

International Corporate Rescue



Published by:

Chase Cambria Company (Publishing) Ltd

4 Winifred Close

Barnet, Arkley

Hertfordshire EN5 3LR

United Kingdom

www.chasecambria.com

Annual Subscriptions:

Subscription prices 2013 (6 issues)

Print or electronic access:

EUR 695.00 / USD 845.00 / GBP 495.00

VAT will be charged on online subscriptions.

For 'electronic and print' prices or prices for single issues, please contact our sales department at:

+ 44 (0) 207 014 3061 / +44 (0) 7977 003627 or sales@chasecambria.com

International Corporate Rescue is published bimonthly.

ISSN: 1572-4638

© 2013 Chase Cambria Company (Publishing) Ltd

All rights reserved. No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means, mechanical, photocopying, recording or otherwise, without prior permission of the publishers.

Permission to photocopy must be obtained from the copyright owner.

Please apply to: permissions@chasecambria.com

The information and opinions provided on the contents of the journal was prepared by the author/s and not necessarily represent those of the members of the Editorial Board or of Chase Cambria Company (Publishing) Ltd. Any error or omission is exclusively attributable to the author/s. The content provided is for general purposes only and should neither be considered legal, financial and/or economic advice or opinion nor an offer to sell, or a solicitation of an offer to buy the securities or instruments mentioned or described herein. Neither the Editorial Board nor Chase Cambria Company (Publishing) Ltd are responsible for investment decisions made on the basis of any such published information. The Editorial Board and Chase Cambria Company (Publishing) Ltd specifically disclaims any liability as to information contained in the journal.

ERSTE Bank Hungary (Judicial Cooperation in Civil Matters) [2012] EUECJ C-527/10 (5 July 2012)

Alexander Riddiford, Barrister, South Square, London, UK

Background

Article 4(1) of Council Regulation (EC) No 1346/2000 (the 'Insolvency Regulation')¹ provides as a general rule that insolvency proceedings and their effects are governed by the law of the Member State in which they are opened (i.e. the *lex concursus*). Article 5(1) of the Insolvency Regulation² provides one of the exceptions to this general rule, namely that rights in rem³ shall not be subject to the effects of the main proceedings arising under the *lex concursus*. Article 5 has been described as a 'negative conflict' rule,⁴ in that its effect is to prevent rights in rem from being governed by the law of a state other than that in which the res is situated (i.e. a law other than the *lex rei sitae*).

The decision in *ERSTE Bank*

The European Court of Justice (First Chamber), in its recent TFEU Article 267 preliminary ruling in *ERSTE Bank Hungary (Judicial cooperation in civil matters)* [2012] EUECJ C-527/10, decided that Article 5(1) of the Insolvency Regulation is applicable even in circumstances where insolvency proceedings had been opened in a Member State (Austria) prior to the accession to the European Union of another Member State (Hungary) in which the debtor's assets, on which the relevant right in rem was based, were situated. The ECJ's decision was

in contrast to the Opinion of Advocate General Mazák who expressed the view that Article 5(1) was inapplicable in such circumstances since it was a condition of its applicability that an asset of the debtor should be located within the territory of another Member State, i.e. not the territory of a prospective Member State, as at the time of the opening of the insolvency proceedings.⁵

The dispute before the referring national court, the Hungarian court of cassation Legfelsobb Bíróság,⁶ was between ERSTE Bank Hungary Nyrt ('ERSTE Bank') and the Hungarian State.

A letter of credit had been issued in 1998 by Postabank és Takarékpénztár Rt ('Postabank'), a Hungarian bank, in favour of BCL Trading GmbH ('BCL Trading'), an Austrian company. BCL Trading subsequently took shares in Postabank which it held as a security deposit so that, in the event that the letter of credit was drawn upon, Postabank would be required to make payment. Insolvency proceedings were opened in Austria in respect of BCL Trading on 5 December 2003, i.e. prior to the accession of Hungary as a Member State of the European Union on 1 May 2004. Subsequently the Hungarian court ordered the Hungarian state, pursuant to an obligation to which it was subject as a matter of Hungarian law, to purchase the shares held by BCL Trading by way of a security deposit. The Hungarian state duly purchased the shares and paid an amount into the Hungarian court representing the value of those shares.

Notes

- 1 Article 4(1) provides: 'Save as otherwise provided in this Regulation, the law applicable to insolvency proceedings and their effects shall be that of the Member State within the territory of which such proceedings are opened, hereafter referred to as the "State of the opening of proceedings".'
- 2 Article 5(1) provides: 'The opening of insolvency proceedings shall not affect the rights in rem of creditors or third parties in respect of tangible or intangible, moveable or immovable assets – both specific assets and collections of indefinite assets as a whole which change from time to time – belonging to the debtor which are situated within the territory of another Member State at the time of the opening of proceedings.'
- 3 Article 5(2) provides a list of rights which are to be regarded 'in particular' as being 'rights in rem' for the purposes of Article 5(1), e.g. the right to dispose of assets (Article 5(2)(a)), the exclusive right to have a claim met (Article 5(2)(b)), etc. The decision as to whether a given right is a right in rem for the purposes of Article 5(1) is to be made according to the rules of the national law which governs that right prior to the insolvency (typically the *lex rei sitae*): see the Virgós-Schmit Report (1996) para. 100.
- 4 Virgós-Schmit Report (1996) para. 163.
- 5 Opinion of Advocate General Mazák, dated 26 January 2012, paragraph 47.
- 6 Note that Advocate General Mazák, in his Opinion dated 26 January 2012, expressed the view that the ECJ lacked jurisdiction to answer the question referred on the basis that it was a 'hypothetical' question (paragraph 46). The ECJ decided that it did have jurisdiction to answer the question referred, presumably, though its reasons do not appear on the face of the judgment, on the basis of the well-established principle that it is not for the ECJ but for the national court seised of a given dispute to determine the need for a preliminary ruling.

Once the sum had been paid by the Hungarian state into court, representing the value of the security deposit, a dispute arose between ERSTE Bank and the Hungarian state as to their rights with respect to the security deposit (the *res* for the purposes of Article 5(1)).

ERSTE Bank, a Hungarian bank which had become the legal successor of Postabank, brought an action before the Hungarian court seeking a declaration that it had a right in rem in respect of the security deposit and requesting the opening in Hungary of secondary insolvency proceedings against BCL Trading. The Hungarian Fovárosi Ítélotábla (Court of Appeal), upholding the decision of the first instance court, held on the basis of Article 4(1) of the Insolvency Regulation that no claim could be brought against BCL Trading since Austrian law, the *lex concursus* with respect to BCL Trading's insolvency, provided that no action could be brought against a company such as BCL Trading once it was in liquidation. ERSTE Bank appealed the Court of Appeal's decision and argued, consistently with the Opinion of Advocate General Mazák, that the Insolvency Regulation was not applicable in the present case on the basis that the judgment opening insolvency proceedings against BCL Trading in Austria had been handed down prior to Hungary's accession to the European Union.

The question referred by the Hungarian court of cassation to the ECJ was specifically whether Article 5(1) was applicable in the context of civil proceedings concerning the existence of a right in rem in circumstances where the property to which that right referred was situated in a prospective rather than actual Member State. In contrast to Advocate General Mazák's Opinion, which was sparsely reasoned in its view as to the referred question itself (focusing instead on the question of jurisdiction), the ECJ's decision was reasoned with some subtlety. The ECJ's starting point was to interrogate and modify the terms of the question referred by focusing not on the relative timing of (i) the opening of insolvency proceedings and (ii) the accession of the state in which the relevant *res* was situated, but rather on the principle established by Case C-444/07 *MG Probud Gdynia* [2010] ECR I-417 (at paragraph 26), namely that Articles 16(1)⁷ and 17(1)⁸ of the Insolvency Regulation entail that 'the judgment

opening insolvency proceedings in a Member State is to be recognised in all the other Member States from the time that it becomes effective in the State of the opening of proceedings and that it is, with no further formalities, to produce the same effect in any other Member State as under the law of the State of the opening of proceedings' (*ERSTE Bank*, paragraph 33).

According to the ECJ's analysis the relevance of the date of a Member State's accession, when viewed from this perspective, goes only to the question as to when that Member State accrues the obligation⁹ to recognise a judgment opening insolvency proceedings handed down by a court of another Member State which has jurisdiction under Article 3 of the Insolvency Regulation (*ERSTE Bank*, paragraph 36). Hungary accrued this obligation on 1 May 2004 and it was from that date onwards that it was obliged to recognise the decision to open insolvency proceedings handed down by the Austrian court, regardless of the date on which that decision might have been handed down by the Austrian court (*ERSTE*, paragraph 44). Further, the court suggested that the only temporal limit to the applicability of the Insolvency Regulation was Article 43,¹⁰ the effect of which is that 'the Regulation applies only to insolvency proceedings opened after its entry into force which, as stated in Article 47 thereof, is fixed for 31 May 2002' (*ERSTE*, paragraph 30). Given that insolvency proceedings were opened in Austria on 5 December 2003, there was 'no doubt that those proceedings were opened in a Member State after 31 May 2002 and that, therefore, they fall within the scope of the Regulation' (*ERSTE*, paragraph 32).

Moreover, since Article 5 is inseparable from the Article 4 general rule to which it is an exception, it follows that the rights and obligations arising under Article 5 are also accrued by the acceding Member State on the date of its accession, and again apply regardless of the date on which the judgment opening insolvency proceedings was handed down. In this way the ECJ's reasoning leads neatly to the conclusion that Article 5(1) must be interpreted 'as meaning that that provision is applicable even to insolvency proceedings opened before the accession of the Republic of Hungary to the European Union in a case ... when, on

Notes

- 7 Article 16(1) of the Insolvency Regulation provides: 'Any judgment opening insolvency proceedings handed down by a court of a Member State which has jurisdiction pursuant to Article 3 shall be recognised in all the other Member States from the time that it becomes effective in the State of the opening of proceedings'.
- 8 Article 17(1) of the Insolvency Regulation provides: 'The judgment opening the proceedings referred to in Article 3(1) shall, with no further formalities, produce the same effects in any other Member State as under this law of the State of the opening of proceedings, unless this Regulation provides otherwise and as long as no proceedings referred to in Article 3(2) are opened in that other Member State'.
- 9 The obligation to recognise judgments opening insolvency proceedings in other Member States is reinforced by the principle of 'mutual trust' encapsulated in Article 16(1) and recital 22 in the preamble of the Insolvency Regulation: *ERSTE*, paragraph 34. See further Case C-341/04 *Eurofood IFSC* [2006] ECR I-3813, (paragraphs 39 and 40) and Case C-444/07 *MG Probud Gdynia* [2010] ECR I-417 (paragraphs 27 and 28).
- 10 Article 43 of the Insolvency Regulation provides: 'The provisions of this Regulation shall apply only to insolvency proceedings opened after its entry into force. Acts done by a debtor before the entry into force of this Regulation shall continue to be governed by the law which was applicable to them at the time they were done.'

1 May 2004, the debtor's assets on which the right in rem concerned was based were situated in that State' (*ERSTE*, paragraph 45).

Assessment and impact of the decision in *ERSTE Bank*

The ECJ's decision in *ERSTE Bank* is plainly correct and its impact is to clarify an issue which was by no means obvious. The decision is consistent with the purposive interpretation of Articles 16(1) and 17(1) advanced in Case C-341/04 *Eurofood IFSC* [2006] ECR I-3813 and Case C-444/07 *MG Probud Gdynia* [2010] ECR

I-417 (see fn. 9 above). Once it is established that the Insolvency Regulation applies at all, there could be no principled basis for holding that Article 4 applied but that Article 5 did not. In this way, whilst the Opinion of Advocate General Mazák may seem intuitively correct in that the asset (the res) in question was plainly not located in another Member State (but only a prospective Member State) as at the time of the handing down of the judgment of the Austrian court opening the insolvency proceedings, nonetheless the decision of the ECJ is the only possible answer to the question referred which would accord both with the principles established in the ECJ case law and with a purposive interpretation of the Insolvency Regulation.

International Corporate Rescue

International Corporate Rescue addresses the most relevant issues in the topical area of insolvency and corporate rescue law and practice. The journal encompasses within its scope banking and financial services, company and insolvency law from an international perspective. It is broad enough to cover industry perspectives, yet specialized enough to provide in-depth analysis to practitioners facing these issues on a day-to-day basis. The coverage and analysis published in the journal is truly international and reaches the key jurisdictions where there is corporate rescue activity within core regions of North and South America, UK, Europe Austral Asia and Asia.

Alongside its regular features – Editorial, The US Corner, Economists’ Outlook and Case Review section – each issue of *International Corporate Rescue* brings superbly authoritative articles on the most pertinent international business issues written by the leading experts in the field.

International Corporate Rescue has been relied on by practitioners and lawyers throughout the world and is designed to help:

- Better understanding of the practical implications of insolvency and business failure – and the risk of operating in certain markets.
- Keeping the reader up to date with relevant developments in international business and trade, legislation, regulation and litigation.
- Identify and assess potential problems and avoid costly mistakes.

Editor-in-Chief: Mark Fennessy, Proskauer Rose LLP, London

Emanuella Agostinelli, Curtis, Mallet-Prevost, Colt & Mosle LLP, Milan; Scott Atkins, Henry Davies York, Sydney; Samantha Bewick, KPMG, London; Geoff Carton-Kelly, Baker Tilly, London; Sandie Corbett, Walkers, British Virgin Islands; Ronald DeKoven, South Square, London; Simon Davies, Cairn Capital, London; Hon. Robert D. Drain, United States Bankruptcy Court, Southern District of New York; Stephen Harris, Ernst & Young, London; Christopher Jarvinen, Berger Singerman, Miami; Matthew Kersey, Russell McVeagh, Auckland; Ben Larkin, Berwin Leighton Paisner, London; Guy Locke, Walkers, Cayman Islands; Professor John Lowry, UCL, London; Dr Carlos Mack, White & Case, Munich; Lee Manning, Deloitte, London; David Marks Q.C., South Square, London; Ian McDonald, Mayer Brown International LLP, London; Riz Mokal, South Square, London; Lyndon Norley, Jefferies Bank, London; Karen O’Flynn, Clayton Utz, Sydney; Rodrigo Olivares-Caminal, Centre for Financial and Management Studies (SOAS), University of London; Christian Pilkington, White & Case LLP, London; Susan Prevezer Q.C., Quinn Emanuel Urquhart Oliver & Hedges LLP, London; Sandy Purcell, Houlihan Lokey Howard & Zukin, London; Professor Philip Rawlings, Queen Mary, University of London; Dr Arad Reisberg, UCL, London; Peter Saville, Zolfo Cooper, London; Daniel Schwarzmann, PricewaterhouseCoopers, London; Richard Snowden Q.C., Erskine Chambers, London; Anker Sørensen, Reed Smith, Paris; Kathleen Stephansen, AIG Asset Management, New York; Dr Shinjiro Takagi, Nomura, Tokyo; Lloyd Tamlyn, South Square, London; Stephen Taylor, Alix Partners, London; Richard Tett, Freshfields, London; William Trower Q.C., South Square, London; Professor Edward Tyler, Department of Justice, Hong Kong Special Administrative Region Government, Hong Kong; Mahesh Uttamchandani, The World Bank, Washington, DC; Robert van Galen, NautaDutilh, Amsterdam; Miguel Virgós, Uría & Menéndez, Madrid; Dr Haizheng Zhang, Beijing Foreign Studies University, Beijing.

For more information about *International Corporate Rescue*, please visit www.chasecambria.com