[105] See *supra* chapter 4 section 4.1.3.8.

appropriate. Therefore, our global approach must also provide the courts with discretion to rectify any error that might emerge from implementing the head-office test. This could be achieved by enabling courts to defer the proceedings to an alternative place that represents in those unique circumstances a stronger nexus for the group as a whole. It is also realised here that in some specific scenarios the whole idea of a single venue is unattainable and therefore other means need to come into effect.

Conclusions

A set of propositions for the application of a global approach

Major recent insolvency cases have demonstrated a growing need for a global approach to multinational enterprises. Indeed, throughout our discussion it was shown that more often than not a global approach is indeed advantageous over a territorial 'separate' approach in guiding insolvencies within MCGs. Its major strength is its ability to reflect the MCG's economic truth prior to its insolvency. Thus, it holds the potential of successfully complying with general insolvency goals. This includes, inter alia, fitting with parties' expectations and promoting cost-efficiency.

However, a global approach's strength depends on its flexibility and its dynamic adaptation to the facts of the matter. A 'black or white' solution to this kind of cases will undoubtedly result with conflicts and contradicting decisions. Consequently, when undertaking to construct a concrete model along the lines of a global approach one should be very prudent and rely heavily on the accumulative experience. As was apparent throughout the analysis, such a model should be committed to depicting as accurate an image as possible of the MCG at hand while appreciating the negative outcomes its application may bring about. It should seek to impose international rules only when it is absolutely needed while trying at the same time to reduce the harm it may cause to particular parties. Nevertheless, it is evident that a systematic and clear body of guidelines based on a global approach for handling insolvency within an MCG holds the promise of facilitating its course and assisting its positive conclusion.

The main body of this study dealt 'serially' with the different insolvency goals, distinctively appreciating the benefits (or potential downsides) a global approach may have on each one. However, to conclude our endeavour towards a practical global model we need to sum up the results from our analyses across the different goals. This will take the form of guidelines to where and how global tools should be imposed. For this purpose it is suggested to make use of the six propositions summarized as follows which are compiled as the basic constructs that build up a proper global model to insolvencies within multinational corporate groups.

A: Creating a linkage between connected companies

At its core our model needs to provide linking mechanisms between the different constituents of an MCG. Means such as fast recognition, access and relief as well as cooperation and coordination should be readily available for cases of MCGs' insolvencies. It should be explicitly and clearly provided that such tools are applicable among affiliated companies in their insolvencies and can be used by courts and foreign representatives. Creating such a linkage will facilitate the insolvency process and reduce cost. It becomes almost essential where the MCG has the potential to take the path of reorganization[1].

These mechanisms are mainly significant for the integrated collapsing MCGs[2]. Yet, for the non-integrated components[3] a line of cooperation should remain open to enable future cooperation should the need arise[4].

B: Centralizing the process

The advantages in centralizing the proceedings of affiliated companies' insolvencies should be appreciated. That is, having the entire process handled by a single forum under a single law (applying 'procedural consolidation' in an international scenario), or, having the proceedings supervised by a single authority[5]. Yet, this depends on the specific scenario at hand. Accordingly, a model should provide alternative solutions to answer the specific demands of the case, refraining though from resulting with too many options that will defeat predictability[6]. Thus, in cases of integrated and centralized collapsing MCGs[7] the proceedings should be handled from a single location. If the MCG was integrated yet coordinated rather than centralized, with significant autonomy to subsidiaries[8], local proceedings can be opened and supervised altogether by a single forum. Determining on the proper venue should be a relatively quick process with immediate recognition in other relevant jurisdictions, considering the entire group including those entities which are apparently solvent at the time of

[1] See *supra* chapter 4 section 4.1.3.
[2] Prototypes A-D (*supra* chapter 1 section 1.6).
[3] Prototype E (*supra* chapter 1 section 1.6).
[4] See *supra* chapter 4 section 4.1.3.5.
[5] See *supra* chapter 4 section 4.1.3.6.
[6] *See supra chapter 4 section 4.1.3.8 and supra* chapter 6 section 6.2.
[7] Prototype A (*supra* chapter 1 section 1.6).
[8] Prototype B (*supra* chapter 1 section 1.6).

filing insolvency by other related companies[9]. However, it should be possible to challenge in real time the decision regarding jurisdiction and it should be allowed to have modifications in the designated venue, in order to accommodate the dynamics of the process[10].

Another important aspect is that legitimate expectations of local (foreign) creditors of affiliated companies should not be forsaken. Thus, these creditors should be able to participate (or in any case taken into account) and be adequately represented in the joint process. Additionally, courts and representative should be responsible to notify these creditors about court hearings and judgements as well as disclose all relevant information. In cases of breach of due process (with relation to notification of the opening of a central insolvency process) local courts can refuse to recognise the joint (or supervisory) process. Furthermore, a global system should provide rules to ensure the objectivity of the administration supervising the group's process by way of appointing an international firm with an international perspective[11].

C: Ignoring a corporate group's 'artificial' structure

It is justifiable to treat the MCG as a fused entity (pooling together the assets and debts and discarding inter group claims) if those who ran the group, either recklessly or as a planned strategy, did not properly maintain the 'corporate veil' (in the ordinary course of the business). If the components of the group were commingled in such a way that in fact created one unified entity[12], then the insolvency regime should 'follow' this economic truth to promote more efficient results. A reinforcing factor in determining on pooling orders is creditors' beliefs and their reliance on a single unit. Though, this should not be a sufficient or decisive factor and will be given less weight on the balance[13]. In addition, in order to make this mechanism less extreme, several levels of 'pooling' should be provided. It would not be always necessary to pool both assets and debts[14]. A model should also encompass 'compensation' mechanisms for

[9] See *supra* chapter 4 section 4.1.3.9.
[10] See *supra* chapter 6 section 6.1.4.
[11] See *supra* chapter 5 section 5.1.5.
[12] As in Prototype C (*supra* chapter 1 section 1.6).
[13] See *supra* chapter 5 section 5.2.2.
[14] See *supra* chapter 4 section 4.3.6.

the cases where prominent unfairness to a particular creditor (or group of creditors) will result from employing 'pooling'[15].

Applying such a mechanism in the international case will demand creating a close linkage among the affiliates preferably imposing centralization to the maximum compatible extent[16]. Where centralization or supervision by a single court is impossible[17] cooperation and coordination between the foreign proceedings will need to encompass a mechanism facilitating the joint realization of assets and distribution of proceeds.

D: Extending jurisdiction over related companies to deal with manipulations and abuse of the corporate form

One of the merits of a global approach is its capacity in dealing with abuse of control over subsidiaries. Essentially this is achieved through the application of a robust 'manipulation avoidance' rule. Accordingly, courts should be given a discretionary power to evaluate the way control was exercised upon group members, and order that a group member will contribute assets to the insolvent company's estate. For this end, a set of guidelines directing the court to evaluate the conduct of group members and the degree of involvement and responsibility towards the insolvency of a subsidiary[18], combined with more specified factors for identifying categories of corporate group abusive behaviour should be used[19].

Alternatively, it will be possible to use a pooling mechanism to combat such scenarios[20]. In addition, courts should be able to subordinate claims of such entities[21]. To make such judgments meaningful in an international context, the model should also enable to extend jurisdiction over entities held liable when they are located in foreign countries (even if they are not integrated with the company or the group and even if not insolvent)[22]. Furthermore, when other components within a group (or related to the group) were part of the group exploitation, it should be possible to

[15] See *supra* chapter 5 section 5.2.2.
[16] See Propositions A and B above.
[17] See Proposition F below.
[18] As provided in the New Zealand legislation (see *supra* chapter 5 sections 5.2.4.4 and 5.2.4.6),
[19] See *supra* chapter 5 mainly sections 5.2.4.2, 5.2.4.4 and 5.2.4.6.
[20] See Proposition C above, and *supra* chapter 5 section 5.2.4.6.
[21] See *supra* chapter 5 mainly sections 5.2.4.4 and 5.2.4.6.
[22] See *supra* chapter 5 section 5.2.4.7.

"extend jurisdiction" over them as well. This course of action will effectively overcome possible manipulations, such as shuttling of assets and funds from one company to another[23].

E: Balancing between stakeholders' interests

Courts should be equipped with a 'balancing mechanism' to be used in cases of conflicting interests. In this regard, 'inside creditors' and shareholders should prima facie be entitled to less weight than that given to third party creditors in the overall equation[24]. In addition, in determining on issues pertaining to the insolvency of MCG members, the entire group scenario should be considered, and the consequences of judgments regarding a particular subsidiary upon stakeholders of other related companies[25].

F: Identifying the proper venue for the MCG insolvency process

The MCG operational structure and how creditors dealt with it (as a whole) should be examined when determining where is the proper place to handle or supervise the proceedings of an integrated MCG[26]. In principle, the MCG's 'actual' head office will reflect the most predictable, easy to identify, meeting point and connection that the group has to a specific venue[27]. It will be a proper place either for placing in all the proceedings[28], or supervising the process[29].

This test of COMI should be accompanied with rules to avoid manipulation of the COMI on the one hand, and to facilitate its identification on the other hand. Accordingly, fake transfer of actual headquarters should be ignored. Weight should be given to the reason behind the change and the timing of this action[30]. Additionally,

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[23] See *supra* chapter 5 sections 5.2.4.6 and 5.2.4.7.
[24] See *supra* chapter 5 sections 5.1.5, 5.2.2.6 and 5.2.4.6.
[25] See *supra* chapters 4 and 5, passim.
[26] Prototypes A-D (*supra* chapter 1 section 1.6).
[27] See *supra* chapter 7 section 7.3.
[28] For the integrated and centralized collapsing MCGs as in Prototype A (*supra* chapter 1 section 1.6).
[29] For the integrated and coordinated collapsing MCGs as in Prototype B (*supra* chapter 1 section 1.6); See *supra* chapter 7 section 7.4.
[30] See *supra* chapter 6 section 6.1.4.

companies will be responsible to clarify their position in an MCG and the MCG's COMI[31].

In the scenarios where there is 'a balance of connecting factors' or where there is more than one actual head office controlling the same integrated centralized or coordinated groups, alternative tests should be used to locate the centre of gravity. This may include examining where assets, activities or creditors are mainly situated[32]. Alternatively, a parallel process should take place using linking mechanisms as were proposed above[33].

Communication between courts and representatives (of foreign affiliates) should be an available tool for quick resolutions of jurisdictional battles[34].

Reconciling between corporate form and a global approach

A global approach to MCGs' insolvencies entails an inherent conflict with the need to respect the corporate form[35]. However, as was obvious from the discussion on the advantages and characteristics of a global approach, in many cases imposing global means will not have the 'veil lifted' in any significant sense. Often the MCG scenario will only demand a joint administration of a certain sort that will unify the various entities' proceedings to provide for a global handling of the estate. However, this will still respect the distinctiveness between the assets and debts of each component and will secure creditors' distribution rights[36]. Hence, to a substantial degree, a global approach will not interfere significantly with the concept of the separate entity.

Only in the particular cases where the integration between the constituent companies was so strong, so that it is neither efficient nor fair to treat it separately, would a global approach become interventionist in the sense that it would provide for substantive consolidation of the separate estates. Even in this regard, it can be argued that a distinction should be made between substantive consolidation and 'piercing the

[31] See *supra* chapter 5 section 5.1.5.
[32] See *supra* chapter 7 section 7.4.
[33] See Proposition A above.
[34] See *supra* chapter 6 section 6.1.
[35] See *supra* chapter 3 section 3.2.
[36] Some degree of alteration in the right of equal distribution may occur as a result of the application of a particular legal regime on the entire estate (see *supra* chapter 5 section 5.2.1).

veil' jurisprudence[37]. Truthfully, both undermine the legal structures that define the different entities. Nevertheless, substantive consolidation rests solely on functional factors related to implementation of the bankruptcy laws and follows from the economic truth of the specific case. It ignores corporate structures only due to their intermingled nature, and not because a specific fragment is regarded as a 'dummy' for its individual shareholders[38]. Substantive consolidation can therefore be regarded as less harmful and less threatening to the limited liability concept and the idea of preserving the corporate entity compared to a straight-forward 'piercing the veil'. Hence, it does hold the potential of being more appealing to nation states given the reluctance of certain jurisdictions to undermine the limited liability idea[39].

The most direct interference with the corporate personality idea will be in the cases where control over entities was abused and thus fairness consideration will demand for the imposition of group liability. In this regard, it was suggested that global (interventionist) means will be applied only in exceptional cases of specific predefined types of misconduct towards entities (and creditors) within the group. It will demand a close inspection of the circumstances. It should be appreciated though that in the relevant scenarios, it will be indeed advantageous for the long run integrity and efficiency of an international insolvency system that courts (with international jurisdiction) will have the necessary means to give appropriate answers and remedies within the bankruptcy regime. It will supply a necessary strength to the proposition that the privilege of limited liability and companies' access to credit is matched by corresponding responsibilities. A well-designed and effective system of insolvency law will provide a valuable incentive for the maintenance of high standards of corporate governance, including the maintenance of financial discipline in the course of managing the company's affairs[40].

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[37] See Blumberg, Bankruptcy (note 43 *supra* chapter 1), p. 431; J.S. Gilbert, "substantive consolidation in bankruptcy: A Primer" (1990) 43 Val L.R. 205 at p. 218; Walkovsky v. Carlton 18 NY 2d. 414, 418-9 ("It is one thing to assert that a corporation is a fragment of a larger corporate combine which actually conducts the business. It is quite another to claim that the corporate is a 'dummy' for its individual shareholders who are in reality carrying on business in their personal capacities for purely personal rather than corporate ends.").

[38] See Walkovsky v. Carlton (*Id.*).

[39] See *supra* chapter 6 section 6.3.

[40] See also Gordon Johnson, "Towards international standards on insolvency: the catalytic role of the World Bank", Law in transition, spring 2000 (http://www.ebrd.com/country/sector/law/insolve/standard/worldbk.pdf).

Possible 'venues' for the proposed approach

The approach delineated in this study attempted to fill in some gaps in the universalist approach to cross border insolvency, particularly tackling the issue of the MCG, in its variety of appearances. MCGs are by no means a minor phenomenon. Rather, it is the enterprise structure in many of the cases[41]. Thus, we have undertaken, inter alia, to address such issues as the 'home country' in an MCG insolvency case (which was previously designated as one of the shortcomings of a universalist approach[42]) as well as issues of substance pertaining to insolvencies within MCGs[43].

One option for implementing the approach suggested in this work is through the assembly of new tools and mechanisms into a new comprehensive model especially tailored for cases of insolvencies within MCGs. Yet, it seems more practical (and contribute to consistency) to use existing models that are already in use, or are in the process of being accepted by countries, and make the necessary adjustments within them. Perhaps suitable adjustment could be achieved by way of a separate annex, appended to an existing model so that it will still be possible to embrace and enact the model (for instance- the UNCITRAL Model Law[44]) without the annex. Furthermore, if a country already enacted the model law, it could separately consider embracing the additional mechanisms for groups.

What is important to appreciate is that the success of a global model heavily depends on it being embraced by a large number of states. Otherwise, the solutions proposed for dealing with 'the MCG syndrome' will be deemed to break down, and proceedings may 'travel' to those jurisdictions ('insolvency heavens') that have not signed up to such a model. It was argued that the model proposed is feasible in the sense that states should be willing to embrace it[45]. In terms of practicalities, efforts should be directed to linking the approach to those economically significant states. This may then increase the pressure on other jurisdiction to join in, and in general raise the standard applied in MCG insolvency cases.

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[41] See *supra* chapter 1.
[42] Professor LoPucki in his latest article identifies these issues as basic problems that make the universalist approach unworkable (Lynn M. LoPucki, "Universalism Unravels" [2005] 79 Am. Bankr. L. J. 143, 143-144).
[43] See *supra* chapters 4 and 5.
[44] On this model see in *supra* chapter 2 section 2.4.4.
[45] See *supra* chapter 6 section 6.3.4.

In addition, it will be beneficial to consider embracing relevant mechanisms within national regimes for both the cases of domestic and international groups of companies. This will be an important initiative as current global models will in many cases refer to national laws anyway to implement their own laws on the case[46]. Therefore, with no adequate domestic approaches, the model will not be equipped with all the needed tools. However, this in itself can be promoted most effectively via international bodies providing guidelines or recommendations in this area of law for implementation within national laws[47]. As a consequence, uncoordinated unilateral state policies will be reduced. In other words, by proposing suitable policies and workable solutions harmonization of the rules pertaining to corporate groups may improve[48].

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[46] See e.g. the Model Law approach (*supra* chapter 2 section 2.4.4.).
[47] For instance, as part of the UNCITRAL Legislative Guide (note 58 *supra* chapter 2).
[48] The author's views on harmonization of national policies related to corporate groups' insolvencies have been further developed in a separate paper (see I. Mevorach, "Appropriate treatment of corporate groups in insolvency- a universal view" [2006] E.B.O.R., forthcoming).

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