Improving Restructuring of Corporate Groups in Europe: Report on the ELI and BLRN conferences in December 2018

Boon, J.M.G.J.; Kokorin, I.; Pool, J.M.W.

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Mr. drs. J.M.G.J. Boon, I. Kokorin LL.M. (adv) & J.M.W. Pool LL.M BSc[1]

Improving Restructuring of Corporate Groups in Europe

Report on the ELI and BLRN conferences in December 2018

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1. Introduction

Complexities of corporate groups play a role in nearly every restructuring or insolvency case. However, legislators pay only limited attention to the group context. This may be surprising, as the phenomenon of corporate groups is nothing new. The current state of law results in cases where a strong economic unity (enterprise) is legally considered only as a conglomerate of separate entities. Once insolvent, such entities are treated separately in the course of insolvency proceedings.

The issue of restructuring in corporate groups was discussed at two conferences that took place on 5 and 11 December 2018. The first one was jointly organised in Leiden (The Netherlands) by the European Law Institute (ELI)[2] and the Business & Liability Research Network (BLRN)[3]. During this conference developments at both the national and European level were extensively discussed. The second conference of ELI took place in Vienna and focussed on the topic of substantive consolidation in insolvency. The starting point for both discussions were the recommendations of the ELI Instrument on Rescue of Business in Insolvency Law (ELI Business Rescue Instrument).

This article provides an overview of the discussions that took place during these conferences. We will consecutively discuss the ELI Business Rescue Project (§2), and more specifically its recommendations on corporate groups (§3). Then, we will elaborate on certain aspects of directors' duties in corporate groups (§4), and options for dealing effectively with the insolvency of corporate groups (§5). This is followed by the Belgian approach to restructuring of corporate groups (§6). Subsequently, we will report on the issue of substantive consolidation (§7), which is followed by a conclusion (§8).

2. The ELI Business Rescue Project

At the conference in Leiden, Prof. Em. Bob Wessels (Leiden University, The Netherlands) introduced the background, scope and results of the ELI Business Rescue Project. He elaborated that the European Commission has aimed, among other things, to harmonise insolvency laws and provide viable businesses in financial difficulties an opportunity for early restructuring. With these developments in mind, the Business Rescue Project was initiated by ELI in 2013, directed at designing a set of norms and requirements that should enable further development of coherent and functional rules for restructuring of distressed businesses in Europe. Reporters for the project were Bob Wessels and Prof. Stephan Madaus (Martin Luther University, Germany).[4] Based primarily on detailed national and international inventory reports, the ELI Business Rescue Instrument was drafted.[5] It comprises 115 recommendations on a legal framework enabling the development of coherent and functional rules for business rescue in Europe.

3. Recommendations on restructuring of corporate groups in Europe

Madaus elaborated on the recommendations made in the ELI Business Rescue Instrument on the issue of corporate groups. Insolvency of (parts of) a corporate group may further complicate things, as many jurisdictions apply a strict individualistic treatment of the insolvent group members (entity-by-entity approach). The structure of the group gets lost when insolvency proceedings are commenced, since in many cases the approach is directed at only one insolvent debtor, involving one estate, one insolvency proceeding, one court and one insolvency practitioner (IP). When there is no coordination between different insolvency proceedings of companies belonging to the same group, there may be a loss of group synergies.

1 Please quote this article as: J.M.G.J. Boon, I. Kokorin & J.M.W. Pool, 'Improving Restructuring of Corporate Groups in Europe', TvI 2019/. Gert-Jan, Ilya and Jessie are researchers at the Leiden University. Gert-Jan was also a member of the Project Team for the ELI Business Rescue Project. The authors can be contacted at: j.m.g.j.boon@law.leidenuniv.nl, i.kokorin@law.leidenuniv.nl, and j.m.w.pool@law.leidenuniv.nl.

2 The ELI is founded in June 2011 as an entirely independent organisation. The ELI aims to improve the quality of European law, understood in the broadest sense. It seeks to initiate, conduct and facilitate research, to make recommendations, and to provide practical guidance in the field of European legal development. For more information, see: www.europeanlawinstitute.eu.

3 BLRN is a multidisciplinary research and expertise network that focuses on a variety of aspects of doing business within the context of company and insolvency law. It is a collaboration of the departments of Company Law and Business Studies of the Leiden University. Good corporate governance, future business structures and distress & insolvency are the key areas of attention. For more information, see: www.universiteitleiden.nl/en/law/business-liability-research-network.

4 For an introduction on the ELI Business Rescue Project, see also: Gert-Jan Boon, Jan Adriaanse & Margot Branger, 'Business Rescue', *TvI* 2018/21. See also: https://europeanlawinstitute.eu/projects-publications/completed-projects/insolvency/.

5 Bob Wessels & Stephan Madaus, Rescue of Business in Insolvency Law – an Instrument of the European Law Institute (September 6, 2017). Available at SSRN: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3032309.

To deal with corporate groups, different approaches have been developed, both in theory and in practice. They provide for different levels of coordination and consolidation but aim to improve the outcomes for corporate groups. Madaus distinguished between six different approaches, characterised by the increasing degree of coordination/consolidation:

1. Coordination: coordination between the involved courts and IPs;
2. Coordination + coordination proceedings: this includes (i) coordination between the involved courts and IP, and (ii) the introduction of a proceeding aimed at facilitating the needed coordination, possibly by appointing a group coordinator;
3. Procedural consolidation 1: appointment of the same IP in all insolvency proceedings;
4. Procedural consolidation 2: this includes (i) appointment of the same IP in all insolvency proceedings and (ii) appointment of the same judge(s) in those proceedings (this may require the implementation of the concept of Enterprise COMI);
5. Procedural consolidation 3: this provides for one restructuring plan for all members of the corporate group; and
6. Substantial consolidation: this provides for a common estate for all insolvent members of the corporate group.

The results of the Business Rescue Project show converging approaches across Europe. Many times, there are no specific rules for dealing with corporate groups, although in practice pragmatic approaches have been pursued. Some countries allow for some levels of coordination and procedural consolidation. Substantive consolidation is allowed in exceptional cases of irreversibly intermingled assets and/or fraud.

The ELI Business Rescue Instrument contains 12 recommendations on corporate groups. In brief, it is recommended for national legislators to create a legal framework for dealing with insolvent corporate groups (Recommendation 9.01). Courts are advised to consider whether a coordinated strategy is possible, before opening insolvency proceedings with regard to a member of a corporate group (Recommendation 9.02). The EU and national legislators should ensure that courts and IPs are guided by principles and guidelines on cooperation and communication, including the CoCo Guidelines (2007),[6] and the EU JudgeCo Principles and Guidelines (Recommendation 9.03).[7] This should also apply when an international insolvency case falls outside the scope of the EIR 2015 (Recommendation 9.04). Coordination proceedings should be made more efficient, for instance, Member States should enable joint opening of insolvency proceedings when the centres of main interests (COMIs) of the members of the group are located in their jurisdiction (Recommendations 9.05 and 9.06), and consider the role of the IP in group insolvency proceedings (Recommendation 9.07).

In addition, whereas participation in group coordination proceedings is voluntary, an explicit decision should be required for group members that wish to opt-out (Recommendation 9.08). Furthermore, solvent group members must be allowed to join group coordination proceedings without subjecting themselves to a court or the insolvency proceedings (Recommendation 9.09). In addition, the group restructuring plan should be binding for its participating members (Recommendation 9.10). For domestic corporate groups, the EU and national legislators should promote the appointment of the same IP in the insolvency proceedings of different group members (Recommendation 9.11). Also, substantive consolidation should be available, but limited to a single jurisdiction and for cases of intermingled assets or fraud only (Recommendation 9.12).

4. Director's duties in corporate groups

The role of directors' duties in the context of (insolvent) corporate groups was discussed by Prof. Reinout Vriesendorp (Leiden University, The Netherlands). In the Netherlands, as in various other jurisdictions, the interests to be considered by directors of a group member differ depending on the position of that member within the group. At the group level (TopCo), the parent's interests must be considered as being equal to the interests of the entire group. This involves the interests of the group as a whole. However, for operational companies (OpCo), directors must consider the specific interest of the respective OpCo.

The relevant duties also depend largely on the extent to which the activities and processes of a group are integrated. When there is a high degree of integration, e.g. for highly integrated companies as was the case with Lehmann Brothers or Parmalat, the OpCo's cannot act independently. This is different when OpCo's are loosely related, act independently within the group and are not dependent on other group members for their individual viability.

The EU proposal for Preventive Restructuring Directive (Proposal)[8] states that directors, when insolvency is looming, should take appropriate action. The scope of provisions of the Proposal on this matter has varied in subsequent versions, in particular, regarding Article 18 and Recital 36 of

6 European Communication and Cooperation Guidelines for Cross-border Insolvency, 2007.

7 EU Cross-Border Insolvency Court-to-Court Cooperation Principles of 2015, which include also the EU JudgeCo Guidelines, 2015.

8 At the time of the conference the most recent version of the Proposal was: Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30 – General approach of 1 October 2018, 12536/18, available at: https://data.consilium.europa.eu/doc/document/ST-12536-2018-INIT/en/pdf.

the Proposal.[9] In discussions on these parts of the Proposal, it has been argued that the complexity of directors' duties may lead to extensive legal proceedings.

Potential conflicts of interests of directors may come in play when directors of OpCo's or a HoldCo must also take into account the group's interests. For instance, when entering into contracts without clear outcomes, when making payments or contributions to the parent or other group entities that deplete the company's assets, when collecting intercompany claims, or where the parent also acts as board of a subsidiary. Interdependency may guide directors in their focus on individual or corporate benefit. To this end, Vriesendorp presents several points of reference for the director: Is there commingling of assets and/or administration? Based on an 'independent viability test', can the group member survive without the group or the parent? Other points of reference can be whether there has been voluntary consolidation by providing an under Dutch law so-called '403 Declaration'?[10] Has the company attracted contractual, non-delictual liability? Finally, depending on the type of company creditors have been contracting with, what is the reasonable expectation of creditors?

5. Reviewing options for dealing with corporate groups

Evaluating the existing legal mechanisms to facilitate efficient resolution of corporate groups in distress

Jessie Pool (researcher at Leiden University) discussed the difficulties of dealing with corporate groups. She considered that the most probable solution under the EIR 2015, cooperation and communication, face significant limitations. First, the EIR 2015 provides for the obligation of actors (IPs and courts) involved in insolvency proceedings of corporate groups to cooperate and communicate. Notwithstanding the obvious advantages of this duty, several difficulties have been identified. The duty, for instance, only applies when cooperation and communication are appropriate to facilitate the effective administration of these proceedings, are compatible with the rules applicable to such proceedings (*lex concursus*), and when it does not entail any conflict of interests. Pool argues that, although the duty to cooperate and communicate is a valuable mechanism, it may not have the desired effect. This is due to exceptions offered by the EIR 2015 that allows courts and insolvency practitioners to deviate from this duty. Second, despite the promising tools offered by the provisions on coordination, group coordination proceedings are strictly voluntary. Third, Pool observes that both the EIR 2015 promotes procedural cooperation and coordination, instead of cross-border procedural or substantive consolidation, which in some cases may be a more effective and efficient approach for corporate groups.

Pool subsequently discussed several solutions that have been offered in literature. Courts may consider appointment of the same IP in the insolvency proceedings of all insolvent members of a corporate group.[11] However, this approach overlooks the potential conflict of interests between members of the corporate group and between their creditors. This conflict of interests may preclude the appointment of the same insolvency practitioner in the proceedings of all corporate groups. Also, several practical difficulties may arise (for instance regarding different languages and cultures). Furthermore, to be appointed as an insolvency practitioner, Member States must recognise the qualifications of the insolvency practitioner in another jurisdiction.

Another solution may be the use of an Enterprise COMI (E-COMI). Under this approach, the COMI of a subsidiary may be identical with the COMI of the parent company, thus enabling one court to open insolvency proceedings of all members of the corporate group. E-COMI is a type of procedural consolidation that allows for the administration of different insolvency procedures in a single forum. It allows for better coordination and avoids at least some transaction costs. Notwithstanding the advantages of the E-COMI approach, following the judgement in Eurofood, the COMI of a subsidiary is not at its own registered office only if the factors showing that the subsidiary's COMI is located at the registered office of the parent company are objective and ascertainable by third parties. Pool argues that the judgement in Eurofood impedes the practical usability and impact of the E-COMI approach.

Reinventing synthetic proceedings in corporate group insolvencies

Ilya Kokorin (researcher at Leiden University) addressed the issue of 'synthetic' insolvency proceedings under the EIR 2015. Having stressed the somewhat limited scope of new provisions on group coordination proceedings, Kokorin highlighted the existence of another potentially powerful, but largely underused tool of the EIR Recast, namely synthetic or 'as if' proceedings. Originating from judicial innovativeness, such proceedings have now been entrenched in Article 36 EIR 2015. This article introduces a legal regime for the avoidance of secondary insolvency proceedings, based

9 This has been revised in the agreement on the Proposal that was reached by the Council and the European Parliament on 17 December 2018. A revised Article 18 was included again, which reads as follows: "Member States shall ensure that, where there is a likelihood of insolvency, directors, as a minimum, have due regard to the following:
(b) the interests of creditors, other stakeholders and equity holders;
(c) the need to take steps to avoid insolvency; and
(d) the need to avoid deliberate or grossly negligent conduct that threatens the viability of the business."
See: Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30 - Confirmation of the final compromise text with a view to agreement of 17 December 2018, 15556/18, available at: https://data.consilium.europa.eu/doc/document/ST-15556-2018-INIT/en/pdf.

10 See Article 2:403 Dutch Civil Code.

11 Advocates of this solution are C.G. Paulus, Überlegungen zu einem modernen Konzerninsolvenzrecht, *ZAP* 44/2005, p. 1948-1955 and N.W.A. Tollenaar, 'Dealing with the insolvency of multinational groups under the European Insolvency Regulation', TvI 2010/14, (p. 94).

on the unilateral promise (undertaking) given by the main IP to local creditors, guaranteeing that the latter will receive treatment 'as if' the secondary proceedings have actually been opened.

Despite obvious advantages (coordination of restructuring efforts and decrease in transaction costs), 'traditional' synthetic proceedings remain ill equipped for insolvencies of corporate groups. After all, in order to reap the benefits of such proceedings in a group context, the COMIs of all group members have to be in the same jurisdiction. Thus, unless a miracle happens, the use of synthetic proceedings will not bring centralisation of insolvency proceedings opened against group members. The question arises whether the logic behind synthetic proceedings can be adapted to avoid multiplication of insolvency proceedings and to pull insolvency proceedings of group members in one jurisdiction. Kokorin gives an affirmative answer on this question, inspired by the recent judgment in *In the Matter of Videology Ltd* [2018] EWHC 2186 and the UNCITRAL's draft Model Law on Enterprise Group Insolvency. He suggests using the companies' establishments as a linking jurisdictional factor, instead of a more rigid concept of COMI. In contrast with 'traditional' synthetic proceedings, in the offered scenario, it is the main insolvency proceedings that may be avoided to facilitate the desired jurisdictional concentration. As a result, insolvency proceedings of group members can be initiated in a single jurisdiction (COMI- and establishment-linked), while additional proceedings in other jurisdictions are avoided. Despite clear attractiveness of this solution, Kokorin considers it to be unavailable under current rules of the EIR 2015, which provide only for the exclusion of secondary proceedings (see Article 36 EIR 2015).

Using insolvency protocols in the context of corporate groups

Gert-Jan Boon (researcher at Leiden University) discussed the potential and practice of using insolvency protocols to improve coordination and cooperation in international insolvencies of members of corporate groups. Compared to other options, insolvency protocols are included as an option in the EIR 2015, both for individual insolvent debtors as well as for corporate groups. However, Boon argues that the EIR 2015 leaves much room for interpretation, which may limit their effectiveness in practice.

In general, protocols are used between insolvency practitioners (and courts) to lay down specific agreements on cooperation and coordination. Insolvency protocols have received attention by various international standard-setting organisations that developed soft law instruments. They highlight that at a minimum, protocols should provide for coordinated court approvals and communication with creditors resulting in timesaving and – also for corporate groups – contribute to maximising the value of the estate(s). Protocols do not make clear what their legal status is, more specifically: Are they binding, or do they create (at least) a moral duty? What is the applicable law? What is the role of courts and creditors regarding a protocol? Although providing for them, the EIR 2015 in Recital 49 and Articles 56 and 57 generally describes protocols as an option too, that can be written or oral, may be varying in scope and lacks a minimum standard. Also, it is unclear how often they are used in practice as they are usually not published.

Boon suggests that protocols have potential but would benefit from further research. Existing soft law instruments, including from UNCITRAL, provide a valuable point of reference. To promote broader use of protocols, consideration may be given to a modular approach offering different models depending, for instance, on the size or sector of the corporate group. This may limit the time and costs for negotiating the protocol, but also function as a helpful point of reference and possibly benchmark for judges.

6. Restructuring Corporate Groups in Belgian Insolvency Law

Prof. Joeri Vananroye (Katholieke Universiteit Leuven, Belgium) introduced the Belgian framework for dealing with insolvent corporate groups.[12] The Belgian law contains only a few provisions that address (the insolvency of members of) corporate groups. In principle, the law treats companies on an entity-by-entity basis. The rules on limited liability of individual legal entities apply to the individual members of a group, with only some exceptions, such as with liability of shareholders in case of single shareholder companies. For instance, a shareholder may risk liability when acting as *de facto* director and for manifestly serious wrongdoings that contributed to the insolvency of the company. A shareholder, in his capacity, does not have specific duties of care and there is no higher threshold than is the case for other parties.

For many years, the issue of corporate groups was practically ignored in Belgium. However, the Belgian legislator implemented the provisions on corporate groups of the EIR 2015 in Book XX of the Belgian Code on Economic Law. These provisions have been extended to include non-EU companies. For domestic groups, Belgian law provides that the COMI of the parent can also be the COMI of all its insolvent group members. This also allows for the appointment of the same IP for each insolvent member of the corporate group. This procedural consolidation has been made possible for domestic groups as of 1 May 2018.[13]

Furthermore, group structures may be used for (strategic) asset partitioning. When this is pursued in the vicinity of insolvency, it may be declared voidable with an *actio pauli-*

12 The presentation is also available here: https://limo.libis.be/primo-explore/fulldisplay?docid=LIRIAS2342833&context=L&vid=Lirias&search_scope=Lirias&tab=default_tab&lang=en_US.

13 Art. XX.13 Belgian Code on Economic Law, it reads (translated in English): Art. XX. 13. The court with jurisdiction over an insolvency proceeding concerning an undertaking has jurisdiction over insolvency proceedings concerning an undertaking affiliated with this undertaking. It can assign a common insolvency practitioner for all proceedings.

ana. Creditors or the insolvency practitioner can also invoke the *actio pauliana* outside the zone of insolvency, when faced with the transfer of value that could not be taken in the interest of the company. For those two cases, it is required that the creditor is harmed due to the contested transaction. A remaining option is a special feature under Belgian law, the so-called *auto-cession*. When a company enters judicial reorganisation proceedings, the aim is to sell (a part of) the business to a new company. Many times the bid is made by insiders (for instance, shareholders or directors), which is called an auto-cession. These insider sales are allowed under certain conditions. Article XX.87 §2 of the Code on Economic Law provides in those cases:

> 'the offer can only be taken into account if such rights are made accessible to other bidders under the same terms and conditions.'

This rule aims to create a level playing field for all interested parties in a judicial reorganisation.

The (new) rules in Belgium provide for more opportunities to restructure distressed corporate groups by providing for better opportunities to facilitate preservation of the going-concern value. In a strongly integrated and inter-woven group, this going-concern value may be perceived as a joint asset of the group as a whole. Currently, this going-concern value is invoked to justify a transfer of value. Joeri suggests that we might consider applying this also more generally as an asset of the corporate group, for which the directors have a duty to safeguard this common going concern value, also in case of insolvency.

7. Consolidated treatment of insolvent corporate groups

A week later, on the occasion of the 54th session of the UNCITRAL Working Group V meeting in Vienna, ELI organised a discussion on using substantive consolidation to deal with insolvent corporate groups. Madaus chaired the session, and emphasised the need for having separate corporate entities, for instance, to allow businesses to shift their risks. Still, businesses must abide and respect the *pari passu* principle in insolvency. Central question during the discussion was whether there would also be room for substantive and/or procedural consolidation.

The European Union Perspective

Florian Bruder (DLA Piper, Germany) elaborated that under the EIR 2015 there is no room for substantive consolidation. It has been a deliberate choice to exclude this in Chapter 5 of the EIR 2015 dealing with corporate groups. In practice, the solution is to pursue maximum cooperation and communication, up to the extent it is not incompatible with (local) procedural rules. In particular, insolvency protocols may be used, also – as is possible in Germany – to grant the insolvency practitioner with extra powers.

The group coordination procedure in the EIR 2015 contains procedural rules on coordination of insolvency proceedings of members of a corporate group. Group coordination proceedings are flexible in the sense that it is possible to opt-out from and (subsequently) opt-in such proceeding. Also, the resulting group coordination plan is not binding. Further consolidation is prohibited under Article 71 of the EIR 2015. In practice, the debtor will try to prevent insolvency proceedings, or, when that is not possible, aim for a single point of entry by focusing on the HoldCo insolvency proceeding. A next step would be to resolve matters that deal with third party security.

If this would not work out and multiple proceedings would be opened, the aim would be, first, to concentrate the COMI of the involved group members. However, under the EIR 2015 it has become increasingly time consuming and uncertain to concentrate the COMIs. German law helps the insolvency practitioner by stating that when one member of a corporate group has filed for the commencement of insolvency proceedings at one court, other group members with their COMI in Germany may, under certain conditions, apply for insolvency proceedings with that same court. Where there would (still) be multiple judges and/or insolvency practitioners involved, it is important to pursue cooperation and communication.

Another option is to proceed with synthetic secondary proceedings, however, the EIR 2015 allows this only for secondary proceedings, not for corporate groups. In addition, debtor in possession proceedings may be considered as a way to promote treatment of enterprise group members.

UNCITRAL Legislative Guide, Part three: treatment of enterprise groups

Prof. Irit Mevorach (University of Nottingham, UK) spoke on the role of consolidation as promoted by UNCITRAL in its third part of the Legislative Guide on Insolvency Law (2010).

The UNCITRAL Legislative Guide Part Three promotes the use of substantive consolidation, but, according to Mevorach, this should not be seen as a one-size-fits-all tool. The Legislative Guide considers several types of proceedings and tools to deal with corporate groups, including: (i) joint application, (ii) procedural coordination, (iii) post-commencement finance, (iv) avoidable transactions, (v) substantive consolidation, (vi) appointment of the same insolvency representative, (vii) coordination of reorganisation plans, and (viii) international aspects. Substantive consolidation is defined as:

> 'the treatment of the assets and liabilities of two or more enterprise group members as if they were part of a single insolvency estate'.[14]

14 UNCITRAL Legislative Guide, Part three: treatment of enterprise groups, Glossary, at 4(e).

Recommendation 219 of the UNCITRAL Legislative Guide emphasises the principles of separate legal entity. Recommendation 220 makes an exemption on this, to apply substantive consolidation, in case of intermingled assets or fraud. This is further discussed in Recommendations 221-231, which make it clear that substantive consolidation is not a one size fits all, and may be applied partially to an insolvent corporate group.

Mevorach argues that UNCITRAL has found the right balance between the principles of company law and insolvency law. In the extreme, under company law a separate entity approach would apply, meaning members of the corporate group would always be treated on an entity-by-entity basis. It recognises the corporate personality and limited liability of the entities. It also provides room for asset partitioning. Under insolvency law, the enterprise approach would prevail. It focuses on maximising asset value, equitable treatment of creditors and timely resolution of insolvency. This allows better chances of addressing problems of fraud. When the corporate group is centrally controlled and organised, we must give more consideration to the group as a whole. Substantive consolidation can fulfil the goal of insolvency with respect to asset partitioning and intermingling of assets. According to Mevorach, the corporate form was – as one could also say – already ignored before the group went insolvent. Furthermore, with fraud it should always be possible to opt for substantive consolidation.

The US perspective on substantive consolidation

Prof. Edward Janger (Brooklyn Law School, USA) mentioned a paper of Bill Widen in which he pointed out that substantive consolidation is quite common for corporate groups in the US.[15] However, the US follows the UNCITRAL Legislative Guide Part Three. According to the Legislative Guide, the US insolvency laws respect the corporate form, an exception is made only in Recommendations 219 and 220.

Substantive consolidation: the practical approach

From this point of view, the observation of Bill Widen raises questions, like: When does substantive consolidation happen? Does substantive consolidation imply *pari passu* treatment of creditors? Are pre-insolvency priorities reconstituted under a restructuring plan when substantive consolidation is applied? Janger mentions that substantive consolidation takes place mostly in the context of consensual (restructuring) plans. In practice, it is not often formally approved, but performed when there are no objections to it. Therefore, it is not applied until there is a restructuring plan. In the restructuring plan, parties agree on substantial consolidation, which takes place under certain safeguards. The restructuring plan can consolidate the members of the corporate group, but the creditors remain separately classified for the purpose of voting and distribution. It is a practical way of respecting the corporate form.

15 William H. Widen, 'Corporate Form and Substantive Consolidation', 75 Geo. Wash. L. Rev.237 (2007), at 309.

In a consensual restructuring plan, there are procedural protections for, for instance, matters of classification of creditors, disclosure, solicitation and voting. Furthermore, for substantive matters, there is a best interests test. In the specific context of corporate groups, we may consider what would happen without any consolidation. In addition, cram-down may be applied, but this can be complex.

A formal versus the practical waterfall for a corporate group

Traditionally, in distributing assets of a corporate group, the so-called formal 'waterfall' is followed to address individual entitlements on: (i) liened assets, and (ii) realisable value traceable to specific group members and their claims. Based on the entity-by-entity approach, the aim would be to attribute assets to the individual member of the group and from there to the respective creditors. This also allows for structural subordination of specific claims and for asset partitioning. The remaining assets are divided among the remaining creditors on a *pari passu* basis. In this rather hierarchical approach, the entitlements are at the top and the *pari passu* principle is effectively at the bottom for the remaining creditors only. Much time and effort will be invested in allocating assets to the right entity within a group.

Another approach is proposed by Janger, which he refers to as the practical waterfall. It is designed to help those insolvent corporate groups, such as with Nortel, where there is a lot of value, but no clear distribution rules as it is hard to ascertain to which entity and within which jurisdiction the specific value belongs. Janger suggests taking firm value as a starting point, which in principle will be shared *pari passu* among all creditors of the corporate group. An exception is made for certain creditors where it can be proved that they have priority. This would, for instance, be the case of a lien, security interest, but also the realisable value of partitioned assets. The benefit of such an approach aligns better and deals more efficiently with the practical situation of a corporate group, with a group of assets on the one hand and many claims on the other hand.

8. Conclusion

At the conferences organised in December 2018 in Leiden and Vienna restructuring of corporate groups was discussed. The starting point was the ELI Business Rescue Instrument of 2017 that gave recommendations also on the treatment of corporate groups. As Madaus highlighted, theoretically, different approaches can be distinguished from limited coordination up until full substantive consolidation. Insolvent members of corporate groups in Europe are traditionally treated on an entity-by-entity basis. Other than the EIR 2015, domestic rules on corporate groups are limited in EU member states. Vananroye, who elaborated on the possibilities under Belgian law, also illustrated this. As highlighted by Vriesendorp, further research may consider the role of directors of (imminent) insolvent corporate groups in the European context.

The discussions have shown that approaches for restructuring of corporate groups are still very much in development, also within the European context. To date, there are no experiences yet with the group coordination proceedings under the EIR 2015. The use of other tools – such as insolvency protocols – is also not yet a typical practice across Europe. In a cross-border European setting, but also domestically, improving coordination by means of cooperation and communication by insolvency practitioners and courts may be the most feasible direction to pursue now. To this end, judges and practitioners may rely on recommendations and best practices, for instance the ELI Business Rescue Instrument, but also those from other standard-setting organisations – both domestically and internationally – that support the restructuring of corporate groups.