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RESEARCH ARTICLE

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The future of harmonisation of directors' duties in the European Union: The Preventive Restructuring Directive and group insolvencies

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Abstract

The European Union (EU) Preventive Restructuring Directive seeks to harmonise directors' duties with the goals of promoting early responses to financial distress and rescuing viable enterprises. However, due to the persistent differences in substantive laws and traditions of EU Member States – most notably concerning the recognition of group interest in company and insolvency law, general and imprecise wording of the Preventive Restructuring Directive and its insufficient attention to group insolvency, additional steps need to be taken to achieve these important goals. (i) This article maps the European debate on group interest, observes its emergence in bank resolution and points out the divergent approaches to its acceptance at the national level. (ii) It examines the recent work and recommendations of UNCITRAL on directors' obligations in the period approaching insolvency in enterprise groups, and (iii) critically analyses the approach of the Preventive Restructuring Directive. (iv) Finally, it discusses the alternative normative

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framework for further harmonisation of insolvency-related directors' duties in the EU. It suggests that instead of focusing on the interests of all stakeholders, it is far better to encourage reasonable steps to preserve and maximise the value of the debtor company. This could include consideration of the wider group environment and group interest, which should not make debtor's creditors worse off (group-mindful “no worse off” standard). It also endorses the adoption of guidelines and tools supporting the decision-making process in a crisis situation, creating *ex-ante* certainty and discouraging opportunistic behaviour.

1 | INTRODUCTION

The Directive on preventive restructuring frameworks (Preventive Restructuring Directive),[1] published in June 2019, acknowledges that in order to promote early restructuring, it is necessary to ensure that directors are not dissuaded from exercising reasonable business judgment or taking reasonable commercial risks.[2] At the same time, it establishes that where there is a likelihood of insolvency, directors need to:

i. have due regard to the interests of creditors, equity holders and other stakeholders;
ii. take steps to avoid insolvency; and
iii. avoid deliberate or grossly negligent conduct that threatens business viability.[3]

Nevertheless, it is unclear how these imprecise instructions should be applied in the context of integrated and interdependent cross-border corporate groups, where companies rely on each other for the provision of financing and other important functions and services.

The Preventive Restructuring Directive does not pay much attention to the enterprise group reality. It recognises that differences between national laws result in additional costs, which are most notable in the context of international groups of companies.[4] Nevertheless, substantive rules on directors' duties remain largely unharmonised. This is especially true for corporate groups, where the EU Member States take divergent approaches to the acceptance of a group interest. As a result, the adoption of a comprehensive and coherent group-wide solution (e.g., a group reorganisation plan or a going concern sale of all or a large part of the group's business) is complicated, and group entities and their directors may be disincentivised to enter into intra-group transactions, further aggravating financial difficulties and expediting the fall of a group.

In contrast to the European harmonisation, driven by the Preventive Restructuring Directive, the United Nations Commission on International Trade Law (UNCITRAL), already a decade ago, was mindful of the group insolvency context. In 2010, UNCITRAL approved Part Three of the Legislative Guide on Insolvency Law, which provided recommendations for the treatment of enterprise groups in insolvency. In 2013, Part Four was added, addressing directors' obligations in the pre-insolvency period. Finally, in 2019, in recognition of the specificity and importance of the directors' duties in a corporate group setting, UNCITRAL adopted an additional section to Part Four, covering the obligations of directors of enterprise group members in the period approaching insolvency. In parallel, the issues of corporate governance and directors' conduct in banking groups have been discussed by standard-setting organisations active in the area of bank supervision and resolution, such as the Financial Stability Board (FSB) and the Basel Committee on Banking Supervision (BCBS). The recommendations and guidelines proposed by these organisations may serve as inspiration for the harmonisation of certain aspects of directors' duties in a group (pre-)insolvency situation in the EU.

Imagine the following scenario: a director of one group entity considers extending a loan to another group member or approving a cross-guarantee or collateral for financing extended by an external lender to such a group member. The reason for entering into these transactions may be to preserve the operational continuity of the group as a whole and, in the long run, (potentially) benefit the providing entity. However, in the short run, the transactions may entail increased risks, as the support is granted to a financially distressed company, and the benefits are not straightforward. In this respect, UNCITRAL accepts that the broader context of an enterprise group should be considered in assessing the behaviour of directors and their duties.[5] For instance, it may be appropriate for a dependent subsidiary to provide financing to other group members:

> in order to keep [the] wider business operating and ultimately save the business of the subsidiary itself.[6]

It also considers that a certain degree of loss or detriment, even if only in the short term, should be allowed.[7]

However, intra-group transactions can pursue a goal of transferring liquid assets or value from one company to another in the vicinity of insolvency (asset dilution), ultimately to the detriment of the transferring entity and its creditors.[8] They may also result in the increase of the riskiness of the company's business (asset substitution) or its borrowing (debt dilution).[9] These are examples of opportunistic group behaviour, which needs to be controlled *ex-ante*, discouraged and remedied *ex-post*.[10] The opportunism is exacerbated in cases of conflicts of interest that may arise where the same director(s) is appointed in more than one enterprise group member.

The complexity of intra-group relations, together with the often-conflicting interests of group entities, their creditors or different pools of creditors, make the position of corporate directors particularly vulnerable and increase risks of their personal liability.[11] As aptly spotted by Licht, the "vicinity-of-insolvency duties form a notoriously murky area, where legal space warps."[12] In light of the above, the question arises: which principles and guidelines are and should be adopted to guide and govern directors' behaviour in a group (pre-) insolvency context while discouraging harmful actions? To explore this question, this article examines the concept of a group interest in company and insolvency law and in bank supervision and resolution (Part 2), reviews the position of UNCITRAL on directors' duties in the period approaching insolvency in enterprise groups (Part 3) and critically analyses the approach taken by the Preventive Restructuring Directive (Part 4). Part 5 suggests the avenues for further harmonisation of directors' duties across the EU Member States in the pre-insolvency period, with the emphasis on the insolvency of enterprise groups. Part 6 concludes.

2 | ENTERPRISE GROUPS AND THE ELUSIVE CONCEPT OF A GROUP INTEREST

2.1 | Company law and European harmonisation attempts

Groups of companies constitute a fact of modern economic life. It is recognised that they (and not single entities) have become the prevailing form of large-sized enterprises in Europe.[13] Multinational corporations are dominant and influential institutions in the global economy of today.[14] Such corporations vary in terms of their business and financial integration and organisational structure. While some groups constitute a conglomerate of self-sustaining and relatively independent entities, other act as a single integrated enterprise, pursuing the same business strategy.[15] There are multiple legitimate reasons why businesses decide to operate through networks of separate legal entities, including those related to the reduction of commercial risks and maximisation of financial returns.[16]

In view of the growing importance of enterprise groups in national economies and the European internal market, since the 1970s the regulation of corporate groups in the EU and the recognition of a group interest have attracted increased attention from academics and policymakers. In the mid-1970s, the Commission of the European Economic Community elaborated a proposal for a Ninth Company Law Directive that was based on the principles of German "concern law" (*Konzernrecht*) and conceived an autonomous body of law specifically targeting groups.[17] This proposal was abandoned due to insufficient support. Nevertheless, discussions about the harmonisation of group law in Europe continued in the 2000s[18] and are still ongoing.[19] Most of these academic initiatives have advocated for the acceptance of a group interest in one form or another.

In 2011, the Reflection Group on the Future of EU Company Law, established by the European Commission (EC) in 2010, issued a report in which it recommended adopting the approach recognising the interest of the group at the EU level.[20] It argued that this would enhance the flexibility of the management of groups in international business activities, provide directors of parent companies with legal certainty and give clarity to directors of subsidiaries as to which transactions they can approve without triggering personal liability.[21] Based on the report, the EC launched a public consultation that, among other things, contained a question regarding the recognition of a group interest. On the basis of generally positive responses, in 2012, the EC prepared the Action Plan, which considered launching an initiative for the recognition of the concept of a group interest.[22] Even though the Action Plan has not led to any legislative proposals, the debate among scholars continued.

For example, in 2015, the Forum Europaeum on Company Groups, a college of company law experts, came up with a proposal, in which it suggested that a subsidiary should be under a duty to follow directions from a parent, even if such directions were against subsidiary's interests, provided that a number of specific conditions have been satisfied. These depended on whether a subsidiary could be classified as a "Service" or "Ordinary" company. As an exception, it was noted that whenever a subsidiary entered into a business crisis "threatening its existence", directions from other group entities stopped having a binding effect without affecting the parent's duty to assist such a subsidiary.[23]

In 2015, the EC requested the Informal Company Law Expert Group (ICLEG) to once again study the issue of a group interest. In its thorough report of 2016, the ICLEG concluded that the introduction of an all-encompassing group interest might be a step too far since it would touch upon deep and long-standing national preferences concerning the protection of creditors and minority shareholders and would likely face opposition from the states which do not recognise the interest of the group.[24] Yet, ICLEG still advocated for the incorporation of a group interest with respect to wholly-owned subsidiaries. Notably, it stressed that clarity over such interest was essential to encourage intra-group financing (i.e., intra-group loans, financial guarantees (upstream and downstream), ultimately contributing to the EU's Capital Markets Union objectives.[25] Uncertainty about what is allowed and prohibited in intra-group financing may facilitate underinvestment[26] and opportunistic behaviour.[27]

More recently, in 2017, a group of scholars from 22 countries presented the European Model Companies Act (EMCA) as a tool to further integration of European company law.[28] The EMCA contains a separate chapter on groups of companies. On the one hand, it accepts that the management of the subsidiary may act in a way contrary to the interests of the subsidiary if the decision pursues the interest of the group as a whole.[29] However, the disadvantage shall not endanger the continued existence of the subsidiary. In this case, the management of the subsidiary may refuse to comply with instructions from the parent company.[30] On the other hand, the EMCA imposes on the parent company a duty to "effect a fundamental restructuring of the subsidiary" should such a subsidiary be at a "crisis point".[31]

These proposals have not resulted in the creation of a company law regulation of enterprise groups at the EU level. However, the regulation of groups at the national level, as well as the gradual acceptance of a group interest in company laws, are worth noting. Hopt distinguishes three regulatory models for groups:

i. regulation by general corporate and/or civil law (UK);
ii. regulation by special corporate group law (France with its *Rozenblum* doctrine, entailing a flexible balancing of interests of a parent and subsidiaries, and Germany, prescribing less flexible compensation rules); and
iii. regulation by other areas of law (accounting, labour, competition, product liability, tax, etc.).[32]

2.2 | Recognition of a group interest in bank supervision and resolution

Regulation of financial institutions and banking groups at the EU level is more developed and comprehensive compared to the regulation of non-financial enterprise groups. This is reflected in the rules concerning bank supervision and resolution. The former is evident in the consolidated supervision regime undertaken by the authorities of a home state pursuant to the Capital Requirements Regulation (CRR).[33] Detailed provisions on consolidated supervision are laid down in the Capital Requirements Directive (CRD).[34] An EU Member State where the ultimate parent or a holding company is incorporated will undertake consolidated supervision over the group's subsidiaries and branches as if it were a single institution.[35] The main goal of this supervision is to ensure that the activities of branches and subsidiaries do not undermine the financial stability of the parent company and the group as a whole.[36] In light of this, the CRR extends its territorial scope to cover subsidiaries located outside the EU and conducting banking activities. It provides for the creation of supervisory colleges and establishes special standards concerning intra-group exposures and the calculation of capital and liquidity on a consolidated basis.[37]

The CRD emphasises that financial institutions must have robust governance arrangements, entailing a clear organisational structure and effective processes to identify and monitor the risks and expeditiously respond to them.[38] In a group context, this means that a parent and its subsidiaries should meet these requirements on a consolidated or sub-consolidated basis.[39] The European Banking Authority (EBA) clarified that the management body of a subsidiary that is subject to the CRD should adopt and implement on an individual level the group-wide governance policies[40] and that a consolidating institution (i.e., parent) should consider the interests of all its subsidiaries and how the pursued strategies further the interest of each subsidiary and the interest of the group as a whole in the long term.[41] Thus, the EU bank supervision instruments acknowledge the interest of a banking group that is linked to risk management and long-term group policy. This is in line with the recommendations of the BCBS, under which the board of the parent company should operate a corporate governance regime that addresses potential intra-group conflicts of interest (e.g., arising from intra-group transactions) "in appropriate recognition of the interest of the group."[42]

The recognition of a group interest is even more visible in the area of bank resolution. Here, the Bank Recovery and Resolution Directive (BRRD) establishes an elaborate framework for coordination in the recovery and resolution of banking groups.[43]

The BRRD adopts a number of tools aimed at ensuring efficient recovery and resolution of banking groups. Among such instruments are resolution colleges,[44] group recovery and resolution plans[45] and a group resolution scheme process.[46] Nevertheless, the idea of a group interest explicitly appears only in the context of intra-group financial support.[47] The BRRD sets a uniform framework for group financial support agreements and mandates that the EU Member States shall remove any legal impediments to intra-group financial support transactions, which may include loans, guarantees and provision of collateral.[48] One of the conditions imposed by the BRRD relates to the objective of financial support. It should aim at preserving or restoring the financial stability of the group as a whole and should be in the interest of the group entity providing support.[49] Regarding the latter, the EBA explained that the assessment of financial support should take into account the interest of the group and the interest of the providing entity, which needs to be looked at from a group perspective (e.g., direct and indirect benefits of support, risks arising from the default of a receiving entity and destabilisation of the group).[50]

The BRRD empowers competent authorities to authorise the provision of support, despite non-compliance with prudential requirements (capital, liquidity and large exposures) of a providing entity.[51] However, this support must not jeopardise the liquidity or solvency of such an entity.[52] Thus, while a group interest is accepted and plays an important role in bank recovery and resolution, it does not trump or sacrifice the interests of an individual company that is a member of a banking group.

2.3 | Recognition of a group phenomenon and a group interest in insolvency law

The matter of directors' duties in the context of enterprise group insolvency has been a clear outlier. Rooted in national legal traditions and predominantly unharmonised insolvency law, it has fallen outside the recent EU harmonisation trend. As a result, such issues as the existence and scope of a group interest, obligations between a parent and subsidiary companies and their directors in the vicinity of insolvency, the permissibility of extending intra-group financial support in a crisis situation and the ways to address a potential conflict of interest, are solely governed by national law.

Notably, over the past decade, legislatures and international organisations have increasingly recognised particular problems caused by the insolvency of corporate groups and the need to develop special approaches and tools to address them. This recognition has occurred at the national, regional and international (soft law) levels. For example, in Europe, in the area of insolvency and restructuring, enterprise groups have, for the first time, been acknowledged in the European Insolvency Regulation of 2015 (EIR Recast).[53] At the national level, group insolvency is addressed in some EU Member States, including Germany,[54] Italy,[55] Spain[56] and France.[57] These legislative frameworks primarily concentrate on procedural aspects, such as jurisdiction, the appointment of a single insolvency practitioner (IP) and communication between courts and IPs. Hence, they do not conceptually deviate from the long-settled principle of entity separateness[58] and instead focus on promoting procedural efficiency. Procedural efficiency is also supported at the international level. In 2019, UNCITRAL adopted the Model Law on Enterprise Group Insolvency (MLEGI), which has not yet been implemented in national law.[59]

The emergence of these new instruments has not led to the harmonisation of insolvency-related directors' duties across the EU Member States,[60] especially when it comes to the recognition of a group interest.[61] In this respect, three categories of jurisdictions can be distinguished:

i. those which, to one extent or another, recognise a group interest as a valid consideration in guiding directors' behaviour in a situation of financial distress;
ii. those adhering to the strict entity-by-entity (atomistical or unitary) treatment or using special rules for compensation of any disadvantage arising from acting in the interests of a group; and
iii. those without a settled position on the issue.

In the first category are countries that recognise that a group interest can play a certain role, even though the exact limits and conditions for its usage are not always clear and may diverge. For example, Dutch courts have confirmed the existence of a "duty of group management" (*concernleidingsplicht*) of a parent company in an integrated group, including an obligation to actively oversee its subsidiaries in order to prevent insolvency or minimise losses.[62] Hence, liability may arise from discontinuing financial support to a subsidiary,[63] where the appearance of creditworthiness is created to third parties (e.g., creditors). Directors of a subsidiary may also take into account a group interest in their decision-making process, although this interest does not take precedence over the interests of an individual company.[64] For instance, the indirect benefits of an intra-group guarantee provided by a subsidiary to its parent will most likely qualify as a consideration, thus justifying its extension from the subsidiary's perspective.[65]

A similar approach is taken in Spain, where courts have accepted a margin of flexibility in realising a group interest to the detriment of an individual entity. This detriment, however, should not lead to the economic destruction (insolvency) of this entity. In the context of intra-group guarantees, the Spanish Supreme Court considered that patrimonial attribution or compensatory advantages (*teoría de las ventajas compensatorias*), even if indirect, in favour of a guarantor (e.g., subsidiary) could justify the provision of a guarantee.[66] English courts have also taken into account the group interdependence and survival of the group when reviewing individual transactions.[67] Other European countries in this group are France, Italy and Belgium.

The second category includes states that either deny the existence of a group interest or impose strict rules to protect individual entities and their creditors. Swedish law does not acknowledge a group interest. Traditionally directors of a parent company owe no duties to its subsidiaries, and vice versa, the board of a subsidiary, owes no duties to the parent company.[68] Similarly, the concept of a group interest is unknown in Finnish law, which adheres to a strict separate entity approach.[69] The acceptance of a group interest is either severely limited or denied under legislation or case law in Germany and the countries influenced by the German model, such as Austria, Croatia and Portugal.[70] The German group law does not devote attention to the advantages of being a member of a group and measures the disadvantages solely from the position of an independent company.[71] It also provides for mandatory compensation for any prejudices and disadvantages resulting from acting in a group interest.

The third category is represented by countries with no settled stance or case law on this issue. Among them is Greece, where the recognition of group interest and its exact content remains unclear.[72]

This very concise comparative overview, of course, does not attempt to provide an exhaustive or detailed account of various approaches existing in Europe. Instead, it highlights the major differences in regulation of directors' duties in a group (insolvency) context and the extent to which a group interest may factor into the decision-making of directors. These discrepancies ultimately complicate the operation of cross-border groups of companies. However, stakeholders – group entities, their directors and creditors – need certainty and predictability to be able to calculate the risks and take timely actions to address financial distress to avoid insolvency. These are the policy goals underlying the Preventive Restructuring Directive, discussed in more detail in Part 4.

3 | UNCITRAL AND DIRECTORS' DUTIES IN ENTERPRISE GROUP INSOLVENCY

The work of UNCITRAL on the topic of directors' duties in the context of enterprise groups in financial distress started in 2013. At that time, it was noted that there were "difficult practical problems" that could hinder business recovery and influence directors to prematurely initiate insolvency proceedings.[73] This is why UNCITRAL decided to develop additional principles and guidelines, building on and adding to the already existing Part Four of the Legislative Guide (2013). The completion of this work took around 5 years, since it had to be synchronised and aligned with the preparation of an instrument on enterprise group insolvency, the MLEGI. The text on the obligations of directors of enterprise group companies in the pre-insolvency period was finalised in 2018 and approved in July 2019 as an additional section in Part Four of the Legislative Guide. This new section puts forward several recommendations for balancing individual and group interests in a situation of financial distress and lays down the relevant directors' duties.

First, it acknowledges that:

> steps that may be regarded as detrimental to a company operating as a stand-alone entity may be reasonable when considered in [the] broader context.[74]

This is premised on the understanding that restructuring a group member may benefit from maximising the value of the enterprise group as a whole. Therefore, a collective or group interest may be taken into account by directors when making decisions that increase the value of an enterprise group or otherwise promote a group solution.[75]

To evaluate the benefits of such group-interest driven behaviour, directors may consider the position of the group member within the group, the degree of business integration between group entities, intra-group financial and other obligations, and assess whether more value is preserved or created by a group insolvency solution and whether the position of creditors is better off under this solution.[76] The reasonable steps may also include participation in informal negotiations with creditors organised at a group level, and where insolvency is unavoidable, cooperation with other group entities on matters of joint insolvency application in order to achieve jurisdictional centralisation.[77] These recommendations effectively introduce a group interest in the decision-making of an individual group entity.

Second, UNCITRAL envisages the "no worse off" standard that ensures that creditors of an individual group entity are not worse off under the steps which are taken for the benefit of a wider enterprise group or some of its parts than they would otherwise have been had those steps not been taken.[78] This test is similar to the "no creditor worse off" test embraced in many legal instruments to safeguard the rights of creditors and prevent opportunistic behaviour.[79] The application of this test is, however, adjusted to the group environment. It highlights that a group interest is not in itself a sufficient justification for the acts which are prejudicial and disadvantageous to the interests of creditors of a group entity. It is also suggested that a short-term detriment to such interests may be permitted for a realistic long-term benefit, where the interests of the individual entity and the group coincide.[80]

This group-mindful or group-sensitive "no worse off" standard may be applied in a multiplicity of situations where actions seek to preserve the group's going-concern value and operational continuity and where the group's business is economically viable,[81] and there are reasonable prospects of its financial recovery. Thus, a subsidiary may be permitted to forward funds to a parent company and therefore incur short-term losses, based on the understanding that such financing is within the long-term interests of or create long-term gains for the subsidiary,[82] such as where it depends on the parent company for its products, services or know-how. On the contrary, a behaviour where the interests of one group member (and its creditors) are sacrificed for the benefit of other group members or the whole group fails the "no worse off" test and should be discouraged.

Third, cases where a director holds a position in more than one enterprise group member may entail conflicts of interest, which intensify in the period approaching insolvency.[83] To address them, UNCITRAL foresees that the director should take reasonable steps to manage such conflicts. These steps might include:

i. obtaining advice to establish the extent of the different obligations owed to different group entities;
ii. disclosing the nature and extent of a conflict to the affected boards of directors and maybe even creditors;
iii. abstaining from voting on matters giving rise to a conflict or from attending board meeting where such matters are discussed;

iv. seeking the appointment of an additional director when the conflict of obligations cannot be reconciled; and (as a last resort)
v. resignation from the relevant board(s).[84]

The exceptionality of the resignation option is based on the understanding that it can actually often add to the difficulties that a company or companies are facing.[85]

4 | THE PREVENTIVE RESTRUCTURING DIRECTIVE AND INCOMPLETE HARMONISATION OF DIRECTORS' DUTIES

In 2014, the EC published the Recommendation on a new approach to business failure and insolvency, which encouraged the EU Member States to establish restructuring frameworks in order to reduce obstacles to the smooth functioning of the internal market and remove difficulties in restructuring cross-border groups of companies.[86] Since the Recommendation has only partially been followed by the EU Member States, the EC issued a proposal for a directive in 2016 (Proposal).[87] This Proposal contained an obligation for the EU Member States to impose specific duties on directors in the vicinity of insolvency, including a duty to have due regard to the interests of creditors and other stakeholders, to take reasonable steps to avoid insolvency and to avoid deliberate or grossly negligent conduct that threatens the viability of the business.[88] Most of these duties have now been incorporated in Article 19 of the Preventive Restructuring Directive.[89] It is, however, for two reasons, doubtful whether the Directive can lead to a desirable level of harmonisation.

First, the Preventive Restructuring Directive uses rather imprecise and vague language in describing directors' duties. For example, it obliges the EU Member States to ensure that, where there is a likelihood of insolvency, directors have due regard to the interests of creditors, equity holders and other stakeholders.[90] However, the terms "likelihood of insolvency",[91] "due regard", and "other stakeholders" are not defined in the text. Moreover, it does not provide any guidance on how to interpret and apply these concepts. This ambiguity can result in discrepancies at the national level, potentially creating the dichotomy between director-friendly and creditor-friendly regimes, bolstering regulatory competition and weakening harmonisation. While the regulatory competition is not bad per se,[92] it can produce certain negative externalities, lowering the protective standards and resulting in the "race to the bottom".[93]

Second, the Preventive Restructuring Directive largely overlooks the context of enterprise groups and the fact that the vast number of large (but also many medium-sized)[94] businesses operate across national borders through interconnected subsidiaries. In groups of companies, balancing conflicting interests becomes even more problematic due to multiple layers of stakeholders, different group members with different obligations to lenders and other creditors, and the level of group integration. In practice, tensions frequently arise when intra-group transactions (e.g., intra-group loans, cross-guarantees and cross-collateralisation) are concerned,[95] or where the same director holds a managerial or an executive position in one or more enterprise groups entities. Can a director of a subsidiary approve an upstream guarantee, even if it may be detrimental to its interests, taken separately, but where it is beneficial to the group as a whole and may promote the long-term survival of the subsidiary? To what extent should a group interest be recognised, and what are the outer limits of such recognition? How should a conflict of interest arising from the multiple directorships be addressed (if at all)?

The Preventive Restructuring Directive does not give answers to these questions and does not indicate any underlying principal notion on the matter.[96] In my opinion, the problem lies in the absence of a clear normative framework or underlying principles, which should drive the harmonisation of directors' duties in a group insolvency environment.

5 | GROUP INSOLVENCY AND FURTHER HARMONISATION OF DIRECTOR'S DUTIES IN THE EU

In November 2020, the European Commission launched the initiative aimed at enhancing the convergence of insolvency laws across the EU.[97] Among the potential areas for the alignment of the insolvency regimes, the EC lists "directors' duties related to handling imminent/actual insolvency proceedings."[98] As such, this is a welcome initiative. However, it remains to be seen what the actual proposal will look like, which rules will be subject to harmonisation and whether the enterprise group context will be addressed at all. This Part builds on the current position of the Preventive Restructuring Directive and discusses the principles that may be embraced to align the approaches to directors' duties in the context of group insolvency across the EU Member States.

5.1 | Stakeholder governance in the vicinity of insolvency

The Preventive Restructuring Directive argues that, in the vicinity of insolvency:

> directors should have due regard to the interests of creditors, shareholders and various other stakeholders.

From this formulation, we can infer that:

i. special directors' duties arise where there is a likelihood of insolvency;
ii. in this period, directors may (*seemingly*) enjoy a lesser level of deference to the business judgment than in regular times, as they need to consider a wider range of interests;
iii. the interests of creditors are merely one of a number of interests that must be considered by corporate managers; and
iv. no differentiations of ranking and status of stakeholder interests are proposed.

It is not entirely clear how different interests are to be determined in the first place and, if they can, how they should be balanced in case of a conflict. Competing interests of stakeholders, including inter-creditor conflicts, are typical for (pre-)insolvency situations and serving them at the same time might be a challenge.[99] The debate about balancing different interests in the (pre-)insolvency context is reminiscent of the discussion about stakeholder interests and corporate purpose in company law and corporate governance. A reference to this debate is sensible since it touches upon similar problems of determining which groups are considered stakeholders and of establishing a method to aggregate or balance the interests of relevant constituencies. In the absence of insolvency, creditors do not become residual claimants of the debtor, and their interests and powers do not substitute those of shareholders,[100] although the rules may need to be adjusted to reflect the changing economic conditions and managerial behaviour.[101]

In the EU, the increased attention to the topic of stakeholder governance is connected to the publication in July 2020 of the Final Report on the director's duties and sustainable corporate governance (Report).[102] This report, commissioned by the EC and prepared by EY, concluded that corporate boards generally do not take sufficient account of the long-term interests of stakeholders (e.g., employees, creditors, local communities and the society at large) other than shareholders.[103] To address this, it suggested various non-legislative and legislative options to increase stakeholder engagement in corporate governance.[104] The publication of the Report has triggered a wave of critical commentaries,[105] some of which pointed out that while arguing in favour of extending the circle of plaintiffs who can enforce directors' duties, the Report did not specify how stakeholders should be identified and delineated, who should be counted as a stakeholder and who should decide on that.[106]

The difficult task of identifying all relevant stakeholders is accompanied by no less difficult exercise of deciding on the trade-offs between the interests of different stakeholders, which may be – and typically are – starkly divergent.[107] The question is how and when directors should balance or choose between these starkly divergent interests.[108] It is hard to say what is expected of directors.

In this respect, Keay points out that:

> focusing solely on creditors' interests when a company is in the vicinity of insolvency might be a less demanding task rather than perhaps some sort of balancing of the interests of shareholders and creditors.[109]

Bebchuk and Tallarita study the issue from a company law perspective and claim that the increasingly influential approach that encourages or mandates directors to take decisions to favour and protect stakeholders – what they call "pluralistic stakeholderism" – is flawed and counterproductive.[110] According to them, stakeholderism can contribute to increased insulation of directors, granting them additional discretion and, in the end, making them less accountable. A similar view as applied to the insolvency context was shared by Paterson, who noted that the approach which imposes on directors the duty to consider or act in the interests of "creditors as a whole", ignoring how different they are, is murky and leaves ample room for directors to justify any chosen behaviour, even when the real motivating factor was the promotion of their self-interest.[111] Paradoxically, the duty to act for the benefit of all may result in acting for the benefit of none or in the self-serving behaviour of corporate leaders.[112]

Additional complexity arises if we assume, rather justifiably, that enterprise group members, either acting as shareholders or simply belonging to the same corporate group as the debtor, also belong to the ranks of stakeholders, whose interests must be given due regard.

In my view, instead of requiring directors to act in the interests of different stakeholders when insolvency is only likely, it may be more sensible to adopt the approach under which directors shall take reasonable steps to maximize the value of the debtor company, ensure continuity of its operations and its long-term survival. The exact course of actions required or allowed would depend on the economic situation and other factors (one size does not fit all). Following this approach, directors would be able to consider the interests of other group entities, address the enterprise group structure, its financial and operational characteristics and degree of financial and decision-making autonomy. However, directors' actions should be in line with the stated goal of value maximization and preservation of the viability of the debtor's business and should be reasonably likely to succeed.

This approach accommodates the "no worse off" test proposed by UNCITRAL and highlighted in Part 3. It resembles and learns from the approach to group financial support established by the BRRD and outlined in Part 2.

On the one hand, it acknowledges the existence of a group interest and permits acting for the benefit of other group entities or the group as a whole. In this way, it reflects the economic reality of group integration and interconnectedness. Besides, it might be in line with creditors' expectations, who can have the impression that the group acts as a single enterprise – the impression further intensified by the commonality of a brand, endorsement of the transaction by other group entities, consolidated financial statements, intra-group guarantees and cross-collateralisation of debt.[113]

On the other hand, it imposes important boundaries and limitations aimed at safeguarding the interests of debtor's creditors and at aligning shareholder value and stakeholder (creditor) value in the long term. Thus, actions aimed at siphoning funds from the insolvency estate or assuming liability without proper economic rationale and without the ultimate benefit to the debtor with a view to its long-term gain should not deserve legal protection. Arguably, taking into account the fact that crisis decision-making involves the "making of tough decisions in an environment of threat, urgency, and uncertainty",[114] and that there is usually increased pressure on directors from shareholders and other group entities, finding the right balance or making the right choice is problematic. Therefore, the decision-making process needs to be supported by the developed regulatory framework.

5.2 | Curbing excessive risk taking and promoting alignment of interests

In addition to the general approach described above, which could serve as a foundation for future harmonisation of directors' vicinity-of-insolvency duties across the EU, there may also be a demand to nudge directors to act in the value maximising way and to deter opportunistic high-risk behaviour and escalation of commitment.[115] For this, a number of tools or strategies can be embraced.

The first strategy includes the promotion of best practices for directors of financially distressed companies, such as those developed by UNCITRAL in Part Four of the Legislative Guide. For example, directors may need to ensure proper maintenance of accounts, acquire and rely on adequate and timely information, hold regular board meetings with comprehensive minutes, seek specialist advice or assistance to have an objective and independent view on the current state of affairs and proposed actions, consider the structure and functions of the business with a view to examining viability and reducing expenditure, and apply additional scrutiny to related party transactions.[116] These recommendations do not articulate the substantive outcome (i.e., which decision should be made) but instead focus on the decision-making process, improving information collection and generation and promoting better awareness and objectivity. They can also help address some of the pertinent cognitive biases intensified in the pre-insolvency period, including the self-serving bias, positive outcome (or optimism) bias and the illusion of control.[117]

The specificity of the context of an enterprise group and, most notably, of holding a managerial or an executive position in two or more group entities calls for additional steps and guidelines. Some of them were noted in Part 3, as proposed by UNCITRAL.[118] These guidelines seek to improve the decision-making in corporate groups by imposing requirements related to the evaluation of the current financial situation of the debtor and the group, consideration of intra-group financial and operational links and interdependencies, assistance in the development of a group insolvency solution, holding and participating in negotiations with creditors held at a group level, as well as taking steps to manage a conflict of obligations.[119] Following these guidelines should expand directors' information base and contribute to the formation of an independent and unbiased view on decision alternatives, and ultimately to rational decisions.

However, taking into account the irregularity of the event of financial distress (compared to business-as-usual events), significant complexity imposed by the variety of interests, including those of other group entities and the group as a whole, high uncertainty and considerable time pressure, choosing a "correct" alternative could be a demanding task. To address this concern, countries have developed various tools to support the decision-making process in a situation of financial distress and potential insolvency and to encourage early actions. Among these tools are safe harbour provisions[120] and frameworks for the *ex-ante* authorisation of a certain course of actions.[121] The *ex-ante* control and approval of transactions are in line with the rules of the Preventive Restructuring Directive on the protection of new and interim finance[122] and other restructuring-related transactions.[123]

Importantly, all these tools target the process of pre-insolvency decision-making rather than the result of the chosen course of action, which retains a degree of uncertainty and whose *ex-post* analysis may be clouded by hindsight and outcome biases.[124] They allow directors to explore restructuring options with limited or manageable risks but within a pre-established or supervised framework.[125] As a consequence, the focus is shifted from the *ex-post* search for the hypothetical "correct" decision to the acknowledgement of a large variety of "acceptable" decisions while preventing opportunistic and ill-informed ones. Another benefit of this approach is that it can be introduced with relative ease and be replicated across jurisdictions, without significant incursions into the existing national legal frameworks.

6 | CONCLUDING REMARKS

Insolvency of enterprise groups is rightfully considered to be one of the most complex fields of law, where the approaches of the EU Member States significantly diverge. This also applies to insolvency-related directors' duties in a cross-border parent-subsidiary setting. The absence of a clear and coherent standard makes it difficult for directors to determine *ex-ante* whether their actions comply with applicable law(s), resulting in increased transaction costs of corporate governance and affecting the ability of companies in a crisis to reorganise their affairs. While some states have special rules for group insolvencies and accept the importance of preserving group synergies, others take a more atomistical or unitary approach.

The EU Preventive Restructuring Directive, published in 2019, seeks to harmonise directors' duties with the goals of promoting early responses to financial distress and rescuing viable enterprises. Nevertheless, keeping in mind the persistent differences in substantive laws and traditions of the EU Member States – most notably with respect to the recognition of a group interest in company and insolvency law, general and imprecise wording of the Preventive Restructuring Directive and its insufficient attention to group insolvency, additional steps need to be taken to achieve these important goals.

This article has shown that the current approach of requiring directors in the vicinity of insolvency to have due regard to the interests of various stakeholders, without providing any guidance on how to determine the relevant stakeholders and how to balance their (often conflicting) interests, may not accomplish the desirable protective and enabling functions. Somewhat counterintuitively, it may actually insulate directors in their decision-making and create uncertainty about the requisite and allowed behaviour.

This article has suggested that, instead of asking directors to act in the interests of all stakeholders, it is more feasible to focus on reasonable steps to preserve and maximise the value of the debtor company, ensure its operational continuity and prosperity over a long-term horizon. This approach is flexible enough to encompass the concept of a group interest, based on the realisation that the debtor's interests may be closely intertwined with those of other group entities and overlooking the latter may undermine restructuring attempts. However, as a necessary prerequisite, I have argued that the "no worse off" standard should be embraced to guarantee that the interests of creditors of the debtor are not sacrificed for the benefit of other group members or the group as a whole. This approach has been advocated by UNCITRAL and can be seen in the BRRD.

Additionally, in order to help directors to navigate in the environment of uncertainty, to mitigate behavioural biases and to improve the decision-making process, a number of guidelines and regulatory tools may be adopted, including *ex-ante* authorisations and safe harbours. The attention is therefore shifted from the result to the process. This normative framework and tools may serve as a basis for the future harmonisation of directors' duties to promote efficient group restructuring and to prevent group opportunistic behaviour.

ENDNOTES

1 Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt (Preventive Restructuring Directive/PRD).

2 Ibid., Recital 70.

3 Ibid., Article 19.

4 Ibid., Recital 7.

5 UNCITRAL Legislative Guide on Insolvency Law, Part Four: Directors' obligations in the period approaching insolvency (including in enterprise groups) (2nd edn) (UNCITRAL, 2019), Chapter II, paragraph 1, noting that "it might be desirable for the law to permit the broader context of the economic reality of the enterprise group to be taken into account in determining the steps that should be taken by a director to avoid liability for breach of those obligations."

6 Ibid., paragraph 10.

7 Ibid., paragraph 4.

8 Richard Squire, "Limits of Group Structures and Asset Partitioning in Insolvency: Supressing Value and Selective Perforation by Means of Guarantees", in Richard Squire et al. (eds), *The 800-Pound Gorilla. Limits to Group Structures and Asset Partitioning in Insolvency* (Eleven International Publishing, 2019), 2, describing the practice of "selective" bankruptcy involving a strategic placing of a single group member into insolvency and stripping it of the value (asset dilution). Other strategies which may harm the interests of creditors include claim dilution and asset substitution.

9 See John Armour, Gerard Hertig and Hideki Kanda, "Transaction with creditors", in Reinier Kraakman et al. (eds), *The Anatomy of Corporate Law: A Comparative and Functional Approach* (3rd edn) (OUP, 2017), 111–112.

[10] On shareholder opportunism and strategies to counter it, see Aurelio Gurrea Martínez, "Towards an Optimal Model of Directors' Duties in the Zone of Insolvency: An Economic and Comparative Approach" (2021) 21 *Journal of Corporate Law Studies*, online access <https://doi.org/10.1080/14735970.2021.1943934>.

[11] This article does not deal with directors' liability under criminal, company or tort law, but solely focuses on directors' obligations under insolvency law.

[12] Amir Licht, "My Creditor's Keeper: Escalation of Commitment and Custodial Fiduciary Duties in the Vicinity of Insolvency" (ECGI Working Paper No. 551/2020) (October 2020) <https://ssrn.com/abstract=3680768>.

[13] Report of the Reflection Group on the Future of EU Company Law (5 April 2011), 59, also noting that the "group management is the heart of this leading business organisation" and arguing that any EU legislation in this area "should seek to maintain and enhance the flexibility of the management of groups."

[14] Phillip Blumberg, "The Transformation of Modern Corporation Law: The Law of Corporate Groups" (2005) 37(3) *Connecticut Law Review* 605, arguing that "traditional corporation law presupposing as its subject the individual corporation and looking upon it as the basis legal unit entity no longer adequately serves all the needs of modern jurisprudence." See OECD, *Duties and Responsibilities of Boards in Company Groups, Corporate Governance* (OECD Publishing, 2020).

[15] For classification of corporate groups, see Irit Mevorach, *Insolvency within multinational enterprise groups* (OUP, 2009).

[16] UNCITRAL Legislative Guide on Insolvency Law, Part Three: Treatment of enterprise groups in insolvency (UNCITRAL, 2010), Chapter I, paragraphs 17–25.

[17] For a review of main provisions, see Klaus Bohlhoff and Julius Budde, "Company Groups – the EEC Proposal for a Ninth Directive in the light of the Legal Situation in the Federal Republic of Germany" (1984) 6 *Journal of Comparative Business and Capital Markets Law* 163.

[18] Forum Europaeum Corporate Group Law, "Corporate Group Law for Europe" (2000) 1 *EBOR* 165; Report of the High Level Group of Company Law Experts on a Model Regulatory Framework for Company Law in Europe (2002) 97, noting that it is feasible to establish a framework rule that allows the adoption and implementation of a group policy, provided that the interests of creditors are sufficiently protected.

[19] Martin Winner, "Group Interest in European Company Law: An Overview" (2016) 5(1) *Acta Universitatis Sapientiae: Legal Studies* 85; Martin Gelter, "EU Company Law Harmonization between Convergence and Varieties of Capitalism" (ECGI Law Working Paper No. 355/2017) <https://ssrn.com/abstract=2977500>. European Company Law Experts (ECLE), A Proposal for the Reform of Group Law in Europe (2017) 18 *EBOR* 1.

[20] Report of the Reflection Group (above note 13).

[21] The report did not elaborate the application of a group interest in a group insolvency scenario, only noting that further consideration of this principle should distinguish between two situations: (i) where a subsidiary is not close to insolvency or insolvent, and (ii) where a subsidiary is close to insolvency or insolvent. Report of the Reflection Group (above note 13), 64.

[22] Action Plan: European company law and corporate governance - a modern legal framework for more engaged shareholders and sustainable companies, COM/2012/0740 final.

[23] Forum Europaeum on Company Groups, "Proposal to Facilitate the Management of Cross-Border company Groups in Europe" (2015) 12(2) *ECFR* 300, 306.

[24] The Informal Company Law Expert Group (ICLEG), Report on the recognition of the interest of the group (2016), 41 <https://ec.europa.eu/info/sites/info/files/icleg_recommendations_interest_group_final_en_0.pdf>.

[25] Ibid., 35.

[26] Irit Mevorach, "The Role of Enterprise Principles in Shaping Management Duties at Times of Crisis" (2013) 14(4) *EBOR* 471, 492, pointing out that "it is often the group that can actually assist (rather than harm) the insolvent entity in resolving its financial difficulties, for example, by providing business opportunities, new financing, guarantees to lenders and so forth."

[27] Stephen Bainbridge, "Much Ado About Little? Directors' Fiduciary Duties in the Vicinity of Insolvency" (2007) 1(2) *Journal of Business & Technology Law* 335, 355, observing that "absent clear standards, directors will be tempted to pursue their own self-interest."

[28] European Model Company Act (EMCA) (First Edition) (2017) <https://ssrn.com/abstract=2929348>.

[29] Ibid., section 15.16(1).

[30] Ibid., section 15.16(3).

[31] Ibid., section 15.17(1).

[32] Klaus Hopt, "Groups of Companies: A Comparative Study of the Economics, Law, and Regulation of Corporate Groups", in Jeffrey Gordon and Wolf-Georg Ringe (eds), *The Oxford Handbook of Corporate Law and Governance* (OUP, 2018), 610–615.

[33] Article 4(41), Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms.

[34] Articles 111–115, Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms.

[35] Article 4(47), CRR.

[36] Recital 47, CRD.

[37] For an overview and analysis of European rules on bank consolidated supervision, see Dalvinder Singh, *European Cross-Border Banking and Banking Supervision* (OUP, 2020), paragraphs 3.31–3.40.

[38] Article 74(1), CRD.

[39] Ibid., Article 109(2).

[40] EBA, *Final Report: Guidelines on internal governance under Directive 2013/36/EU* (EBA/GL/2017/11) (2017).

[41] Ibid., paragraphs 83 and 85.

[42] BCBS, *Guidelines: Corporate governance principles for banks* (July 2015), paragraph 96. At the same time, where a group policy is detrimental to the sound and prudent management of a subsidiary or leads to a breach of applicable law, the subsidiary should be able to make the necessary adjustments (paragraph 98).

[43] Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms.

[44] Articles 88 and 89, BRRD (European resolution colleges). See also Michael Schillig, *Resolution and Insolvency of Banks and Financial Institutions* (OUP, 2016), paragraphs 16.58–16.65.

[45] Articles 7 and 12, BRRD.

[46] Ibid., Articles 91 and 92.

[47] For an overview of rules and operation of intra-group support agreements under the BRRD, see Ilya Kokorin, "Intra-Group Financial Support in a Crisis: Between Rescue and Abuse" (2020) 29(5) *Norton Journal of Bankruptcy Law and Practice* 378.

[48] Article 19(4), BRRD.

[49] Ibid., Article 23(1)(b).

[50] EBA, Guidelines specifying the conditions for group financial support under Article 23 of Directive 2014/59/EU (EBA/GL/2015/17) (9 July 2015).

[51] Article 23(1)(g), BRRD.

[52] Ibid., Article 23(1)(e).

[53] Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings.

[54] § 3a, Insolvenzordnung (InsO) (Gruppen-Gerichtsstand). See also § 269d-269i, Insolvenzordnung (InsO) (Koordinationsverfahren), introducing coordination proceedings.

[55] Article 284, Codice della crisi d'impresa e dell'insolvenza in attuazione della legge 19 ottobre 2017, n. 155. Andrea Zorzi, "The Italian Law Reform" (2019) <https://ssrn.com/abstract=3492422>. Diego Corapi and Domenico Benincasa, "The Law on Groups of Companies in Italy" (2019) 16(4) *European Company Law Journal* 121.

[56] Artícle 25, *Ley Concursal*, allowing a debtor or a creditor to submit a petition for declaration of joint insolvency proceedings of several debtors if they are part of the same group of companies.

[57] *Loi n° 2015–990 du 6 août 2015 pour la croissance, l'activité et l'égalité des chances économiques* (sometimes referred to as *Loi Macron*), adding Article L. 721–8, *Code de commerce*. This article specifies jurisdiction of specialised commercial courts over certain insolvency proceedings and provides that companies facing an insolvency proceeding with subsidiaries in a similar position will be subject to the same court. See also Article L. 621–2, *Code de commerce*, which allows the extension of insolvency proceedings to a related company in the event of confusion of its assets with that of the debtor or of fictitiousness of that legal person.

[58] In insolvency, legal separateness is manifested in the principle of "five ones", whereas each company is treated separately, which leads to one insolvent debtor, one insolvency estate, one insolvency proceeding, one court and one insolvency practitioner. See Bob Wessels and Stephan Madaus, "Rescue of Business in Insolvency Law, Instrument of the European Law Institute" (2017), paragraph 697 <https://ssrn.com/abstract=3032309>.

[59] UNCITRAL Model Law on Enterprise Group Insolvency, 2019. The MLEGI offers the tools supporting the development of group insolvency solutions, based on communication, cooperation and coordination. See Irit Mevorach, "A fresh view on the hard/soft law divide: implications for international insolvency of enterprise groups" (2019) 40(3) *Michigan Journal of International Law* 505.

[60] Gerard McCormack et al., *Study on a new approach to business failure and insolvency. Comparative legal analysis of the Member States' relevant provisions and practices* (2016), 47, mentioning such duties as to consider the interests of creditors, take measures to avoid insolvency, to convene a meeting of shareholders to consider the necessary steps, etc. See also Carsten Gerner-Beuerle, Philipp Paech and Edmund Schuster, *Study on Directors' Duties and Liability* (2013), 208–224.

[61] This observation is by far not restricted to EU countries. See for example, the Australian case of *Westpac Banking Corporation v. Bell Group Ltd (in liq) (No 3)* (2012) 270 FLR 1, where directors' duties in the group insolvency context were in the spotlight. See Anil Hargovan and Jason Harris, "For Whom the Bell Tolls: Directors' Duties to Creditors after Bell" (2013) 35 *Sydney Law Review* 433.

[62] HR 21 December 2001, NJ 2005, 96 (*Sobi/Hurks*).

[63] For a similar rule in French law, see Article 442-6-I-5°, *Code de commerce*.

[64] HR 26 October 2001, NJ 2002/94 (*Juno*). See Steef Bartman, "Dutch Supreme Court at a Loss over Groups" (2016) 13(4) *European Company Law Journal* 123.

[65] Aart Jonkers, "Selective Perforation by Means of Guarantees: Dutch Law", in Squire et al. (eds) (above note 8), 79.

[66] Discussed by Mónica Naharro, "National Report on Spain", in Rafael Manóvil (ed), *Groups of Companies: A Comparative Law Overview* (Springer, 2020), 149.

[67] *Facia Footwear Ltd v. Hinchcliffe* [1998] 1 BCLC 218. See also *Re Oxford Pharmaceuticals Ltd, Wilson v. Masters International Ltd* [2010] BCC 834.

[68] Rolf Dotevall, "National Report on Sweden", in Manóvil (ed) (above note 66), 129. The lack of developed group law in Sweden, apart from areas of accounting and taxation, may at least partially be attributed to the effective social control that can counter agency problems. See Jonas Agnblad et al., "Ownership and Control in Sweden: Strong Owners, Weak Minorities, and Social Control", in Fabrizio Barca and Marco Becht (eds), *The Control of Corporate Europe* (OUP, 2002), 228–258.

[69] Ville Pönkä, "National Report on Finland", in Manóvil (ed) (above note 66), 495.

[70] The Informal Company Law Expert Group (ICLEG), *Report on the recognition of the interest of the group* (2016), 24.

[71] Hopt (above note 32), 624. See also Klaus Hopt, "Comparative Company Law", in Mathias Reimann and Reinhard Zimmermann (eds), *The Oxford Handbook of Comparative Law* (2nd edn) (OUP, 2019), 1151, noting that due to the rigidity of the German approach, it did not appear very attractive in most of EU Member States.

[72] Vassilios Tountopoulos, "National Report on Greece", in Manóvil (ed) (above note 66), 575.

[73] UNCITRAL, Report of Working Group V (Insolvency Law) on the work of its forty-fourth session (A/CN.9/798) (8 January 2014), paragraph 23.

[74] Legislative Guide, Part Four, Section II, Chapter II, paragraph 10.

[75] Ibid., Recommendation 267. The term "group insolvency solution" is used in the MLEGI. It is intended to be a flexible concept and may include reorganisation or sale as a going concern of the whole or part of the business or assets of one or more entities in a group. See Guide to Enactment of the MLEGI, paragraph 42.

[76] Legislative Guide, Part Four, Recommendation 268(1).

[77] Ibid., Recommendation 268(2).

[78] Ibid., Recommendation 267(b). Along these lines, Van Galen proposes a "group compensation rule", according to which: "[a]n insolvent group company may agree to a scenario which is in the interests of other group companies but detrimental to its own creditors only if accompanying measures are taken to ensure that its creditors receive at least what they would have received under the likely stand-alone scenario for this company." See Robert van Galen, "Insolvent Groups of Companies in Cross Border Cases and Rescue Plans" (Report to the Netherlands Association for Comparative and International Insolvency Law) (Conference of 8 November 2012) (NACIIL Report, 2012), 24 <http://www.naciil.org/publications/preadviezen-reports-2012/>.

[79] Article 10(2), PRD, referring to this test as the best-interest-of-creditors test; Article 74, BRRD; § 1,129(a)(7), US Bankruptcy Code.

[80] Legislative Guide, Part Four, Section II, Chapter I, paragraph 4.

[81] Viability is a complex concept, which may indicate competitiveness of the debtor's business model and good prospects for its post-restructuring survival. It also characterizes businesses whose going concern value exceeds their liquidation value. Attempts at restructuring non-viable enterprises can lead to the destruction of value, instead of its preservation or creation. See Lydia Tsioli, "Evaluating the Policy Effectiveness of the Directive on Restructuring and Insolvency: a Question of the Framework's Scope?", in Jennifer Gant (ed), *Harmonisation of Insolvency and Restructuring Laws in the EU, Papers from the INSOL Europe Academic Forum Annual Conference Copenhagen, Denmark* (INSOL Europe, 2019), 36. See also Matthias Kahl, "Economic Distress, Financial Distress, and Dynamic Liquidation" (2002) 57(1) *The Journal of Finance* 141, arguing that "[v]iable firms should be continued because their continuation value is higher than their liquidation value."

[82] See in this respect, Legislative Guide, Part Three, Recommendations 211–212.

[83] In *Klempka v. Miller (Re Parkside International)* [2010] BCC 309, the court characterised common directorship in a group context as the case "which foreshadows for group directors an almost impossible position, when one group member becomes insolvent."

[84] Legislative Guide, Part Four, Recommendations 269–270.

[85] Ibid., Section I, Chapter I, paragraph 4.

[86] Recommendation on a new approach to business failure and insolvency (C(2014) 1500 final) (12.3.2014).

[87] 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 (COM/2016/0723 final) (22.11.2016).

[88] Ibid., Article 18.

[89] The only visible difference relates the duty to take immediate steps to minimise the loss for creditors, workers, shareholders and other stakeholders, that was included in the Proposal, but not in the Preventive Restructuring Directive. This difference is not significant, because the steps to minimise the losses may be covered by other duties.

[90] Article 19(a), PRD.

[91] The Preventive Restructuring Directive uses different terms when referring to the pre-insolvency period, including the "likelihood of insolvency" (Recital 24, Articles 1, 19) and time when debtors "start to experience financial difficulties" (Recital 22). The Proposal also mentioned the "vicinity of insolvency" (Recital 36). The text clarifies that the term "likelihood of insolvency" is to be understood as defined by national law (Article 2(2)).

[92] Horst Eidenmüller, "The Transnational Law Market, Regulatory Competition, and Transnational Corporations" (2011) 18(2) *Indiana Journal of Global Legal Studies* 707, 748, noting that "[r]egulatory competition between the legal products of different states and the law market are, in principle, to be assessed positively and used as a process to discover which law is best."

[93] See Johanna Stark, *Law for Sale: A Philosophical Critique of Regulatory Competition* (OUP, 2019), Chapter 2.

[94] Commission Assessment accompanying Proposal for a Directive on preventive restructuring frameworks (SWD(2016) 357 final) (22 November 2016), 35, stating that "[t]here are more than one million SMEs in Europe which have subsidiaries or joint ventures abroad."

[95] Jens Dammann, "Related Party Transactions and Intragroup Transactions", in Luca Enriques and Tobias Tröger (eds), *The Law and Finance of Related Party Transactions* (OUP, 2019), 219, pointing out the difficulty of monitoring the fairness of intra-group transactions for creditors. See Elizabeth Warren et al. (eds), *The Law of Debtors and Creditors: Text, Cases, and Problems* (8th edn) (Wolters Kluwer, 2020), 526, explaining that intercorporate guarantees benefit both the creditor and the debtor in a loan transaction, but creditors of a guarantor providing a cross-stream guarantee can lose out in the transaction, since the guarantor may be pushed into insolvency.

[96] Moreover, the Preventive Restructuring Directive may even facilitate divergence to the extent that it accepts that countries may declare new and interim financing (e.g., loans, guarantees) void or voidable when extended by shareholders. See Recital 67, PRD.

[97] Enhancing the convergence of insolvency laws, Inception Impact Assessment, Ares(2020)6591479 <https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12592-Enhancing-the-convergence-of-insolvency-laws>.

[98] Ibid.

[99] Elizabeth Warren, "Bankruptcy Policy" (1987) 54(3) *The University of Chicago Law Review* 775, 777, arguing that insolvency "encompasses a number of competing – and sometimes conflicting – values in [the] distribution." For the role of stakeholders in the European insolvency law debate, see Gert-Jan Boon, "Harmonising European Insolvency Law: The Emerging Role of Stakeholders" (2018) 27(2) *International Insolvency Review* 150, noting that the field of insolvency law is "characterised by diverse stakeholders with strongly opposing interests."

[100] Andrew Keay, "The shifting of directors' duties in the vicinity of insolvency" (2015) 24(2) *International Insolvency Review* 140, 159, noting that if the company is not insolvent, "creditor interests should not override those of the shareholders totally."

[101] It is argued that in a situation of a financial distress, debtor's shareholders tend to prefer riskier strategies and "gamble for resurrection". See Paul Davies, "Directors' Creditor-Regarding Duties in Respect of Trading Decisions Taken in the Vicinity of Insolvency" (2006) 7 *EBOR* 301, 306, stating that in the vicinity of insolvency directors may focus solely on the upside however remote the probability of success is. The empirical evidence of risk shifting is inconclusive. See Assaf Eisdorfer, "Empirical Evidence of Risk Shifting in Financially Distressed Firms" (2008) 63(2) *The Journal of Finance* 609, supporting the hypothesis. See Erik Gilje, "Do Firms Engage in Risk-Shifting? Empirical Evidence" (2016) 29(11) *The Review of Financial Studies*, 2,925, finding that companies in distress actually reduce investment risk.

[102] EY, *Study on Directors' Duties and Sustainable Corporate Governance: Final Report* (2020).

[103] Ibid., 37.

[104] Ibid., VIII-IX.

[105] See Mark Roe et al., "The European Commission's Sustainable Corporate Governance Report: A Critique" (ECGI Law Working Paper 553/2020) (2020) <https://ssrn.com/abstract=3711652>. Alex Edmans, "Response to the EU Commission Study on Sustainable Corporate Governance" (2020); <https://alexedmans.com/wp-content/uploads/2020/10/European-Commission-Sustainable-Corporate-Governance.pdf>. See also Jesse Fried and Charles Wang, "Short-Termism, Shareholder Payouts, and Investment in the EU" (ECGI Law Working Paper 544/2020) (2020) <https://ssrn.com/abstract=3706499>.

[106] Paul Andersen et al., "Response to the Study on Directors' Duties and Sustainable Corporate Governance by Nordic Company Law Scholars" (Nordic & European Company Law Working Paper No. 20–12) (2020), 16 <https://ssrn.com/abstract=3709762>.

[107] *Prod. Res. Grp. LLC v. NCT Crp Inc.* 863 A. 2d 772 (Del. Ch. 2004), 790.

[108] The difficulty of addressing directors' duties through the lens of insolvency law, defining the moment when due consideration of creditors' interests needs to be given and what this means for directors, was in the spotlight of the recent case of *BTI 2014 LLC v Sequana S.A. & Ors* [2019] EWCA Civ 112 (6 February 2019).

[109] Keay (above note 100), 159.

[110] Lucian Bebchuk and Roberto Tallarita, "The Illusory Promise of Stakeholder Governance" (Harvard Law School John M. Olin Center Discussion Paper No. 1052) (2020) <https://ssrn.com/abstract=3544978>. For criticism of stakeholder theory, see Elaine Sternberg, "The Defects of Stakeholder Theory, Corporate Governance" (1997) 5(1) *Corporate Governance: An International Review* 3, 4, asserting that balancing stakeholder benefits is an unworkable objective.

[111] Sarah Paterson, "The Paradox of Alignment: Agency Problems and Debt Restructuring" (2016) 17 *EBOR*, 497, 510. Paterson suggests replacing the test which imposes a vague obligation on directors to act in the interests of all creditors with the test of "whether the directors have sought to maximise the value of the company for all the stakeholders in preparing the business plan and projections on which the debt restructuring is based."

[112] This is an example of the two-masters-problem. See Frank Easterbrook and Daniel Fischel, *The Economic Structure of Company Law* (Harvard University Press, 1991), 38, writing that "A manager who is told to serve two masters (a little for the equity holders, a little for the community) has been freed of both and is answerable to neither." See Andrew Keay, *Board Accountability in Corporate Governance* (Routledge, 2015), 141.

[113] Kannan Ramesh, "Synthesising Synthetics: Lessons learnt from Collins & Aikman" (2nd Annual GRR Live New York, 2018), paragraph 22.

[114] Uriel Rosenthal and Paul 't Hart, "Experts and Decision Makers in Crisis Situations" (1991) 12(4) *Knowledge: Creation, Diffusion, Utilization* 350.

[115] Licht (above note 12), describing the escalation of commitment as a tendency of managers to unjustifiably continue failing projects.

[116] Legislative Guide, Part Four, Recommendation 256.

[117] On cognitive biases in the vicinity-of-insolvency decision-making, see for example, Mao-Wei Hung and Wen-Hsin Tsai, "Managerial optimism, CEO retention, and corporate performance: evidence from bankruptcy-filing firms" (2020) 44(3) *Journal of Economics and Finance* 506, analysing data on bankruptcy-filing firms in the US and concluding that managerial optimism is detrimental to operating performance at filing and survival prospects. See Frederik Drescher, *Insolvency Timing and Managerial Decision-Making* (Springer Gabler, 2014), 84, noting that the "context factors of the insolvency timing decisions are very likely to aggravate the manager's cognitive limitations."

[118] Legislative Guide, Part Four, Recommendation 268.

[119] Ibid., Recommendation 270.

[120] See for example, section 588GA, Corporations Act 2001 (Australia). The safe harbour regime in Australia was introduced in 2017 as a carve out from the insolvent trading liability. It applies where a director in the period of approaching insolvency engages in "one or more courses of action that are reasonably likely to lead to a better outcome for the company" and "the debt is incurred, or the disposition is made, directly or indirectly in connection with any such course of action." See Stacey Steele, Ian Ramsay and Miranda Webster,

"Insolvency law reform in Australia and Singapore: Directors' liability for insolvent trading and wrongful trading" (2019) 28(3) *International Insolvency Review* 363.

[121] Such an approval or authorisation framework has been introduced in the Netherlands in 2020 by the Act on Court Confirmation of Extrajudicial Restructuring Plans (*Wet Homologatie Onderhands Akkord* or WHOA). The WHOA added Article 42(a), Dutch Bankruptcy Act. It allows the court to grant an authorisation of a legal act at the request of the debtor, which protects the authorised acts from future annulment actions. The authorisation can be granted if (i) the debtor has started preparing a restructuring plan and has submitted the relevant statement with the court, (ii) the performance of the legal act in question is necessary for the debtor's business to continue during the preparation of a restructuring plan, and (iii) at the time the authorisation is granted, it may reasonably be assumed that the interests of the debtor's joint creditors would be served by such an act, while none of the individual creditors would be materially harmed. French law grants protection to transactions made in the context of the *conciliation* procedure, provided that the court has sanctioned the agreement (*homologation*), see Article L.611-4 *et seq*., *Code de Commerce*.

[122] Article 17, PRD.

[123] Ibid., Article 18.

[124] Niek Strohmaier et al., "Hindsight bias and outcome bias in judging directors' liability and the role of free will beliefs" (2020) 51(3) *Journal of Applied Social Psychology* 141.

[125] The use of safe harbours or similar protective regimes has been supported in literature. See Madaus and Wessels, (above note 58), Recommendation 1.16. Lorenzo Stanghellini et al. (eds), *Best Practices in European Restructuring. Contractualised Distress Resolution in the Shadow of the Law* (Wolters Kluwer, 2018), 119.

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