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Cramming down cross-border secured debt under the Insolvency Regulation and the Directive on Restructuring and Insolvency: laws in conflict or in development?

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Abstract

Article 8 of the European Insolvency Regulation provides creditors with security rights on assets located in another Member State than where insolvency proceedings are opened with the remarkable position that the opening of the insolvency proceedings cannot affect their security right. This has been heavily debated in the past, including whether art. 8 EIR protects against a reduction of the cross-border secured claim in foreign insolvency proceedings. This debate is cast in a new light by not only the increased interconnectivity of the European continent since the development of (predecessors of) art. 8 EIR, but also by the introduction of the Directive on Restructuring and Insolvency and the plan-proceedings it has sparked. Whilst art. 8 EIR aims to protect cross-border secured creditors against unexpected foreign insolvency proceedings, cross-border secured creditors can now no longer legitimately expect that other Member States have not implemented the Directive and incorporated in their national law plan proceedings that can bind secured creditors. The Directive not only shapes the legitimate expectations of cross-border secured creditors, it also sets a new standard for restructuring proceedings, including a new standard of creditor protection with the best interest test. This paper argues that in this light art. 8 EIR should be interpreted as to not prevent a cram-down of cross-border secured claims that meets the safeguards of the Directive, although amendment of art. 8 EIR to adapt it to the new Directive is to be preferred.

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1. Introduction

1. Over the last few decades the traditional focus of insolvency law has widened from orderly liquidation of a debtor's assets and distribution of the proceeds to include restructuring efforts, aimed at allowing debtors (or their businesses) to overcome financial difficulties. This is not only visible in the insolvency laws of the Member States, that have introduced all kinds of rescue procedures, but also shows on the European level. In the recast of the European Insolvency Regulation[1] (EIR) the European legislator widened the scope of this instrument, that was traditionally focused on liquidation, to include hybrid proceedings.[2] Moreover, in 2019 the EU pushed its Member States further in the direction of the so desired 'rescue culture' with the adoption of the Directive on Restructuring and Insolvency (also sometimes referred to as the Directive on Preventive Restructuring Frameworks).[3] This shifting focus can cause tension, since restructuring often involves, and insolvency laws aimed at restructuring facilitate, curtailing some creditors' rights in order to achieve a better outcome for all creditors, whilst traditional liquidation-oriented insolvency law aims to exercise the creditors' rights to take recourse.[4]

2. This tension becomes very clear when we focus on the position of a secured creditor, whose *in rem* security rights are vested in assets of the debtor located in a different Member State than the one in which the debtor's centre of main interests (COMI) lies. The Insolvency Regulation prescribes in article 8 that the opening of insolvency proceedings in one Member State shall not affect rights in rem over assets located in other Member States.[5] The interpretation of this provision has been the subject of substantial debate, particularly raising the question what effects of the insolvency proceeding would qualify as 'affecting' the cross-border security rights.[6] This paper aims to revisit that debate, and show how it is cast in a new light since the introduction of the Directive on

1 Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast).
2 Wessels-Madaus, *International Insolvency Law Part II* 2022/10425s.
3 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, and amending Directive (EU) 2017/1132.
4 Of course insolvency proceedings focused on liquidation may also inhibit certain individual creditor rights, for example by replacing liquidation by individual creditors themselves with collective liquidation by a court-appointed insolvency practitioner.
5 Art. 8 EIR.
6 Cf. Wessels-Madaus *International Insolvency Law Part II* 2022/10655 et seq. and Heidelberg-Luxembourg-Vienna report, par. 6.2.5.2.2, both with extensive further references.

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Restructuring and Insolvency, and the restructuring procedures it has sparked. More specifically, this paper aims to address whether a secured creditor with security rights on assets located in one Member State may be bound to an amendment of his claim (a haircut) as part of a restructuring plan confirmed by the courts of another Member State and if so, to what extent.

3. To put things in a practical perspective, consider the following two hypothetical examples.

4. First, a German company (i.e. with its COMI in Germany) has expanded into the Dutch market, with a loan from a Dutch bank that is secured by pledges on assets used in their Dutch operations. Confronted with unbearable left-over debts from the Covid-crisis, the company seeks to restructure its debt through the German public StaRUG-procedure.

5. Second, a Dutch company (i.e. with its COMI in the Netherlands) is financed by a Dutch bank with a loan. To secure repayment of the loan the company has pledged all its receivables to the bank. This includes claims against the company's customers in Belgium. Under the Insolvency Regulation claims are located at the debtor of the claim (i.e. in Belgium)[7], so this pledge is a cross-border security right if insolvency proceedings are opened in the Netherlands.[8] Similarly, pledging shares in foreign subsidiaries can quickly turn a seemingly national matter into a cross-border one.[9]

6. Now both companies seek to restructure their debt through a composition plan, the Dutch one through the public WHOA-proceeding, the German one through the public StaRUG-procedure. In both cases the restructuring plan considers that in a liquidation proceeding the bank would be able to recover 75% of its claim through foreclosure of its security rights. The remaining 25% of the claim is an ordinary unsecured claim upon which in liquidation 5% would be paid, i.e. another (5% * 25% =) 1.25% of the total claim. Under the plans,

7 Art. 2 (9) (i) EIR.

8 Moreover, the law applicable to vesting security rights in claims is as of yet determined by national international private law. Dutch law applies the law of the obligation to vest the security right, which in this case is Dutch law as applicable to the Dutch financing agreement; art. 10:135 Dutch Civil Code. Under the proposed Regulation on the law applicable to the third-party effects of assignments of claims the claim against the Belgian customer could also be pledged according to Dutch law, as the law of the pledgor.

9 Art. 2 (9) (viii) EIR.

the claim of the Dutch bank is placed in two classes.[10] In the secured class, in which 75% of the secured claim is placed, the bank is not confronted with a haircut, only with a forced extension of the maturity date. In the unsecured class, in which the remaining 25% is put, the bank is offered a payment of 20% on this unsecured 25% of its claim, implying an 80% haircut on this unsecured part. Thus, in total, the plans offer 80% of the original claim (75% * 100% + 20% * 25% = 80%). Both courts confirm the plan. This raises the question whether after confirmation and execution of the plan, the Dutch banks can still foreclose on its rights of pledge to recover the unpaid 20% of their claim.[11]

7. In both examples art. 8 EIR comes into play, because art. 8 EIR applies to all security rights vested on assets located outside of the Member State where the insolvency procedure, in this case the plan proceedings, are opened. It does not require that the secured creditor is located in another Member State than where the plan proceedings take place.

8. Viewed from art. 8 EIR, this boils down to the question whether under the Insolvency Regulation a cram-down on cross-border secured claims is possible. The answer to this questions requires a delicate interplay between the Insolvency Regulation and the Directive on Restructuring and Insolvency. In the following, I will first explore the problem at hand through the provisions of the Insolvency Regulation (par. 2), then consider the approach of the Directive on Restructuring and Insolvency (par. 3), and ultimately try to reconcile the two instruments (par. 4). For brevity, I will use the term 'cross-border security rights' for *in rem* security rights vested in assets located in a Member State other than the Member State in which the debtor has its centre of main interests under the Insolvency Regulation. 'Cross-border secured creditors' are then creditors whose claims have been secured with cross-border security rights. I will refer to the current recast Insolvency Regulation simply as the Insolvency Regulation, and treat earlier sources that strictly speaking mostly discuss art. 5 of the original Insolvency Regulation (or even its predecessor), as discussing art. 8 of the current Insolvency Regulation, which is the exact same as its predecessors. Where is referred to restructuring proceedings, reference is made to plan-like proceedings envisioned in Title II of the Directive on Restructuring and

10 Bifurcation is prescribed by art. 374 of the Dutch Bankruptcy Code. The same applies in many other Member States. See for example under German law art. 24 (1) no. 2 and (3) StaRUG, and T. Pogoda & C. Thole, 'The new German "Stabilisation and Restructuring Framework for Businesses"', *EIRJ* 2021-6, p. 12. See further below for further references on other Member States.

11 Assuming the Dutch bank has not consented to the plan.

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Insolvency such as the Dutch WHOA, the German StaRUG, and many other similar European procedures. These all essentially consist of a debtor (or a court-appointed expert) proposing a restructuring plan to the creditors and/or shareholders, upon which the creditors and/or shareholders decide by voting in classes, and which is ultimately confirmed or rejected by a court. As all national restructuring proceedings that are implementations of the Directive on Restructuring and Insolvency contain the common core of the Directive on Restructuring and Insolvency, I will focus on those shared characteristics as laid down in the Directive on Restructuring and Insolvency. Moreover, since this paper focuses on restructuring proceedings and their treatment under the European Insolvency Regulation, it excludes from consideration proceedings that are outside the scope of the European Insolvency Regulation, as may for example be the case for the private restructuring plans under the Dutch WHOA and the German StaRUG.[12]

2. Cross-border security rights under the Insolvency Regulation

2.1 Starting point

9. The Insolvency Regulation aims to address the questions of private international law that may arise in the context of cross-border insolvency proceedings.[13] Hence, the Insolvency Regulation addresses the three traditional questions of private international law: i) which court has jurisdiction? ii) which law applies? and iii) can judgements rendered in one jurisdiction be recognized and enforced in other jurisdictions?

10. The Insolvency Regulation then answers these question with quite a straight-forward approach. The court of the Member State in which the center of

12 Whether or not such private plan proceedings fall within the scope of the EIR is outside the scope of this paper. I will focus on those restructuring proceedings that are placed on annex A of the Insolvency Regulation, for which there can be no doubt that the Insolvency Regulation applies. See further, *inter alia*, J. Schmidt, *Preventive restructuring frameworks: jurisdiction, recognition and applicable law*, IIR 2022; 31:81-100; R. Mokal, *What is an insolvency proceeding? Gategroup lands in a gated community*, IIR 2022; 31:418-473, W.J.E. Nijnens, 'Internationaal privaatrechtelijke aspecten van de WHOA', *TvI* 2019/34, P.M. Veder, 'Internationale aspecten van de WHOA: de openbare en de besloten akkoordprocedure buiten faillissement', *FIP* 2019/219, p. 60, G.Á.C. Orbán, 'Dull rerun or successful spin-off? Is the new 'private' version of the Dutch Scheme covered by the EU Judgments Regulation?', *FIP* 2022/112.

13 Recital 6 of the EIR, and ECJ 16 July 2020, ECLI:EU:C:2020:585.

main interest of the debtor lies (as the creditors can perceive it to lie)[14], has jurisdiction to open main insolvency proceedings, and its laws determine most consequences of the insolvency proceeding, including most powers of the insolvency practitioner.[15] In the interest of local creditors in other Member States secondary insolvency proceedings may be opened in such other Member State, but this is clearly not the preferred option.[16] Court decisions opening insolvency proceedings, and their consequences, are automatically recognized in all Member States.[17]

2.2 Turning to security rights

11. More specifically, the Insolvency Regulation aims to answer questions of private international law concerning the effect of the opening of insolvency proceedings on validly created *in rem* security rights. Art. 8 EIR provides that "*The opening of insolvency proceedings shall not affect the rights in rem of creditors or third parties in respect of (...) assets (...) belonging to the debtor which are situated within the territory of another Member State at the time of the opening of proceedings.*"

12. It has been argued that this should be interpreted as a conflict of law provision. Flessner interpreted it to mean that the cross-border security rights cannot be impeded by the insolvency law of the *lex fori concursus*, but the *lex rei sitae* applies.[18] Some ground can be found for this in the opinion of A-G Mazák and the ruling in the *ERSTE Bank Hungary* case.[19]

13. Others have suggested to interpret art. 8 EIR to mean that the cross-border secured creditor can only be limited in his rights by the *lex fori concursus* if

14 Recital 28 of the EIR, and ECJ 16 July 2020, ECLI:EU:C:2020:585.
15 Art. 7 EIR.
16 Cf. Recital 41 of the EIR, the 'Right to give an undertaking in order to avoid secondary insolvency proceedings' in art. 36 EIR and Wessels-Madaus 2022/10836b.
17 Art. 19 and 20 EIR.
18 A. Flessner, 'Dingliche Sicherungsrechte nach dem Europäischen Insolvenzübereinkommen' in: J. Basedow, K.J. Hopt & H. Kötz (red.), *Festschrift für Ulrich Drobnig*, Tübingen: Mohr Siebeck 1998, p. 277-287, esp. p. 285.
19 ECJ 5 July 2012, ECLI:EU:C:2012:417, at 41 and 42 and opinion of A-G Mazák,12 January 2012, ECLI:EU:C:2012:37, at 36. See J.T. Jol, *The Future of International Restructurings after the implementation of WCO II and the amendment of EIR: Is the Best yet to come?* (NACIIL Annual report 2015), The Hague: Eleven Publishing, 2016, p. 80.

the *lex rei sitae* provides for the same limitations[20], or that limitations by the insolvency law of the *lex rei sitae* are acceptable, but it is optional to the insolvency practitioner to invoke those.[21]

14. The prevailing interpretation however is that of art. 8 EIR as a 'hard and fast rule' of substantive law. This means that the rights in rem cannot be impeded as a consequence of the opening of insolvency proceedings either by the *lex rei sitae* or the *lex fori concursus*. The Virgós-Schmit report supports this interpretation,[22] and the literature largely follows this report[23].

15. In this prevailing hard and fast rule interpretation, art. 8 is an exceptional provision in the Insolvency Regulation. It solves a conflict of laws problem not with a choice-of-law rule, but with a uniform substantive rule.[24] It does not refer the matter at hand to any specific national law, but by itself dictates the outcome of the confrontation between cross-border security rights and an insolvency proceeding. Hence, art. 8 EIR is a uniform rule of substantive law specifically for cross-border matters, which limits the cross-border effects of insolvency proceedings.

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20 Compare S.C.J.J. Kortmann & P.M. Veder, 'De Europese Insolventieverordening', *WPNR* 2000/6421, who take the hard and fast rule interpretation as a starting point, but doubt its desirability and suggest this limited interpretation 'is not unjustifiable'.

21 A.J. Berends, *Insolventie in het internationaal privaatrecht* (Serie R&P InsR2), Deventer: Kluwer 2011, p. 337.

22 Virgós-Schmit report at 97.

23 M. Virgós & F. Garcimartín, *The European Insolvency Regulation: Law and Practice*, Kluwer Law International 2004, par. 163, B. Wessels, 'Secured rights of banks in international insolvency' in: N.E.D. Faber (ed., et. al.), *Bancaire zekerheid – Liber Amicorum mr. J.H.S.G.K. Timmermans*, Kluwer: Deventer 2010, par. 3.2, Wessels *Insolventierecht* X-II 2022/10654, R. van Galen, *An Introduction to European Insolvency Law*, Deventer: Wolters Kluwer 2021, par. 147; P. Smart, 'Rights in rem, article 5 and the EC Insolvency Regulation: An English Perspective', *Int. Insolv. Rev.* 17,33, Balz, 70 Am. Bankr. L.J. 485, 509 (1996), Snowden in Bork & van Zwieten (eds) *Commentary on the European Insolvency Regulation* (2nd edn), par. 8.44 et seq., Dirix & Sagaert, 'Verhaalsrechten en zekerheidspositieis van schuldeisers onder de Europese Insolventieverordening', *Revue de droit commercial Belge*, 2001580-600; further (with extensive references) Heidelberg-Vienna report, par. 6.2.5.2.2, Veder 2004, P.M. Veder, 'Goederenrechtelijke zekerheidsrechten in de internationale handels- en financieringspraktijk', in: R.W. Clumpkens (red., et al.), *Zekerhedenrecht in ontwikkeling* (Reports KNB 2009), Den Haag: Sdu 2009, p. 269-321, P.M. Veder, 'The Future of the European Insolvency Regulation – Applicable law, in particular security rights', *IILR* 2011, 285-297 supports it as *lege lata*, but challenges it as *lege ferenda*, P.M. Veder & J.J. van Hees, 'Internationale aspecten van het dwangakkoord ter voorkoming van faillissement', in A.C.P. Bobeldijk (et. Al), *Het dwangakkoord buiten faillissement (Vereeniging Handelsrecht 2017)*, Paris: Zutphen 2017, p. 192, P.M. Veder, 'Zekerheidsrechten en de Insolventieverordening: op zoek naar balans', *NTHR* 2013/2.

24 Virgós & Garcimartín 2004, par. 163, A-G Spuznar, opinion of 27 November 2014, ECLI:EU:C:2014:2404 (*Lutz/Bäuerle*), Struycken 2022, p. 255, Wessels *Insolventierecht* X-II 20222/10653a; Veder 2004, p. 340; MüKoInsO/Reinhart, 4. Aufl. 2021, VO (EU) 2015/848 art. 8 Rn. 17-18.

16. The substantive rule of art. 8 EIR is remarkable. It provides the holder of cross-border security rights with a better position than he would have under many national laws, which generally provide for some limitations on the ability of secured creditors to liquidate the encumbered assets.[25] Under German law, for example, it is not the secured creditor that sells encumbered assets but the insolvency practitioner, albeit that the proceeds of the encumbered assets are distributed outside of the insolvency proceeding.[26] Under Dutch law, the secured creditors can be bound by a so called 'cooling down period' (*afkoelingsperiode*), a special moratorium that can be ordered by the court during insolvency proceedings (including during restructuring proceedings), and the insolvency practitioner can set a reasonable time period within which the secured creditor must sell the encumbered assets upon penalty of losing the right to do so.[27] In the hard and fast rule interpretation of art. 8 EIR, cross-border secured creditors could be exempt from such limitations, and thus obtain a significantly better position than secured creditors with security rights in assets located within the Member State where insolvency proceedings were opened.[28]

17. This 'cross-border bonus' for secured creditors has been criticized before[29] and deserves increased scrutiny as insolvency proceedings shift their focus from liquidation to restructuring, as procedures aimed at restructuring may treat security rights differently from traditional liquidation-focused procedures. To evaluate this system further, we first need to examine the background of the hard and fast rule that creates the cross-border bonus.

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25 Veder 2013. As Veder 2004, p. 343 notes, the immunity from insolvency proceedings that art. 8 EIR provides cross-border secured creditors with is 'a considerable step backwards' from the developments in national laws seeking to engage secured creditors in reorganisations. See also R. Bork, *Principles of cross-border insolvency law*, Cambridge: Intersentia 2017, par. 6.13.

26 § 166 and 170 InsO.

27 Art. 63a for bankruptcy, art. 376 for restructuring proceedings, and art. 58 Dutch Bankruptcy Code.

28 As Veder puts it: *"Article 5 EIR [current art. 8 EIR, NP] in fact allows secured creditors in a cross-border context to acquire a position that they have under no existing insolvency law."*; Veder 2011; Virgós & Garcimartín note that this rule may 'overprotect' secured creditors, Virgós & Garcimartín 2004, nr. 164. See also Virgós 1998, p. 19, Wessels 2010, p. 349, Struycken 2022, p. 255; cf. Heidelberg-Luxembourg-Vienna report, par. 6.2.4.2.1.

29 For example Asser/Kramer & Verhagen 10-III 2022/395; Veder 2004, p. 342-347; J. Israël, *European Cross-border Insolvency Regulation*, Antwerpen: Intersentia 2005, p. 281-282, Veder & Kortmann 2000, Dirix & Sagaert 2001, p. 588, Berends 2011, p. 336, Veder 2011, no. 25; MüKoInsO/Reinhart, 4. Aufl. 2021, VO (EU) 2015/848 Art. 8 Rn. 17-18; Mankowski/Müller/Schmidt/J. Schmidt, 1. Aufl. 2016, EuInsVO 2017 Art. 8 Rn. 31-34; R. Bork, *Principles of cross-border insolvency law*, Cambride: Intersentia 2017, par. 6.22 with further references.

2.3 Background of the 'hard and fast rule', origins of the cross-border bonus

18. Recital 68 of the European Insolvency Regulation offers some, but little, guidance as to the reasoning behind art. 8 EIR:

19. *"(68) There is a particular need for a special reference diverging from the law of the opening State in the case of rights in rem, since such rights are of considerable importance for the granting of credit. The basis, validity and extent of rights in rem should therefore normally be determined according to the lex situs and not be affected by the opening of insolvency proceedings. The proprietor of a right in rem should therefore be able to continue to assert its right to segregation or separate settlement of the collateral security."*[30]

20. Notably, this recital does not mention any specific basis for the cross-border bonus. It stresses the importance of security rights because of the granting of credit, but this is a general consideration on the position of secured creditors in insolvency, and one that is widely recognised in the laws of the Member States. It does not explain why there should be a specific rule for treatment of cross-border security rights, other than the private international law questions mentioned in the recital, i.e. the reference to the lex situs.[31]

21. The Virgós-Schmit report offers a little more foundation for the rule of art. 8 EIR. It should be noted however that this report sets out by describing the aim of art. 8 EIR to be much more limited than the hard and fast rule interpretation provides for:

22. *"Rights in rem can only properly fulfil their function insofar as they are not more affected by the opening of insolvency proceedings in other Contracting States than they would be by the opening of national insolvency proceedings. This aim could be achieved through alternative solutions which were in fact discussed in the working party. However, to facilitate the administration of the estate the simplicity of the formula laid down in the current Article 5 [current art. 8 EIR, NP] was preferred by the majority: insolvency proceedings do not affect rights in rem on assets located in other Contracting States. [underlining NP]"*[32]

30 Recital 68 of the EIR.
31 Cf. Struycken 2022, p. 261.
32 Virgós-Schmit report at 97.

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23. Further reporting by Virgós confirms that the immunity of secured credit was not necessarily a policy goal in the drafting of the predecessor of art. 8 EIR.[33] In fact, the original idea when discussing cross-border security rights was '*to protect national creditors and third party holders of rights in rem from bankruptcy effects* which exceed those provided for by the insolvency rules of the lex causae of their rights *[underlining NP].*' This was not entirely achieved as '*[A] balance between the simplicity of application and the legal certainty provided for by this rule [current art. 8 EIR, NP] against competing alternatives convinced the Working Group in favour of maintaining this solution.*'[34]

24. This argument that, essentially, other systems than the current art. 8 EIR would be too complicated in practice[35], should in my opinion, in the current climate be taken with a grain of salt.[36] Firstly, information about the insolvency regimes of other Member States is widely available and traffics much more freely now than it did when the predecessors of art. 8 EIR were drafted during the three decades of negotiations that led up to the Convention on Insolvency Proceedings of 1995.[37] It has become much easier to know the law of other Member States.[38] The Recast Insolvency Regulation recognizes this where it explicitly gives the insolvency practitioner the possibility to give an undertaking that he will treat assets in other Member States and the proceeds thereof in accordance with the local law of that other Member State.[39] This assumes insolvency practitioners are able to do so. Moreover, where insolvency practitioners would need to inform themselves of the laws of another Member State, for example to deal with the security rights in accordance with the *lex rei sitae*, they should be

33 See (in addition to the following footnote) also Virgós & Garcimartín 2004, no. 154, which stresses that it was never a goal to provide the secured creditor with a better position than outside of insolvency proceedings, and therefore that the law governing the right in rem will still govern the priority of payment between the secured creditor and other creditors.

34 M. Virgós, The 1995 European Community Convention on Insolvency Proceedings: an Insider's View, Forum Internationale, Deventer: Kluwer, 1998, p. 19. See also p. 20: '*... again the idea of facilitating the administration of the etate and the purpose of achieving a PIL text of simple application was decisive: better but more difficult to administer PIL solutions would require constant recourse to legal services, added costs and time-delays*.' See also P.M. Veder, *Cross-border insolvency proceedings and security rights* (diss. Nijmegen, Law of Business and Finance volume 8), Kluwer: Deventer 2004, p. 342.

35 See also Virgós & Garcimartín 2004, no. 135b, Balz 1996, p. 509, A-G Szpunar at SCI Senior home, at 22.

36 See also Flessner 1998, p. 285, who already challenged the simplicity of the hard and fast rule in the case of foreign release of debts, and pointed out that the *lex rei sitae* approach would be much simpler.

37 The Convention was developed between the 1960's and 1995, see Virgós 1998. For context, internet first became available to consumers in 1993/1994.

38 Cf. R. Bork, *Principles of cross-border insolvency law*, Cambride: Intersentia 2017, par. 6.25.

39 Art. 36 EIR.

deemed more than qualified to assess whether they are willing to make that investment in foreign law advice.[40] Secondly, one should not overestimate the complexity of dealing with foreign security rights within the *lex concursus*, as many European security rights have similar characteristics.[41] Thirdly, in the field of international restructurings with cross-border secured creditors, the hard and fast rule interpretation of art. 8 EIR does not bring simplicity at all. It greatly enhances the complexity of such restructurings, practically forcing debtors to either pursue parallel proceedings in multiple jurisdictions or circumvent the Insolvency Regulation with the application of undisclosed restructuring proceedings.[42] Fourthly, the security and predictability that are often cited as the basis for the hard and fast rule-interpretation of art. 8 EIR do not require such a cross-border bonus. As Bork puts it '*Protection of trade does not necessarily mean granting the secured creditor the best solution possible but rather enforcing the principles of predictability (legal certainty) and protection of trust*'[43]. Although the immunity of art. 8 EIR delivers predictable outcomes to some extent (although often surprising because of its divergence from national laws), it is not necessary to achieve predictable results.[44] Lastly, the idea of protecting a secured creditor against application of a foreign and unknown lex concursus simply does not apply when the creditor is located in the same Member State as the debtor entering into plan proceedings, such as in the second example above. A Dutch bank financing a Dutch company may quickly become a cross-border secured creditor if its catch-all right of pledge turns out to encompass a claim against a debtor in another Member State, yet said Dutch bank financing a Dutch company can hardly be legitimately surprised by the application of Dutch insolvency law in the plan proceeding.[45]

25. All in all, one can wonder whether this argument of simplicity is (still) enough justification for the cross-border bonus. This has been a valid question for a

40 Cf. Berends 2011, p. 337.
41 Struycken 2022, p. 265.
42 See below, par. 4.3.2.
43 R. Bork, *Principles of cross-border insolvency law*, Cambridge: Intersentia 2017, par. 4.61.
44 R. Bork, *Principles of cross-border insolvency law*, Cambride: Intersentia 2017, par. 6.24.
45 The discussed example also opens up the question how to apply art. 8 EIR when the claim of the secured creditor is covered by multiple security rights, some vested in assets located within the Member State of the *forum concursus* and some vested in assets located in other Member States. Should in such cases the entire claim be considered a cross-border secured claim – as the cross-border security rights are vested for the entire claim –, or should it only be considered a cross-border secured claim to some limited extent, for example only where it concerns recourse on those cross-border secured assets? In the interpretation of art. 8 EIR proposed here this question is not relevant. Further, it is considered outside of the scope of this paper.

long time, especially given that the Virgós-Schmit report also shows the aim was never to create a cross-border bonus, but to give cross-border secured creditors the same position as they would have in insolvency proceedings opened in their own jurisdiction.[46] This question whether the argument of simplicity justifies the cross-border bonus is further challenged by not only the passage of time, including the interconnectivity of the European continent and the increased insight in other Member States legal systems that this has brought, but also more recently and more explicitly the European Directive on Restructuring and Insolvency, as we will see later on.

26. In support of the hard and fast rule interpretation one could argue that art. 8 EIR exists to protect the cross-border secured creditor's legitimate expectation that his security right shall not be limited by the application of an unforeseeable lex concursus.[47] This idea must also be met with scepticism. Firstly, given that insolvency laws of many Member States allow for some limitations on the rights of secured creditors, and that the Directive on Restructuring and Insolvency explicitly prescribes such possibilities, one can question whether a cross-border secured creditor can legitimately expect the complete immunity from insolvency proceedings that the substantive rule of art. 8 EIR prescribes in the hard and fast rule interpretation. Secondly, one may wonder if, for example, application of the lex rei sitae should really come as a surprise to the secured creditor as rights in rem usually are regulated by the lex rei sitae. Moreover, even if the lex concursus could limit the rights of the cross-border secured creditor, the lex concursus is determined by the centre of main interests which is constructed in exactly such a manner as to be predictable for creditors.[48] Hence, neither limitations in the context of insolvency proceedings nor application of the lex rei sitae or the lex concursus should come as a surprise to the cross-border secured creditor.[49] While Bork rightfully stresses that the principle of protection of trust only covers *legitimate* expectations[50], it is questionable whether it is a legitimate expectation of the secured creditor to

46 Virgós-Schmit report at 97, as quoted above.

47 Cf. Wessels 2010/18.5.3 and A-G Szpunar's conclusion before ECJ 26 October 2016, ECLI:EU:C:2016:804 (*SCI Senior Home*), at no. 22. Cf. recital 67 of the Insolvency Regulation, which considers that exceptions to the application of the *lex concursus* must be made to protect legitimate expectations.

48 Art. 3 (1) EIR, recital 28 thereof and ECJ 16 July 2020, ECLI:EU:C:2020:585 (*MH/Novo Banco*). Cf. R. Bork, *Principles of cross-border insolvency law*, Cambride: Intersentia 2017, par. 6.24.

49 Limitations by either law individually may come as a surprise, but as we will see later because of that some propose an opposition rule, where only limitations allowed by both laws are allowed.

50 R. Bork, *Principles of cross-border insolvency law*, Cambridge: Intersentia 2017, par. 4.56 and 4.57.

be left entirely unaffected by insolvency proceedings. Instead, by implementing the immunity from insolvency proceedings that art. 8 EIR provides in the hard and fast rule interpretation, the cross-border secured creditor is awarded a 'cross-border bonus' that the secured creditor could not have reasonably expected in any national case.[51] Expectations of such an immunity position can only be justified by the existence of art. 8 EIR and the hard and fast rule itself, but a rule cannot be based on the expectations that the rule itself creates.

2.4 Scope of protection

27. Art. 8 EIR does not provide limitless protection to the cross-border secured creditor.

28. Firstly, the hard and fast rule only applies as long as no secondary insolvency proceedings are opened in the Member State where the encumbered assets are located. If such secondary proceedings are opened, then the cross-border secured creditor is no longer a cross-border secured creditor within those secondary proceedings, because the encumbered assets are located in the Member State where those secondary proceedings are opened. Hence the *lex concursus* of the secondary proceedings will determine the position of the secured creditor in those proceedings.[52] Thus, if secondary proceedings are opened, the cross-border secured creditor must accept the limitations that the lex concursus of the secondary proceeding may place on (the exercise of) his security rights. As noted in the Heidelberg-Luxembourg-Vienna report, this undermines the position of the cross-border secured creditor under the hard and fast rule interpretation.[53] The insolvency practitioner in the main proceedings can request the opening of secondary proceedings in the Member State where the encumbered assets are located, and the secured creditor can hardly prevent that.[54,55]

51 R. Bork, *Principles of cross-border insolvency law*, Cambride: Intersentia 2017, par. 6.26, see also the quote by Veder in footnote 28.
52 Art. 35 EIR.
53 Heidelberg-Vienna report, par. 6.2.2.1.
54 Art. 37 EIR.
55 Incidentally, this means that secondary proceedings may operate contrary to the stated goal of secondary proceedings to safeguard the interest of local creditors (on this goal: art. 51 EIR, recital 40 of the EIR, Virgós 1998, p. 11.). These local secured creditors would be better off as cross-border secured creditors in the main proceedings than they are as local creditors in the secondary proceedings, in which they are not cross-border secured creditors that can invoke the protection of art. 8 EIR. This may be a possible defence against the opening of such proceedings.

29. Further, based on the wording of art. 8 EIR, it only protects the cross-border secured creditor from the effects of the *opening* of insolvency proceedings in another Member State. Looking at the cram-down in restructuring proceedings, one may well question if that can be considered the effect of the *opening* of insolvency proceedings at all. The cram-down of debt in restructuring proceedings is the result of the confirmation of the plan, which is in fact the end of the restructuring proceeding. Virgós & Garcimartín and Veder however reject any interpretation of art. 8 EIR with reference to it only mentioning the *opening* of insolvency proceedings. They argue this is incompatible with the legislative intention to limit the scope of this article and, in their view, this would also conflict with a strict literal interpretation because art. 8 EIR does not refer to the 'declaration of opening insolvency proceedings' but just 'the opening'.[56] They argue art. 8 EIR (that is, its equal predecessor) shields the security right from the entirety of the insolvency proceedings.

30. This argument has merit, but it does not do justice to the fact that the Insolvency Regulation still refers to the *opening* rather than the entirety of insolvency proceedings, whilst the Regulation provides for separate provisions on the recognition of judgements on the opening of insolvency proceedings (art. 19) and other provisions on the recognition of other judgements, including approval of composition plans (art. 32).[57] Because the Insolvency Regulation recognizes this difference, it is not clear that art. 8 EIR, which limits the effect of the *opening* of insolvency proceedings on rights in rem, also applies to confirmation decisions regarding restructuring plans, which *close* insolvency proceedings.[58] Moreover, the fact that the text of art. 8 EIR only refers to the opening of insolvency proceedings, and not to other decisions including the confirmation of restructuring plans, does not seem to be a drafting error, as article 9 and 10 contain the same wording, but article 11 through 14 – which are comparable to art. 8 in the sense that they mitigate the applicability of the *lex concursus* – more broadly regard all effects of insolvency proceedings. It would have been simple to similarly refer to all effects of insolvency proceedings in art. 8 EIR rather than just to the opening. In this light, the arguments to suggest

56 Virgós & Garcimartín, p. 107, Veder 2004, p. 351 and Veder 2009, p. 309.
57 Berends 2011, p. 340-341 and Heidelberg-Luxembourg-Vienna report, par. 6.2.5.2.2.
58 Duursma-Kepplinger 2002 concludes that an insolvency plan can reduce even cross-border secured claims, notwithstanding art. 8 EIR; Duursma-Kepplinger, commentary to art. 5 at no 37, in Duursma-Kepplinger, Duursma, & Chalupsky, *Europäische Insolvenzordnung – Kommentar*, Wien: Springer Verlag 2002. See also Wessels *Insolventierecht* X-II 20222/10653a, Heidelberg-Luxembourg-Vienna report, par. 6.2.5.2.2 (with further references), Berends 2011, p. 340-341.

that the reference specifically to the opening of insolvency proceedings in art. 8 EIR is unintentional or to be disregarded seem inconclusive. Case law has not clarified whether this distinction is relevant. The European Court of Justice did consider that (the predecessor of) art. 8 EIR does protect acts based on the security right to be conducted *after* the opening of insolvency proceedings, such as foreclosure, but this refers to acts of the secured creditor, not subsequent rulings of the court, or other elements of the insolvency procedure than the opening thereof.[59]

31. Lastly, and possibly most crucially, to determine the position of the cross-border secured creditor in restructuring proceedings one must decide whether art. 8 EIR only protects the security right itself, or also the underlying claim that the security right secures. The text of art. 8 EIR suggests that it only protects the security right itself: "The opening of insolvency proceedings shall not affect the *rights in rem* of creditors or third parties in respect of tangible or intangible, moveable or immoveable assets …". A claim, even when secured, is not a right in rem. Hence, the provision does not mention the secured claim.[60] It has been argued repeatedly that art. 8 EIR does not protect the underlying claim.[61] On the other hand, many have argued that for art. 8 EIR to be effective, it must also protect the underlying claim, because otherwise the protection of art. 8 EIR could be rendered useless by affecting the underlying claim.[62] This notion, that art. 8 EIR not only immunizes the security right, but also the secured claims, is thus presented as a corollary of the hard and fast rule interpretation. I will refer to it as such, and revisit this point later.

59 ECJ 16 April 2015, ECLI:EU:C:2015:227 (*Lutz/Bäuerle*).

60 The wording of the article does apply when a claim is the object that the security right is vested *in*, but here reference is made to the claim that the security right is vested *for*.

61 Cf. Piekenbrock in Heidelberg-Luxembourg-Vienna report, par. 6.2.5.2.2 with further references, Wessels-Madaus *International Insolvency Law Part II* 2022/10655, Struycken 2022, p. 256, McCormack & Bork, no. 77, cf. in doubt: Isaacs in Moss, Fletcher, Isaacs, *Moss Fletcher and Isaacs on the EU Regulation in insolvency proceedings*, OUP 2016, at no. 6.136.

62 McCormack & Bork, no. 77, Virgós & Garcimartín, p. 104, Veder 2011, at. 30; Snowden in R. Bork & K. van Zwieten (eds.), *Commentary on the European Insolvency Regulation*, (2nd edn), at 8.46; J. Marshall, 'The future of the European Insolvency Regulation – Rights in rem', *IILR* 2011/263, at 26; P. Smart, 'Rights In Rem, Article 5 and the EC Insolvency Regulation: An English Perspective' (2006) 15 *Int. Insolv. Rev.* 17, p. 33, S. van den Broek & S.H.A.M. Schols, 'De zekerheidsgerechtigde in het grensoverschrijdende WHOA-traject', *TvI* 2023/7, par. 4.2.2, Heidelberg-Luxembourg-Vienna report, no. 749; Balz 1996, p. 509; Moss, Fletcher, Isaacs, *Moss Fletcher and Isaacs on the EU Regulation in insolvency proceedings*, OUP 2016, at no. 6.145, R. Sheldon in R. Sheldon (ed.), *Cross-Border Insolvency* Bloomsbury 2015, p. 52.

32. Viewed in this light, the question whether cross-border secured claims can be crammed down in restructuring plans is a debate between precision in wording of art. 8 EIR, and an effective, material interpretation of that same art. 8 EIR. We will return to this after consideration of a new viewpoint, the new European Directive on Restructuring and Insolvency.

3. A new perspective: The Directive on Restructuring and Insolvency

3.1 Introduction

33. In 2019, nineteen years after the coming into being of the original Insolvency Regulation, and 24 years after the negotiations on the Convention on Insolvency Proceedings were concluded, the European Union took a leap forward in European insolvency law by enacting the Directive on Restructuring and Insolvency. This Directive aims (inter alia) to promote successful restructuring throughout the European Union, most importantly by requiring Member States to introduce restructuring plan proceedings.[63] Such plan proceedings must, so considers the Directive, allow debtors to change 'the composition, conditions or structure of their assets and their liabilities or *any other part of their capital structure*'.[64] This includes secured creditors.[65]

3.2 Relation between the Insolvency Regulation and the Directive on Restructuring and Insolvency

34. The Directive on Restructuring and Insolvency aims to be compatible with and complementary to the Insolvency Regulation.[66] This aim is largely achieved because these instruments mostly focus on different topics. The Directive on Restructuring and Insolvency requires Member States to enact restructuring proceedings, the Insolvency Regulation sets a private international law framework for insolvency proceedings, which also applies to many restructuring proceedings.[67]

63 Recital 1: "... this Directive aims to remove such obstacles by ensuring that: viable enterprises and entrepreneurs that are in financial difficulties have access to effective national preventive restructuring frameworks which enable them to continue operating..."

64 Recital 2.

65 Recital 37, 44, 55, art. 6 (2), art. 9 (4) Directive on Restructuring and Insolvency.

66 Recital 13.

67 Recital 10 and annex A EIR. As noted above the question which exact restructuring proceedings fall within the scope of the Insolvency Regulation is outside of the scope of this paper.

35. Yet, at the same time, the Directive on Restructuring and Insolvency marks a step from liquidation to restructuring.[68] This means that while the Insolvency Regulation primarily aims to facilitate processes focused on creditors realizing their rights, replacing individual recourse procedures only with collective ones because of the common pool problem of insolvency proceedings, the Directive on Restructuring and Insolvency sets a new step, prescribing restructuring proceedings not only aimed at realization of the rights of creditors, yet also at survival of the debtors business. This viewpoint of restructuring successful businesses legitimizes more interventions in the rights of recourse of individual creditors. As a consequence, the restructuring procedures envisioned in the Directive on Restructuring and Insolvency must, for example, include a moratorium that can bind all claims, also secured and preferred claims[69], include a temporary lifting of obligations to file for (other) insolvency proceedings[70], and have a mechanism to safeguard interim financing.[71] All such measures limit the powers of individual creditors to enforce their claims for the benefit of the restructuring, whereas in the liquidation paradigm that the Insolvency Regulation was mostly developed under, creditor rights are only limited insofar as necessary to ensure orderly collective liquidation.

36. This difference in approach also shows with regards to the position of the secured creditor. The Insolvency Regulation (in the prevailing hard and fast rule interpretation of art. 8) affords the secured creditor uninhibited powers of foreclosure, whilst the Directive on Restructuring and Insolvency allows for much more limits to be placed on the secured creditor, in order to promote the successful restructuring, whilst only allowing restructuring plans that are also in the best interest of the secured creditor.

3.3 Binding (secured) creditors to a restructuring plan

37. The restructuring plans envisioned by the Directive on Restructuring and Insolvency can bind secured creditors without their consent.[72] The Directive on Restructuring and Insolvency offers guidance as to the involvement of

68 Recital 4: "The trend favours approaches that, unlike the traditional approach of liquidating a business in financial difficulties, have the aim of restoring it to a healthy state or, at least, saving those of its units which are still economically viable."
69 Art. 6 (2) Directive on Restructuring and Insolvency.
70 Art. 7 Directive on Restructuring and Insolvency.
71 Art. 17 Directive on Restructuring and Insolvency.
72 Recital 2 & art. 15 Directive on Restructuring and Insolvency.

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secured creditors, for example by providing that the moratorium must also cover secured creditors.[73]

38. The possibility that restructuring plans bind creditors to a plan without their consent requires safeguards, also for secured creditors. The Directive on Restructuring and Insolvency recognizes this. It safeguards the interests of secured creditors not only with the safeguards provided for all creditors, but also contains specific provisions safeguarding the interests of secured creditors.

39. First, the Directive on Restructuring and Insolvency protects secured creditors by requiring that they be placed in a separate class.[74] In the voting system of modern restructuring proceedings this gives the secured creditors particular influence, as any plan opposed by a class of creditors can only be confirmed if it satisfies the extra requirements for cross-class cram-downs. Moreover, when the plan only affects a single secured creditor or when a secured creditor is in its own class for other reasons, that single secured creditor unilaterally determines whether this class of secured creditors votes in favor of the plan.

40. The Directive on Restructuring and Insolvency by itself does not prescribe whether secured creditors should be placed in a separate class for the entire nominal amount of the claim for which the security rights are vested, or whether the class composition should distinguish between the secured part of the claim and the unsecured part of the claim. This idea of *bifurcation* comes from Chapter 11. The Directive on Restructuring and Insolvency explicitly considers that Member States should be able to enact bifurcation.[75] Member States commonly do so.[76] Such 'bifurcation' of secured claims is underpinned by the notion that when a secured claim cannot be paid in full by foreclosure on the encumbered assets, then in fact the secured claim is only partially secured,

73 Art. 6 (2) Directive on Restructuring and Insolvency.
74 Art. 9 (4) Directive on Restructuring and Insolvency.
75 Recital 44.
76 See for example in Germany art. 24 StaRUG, and T. Pogoda & C. Thole, 'The new German "Stabilisation and Restructuring Framework for Businesses"', *EIRJ* 2021-6, Sweden: J. Schytzer, 'The Swedish Implementation of the EU Directive on Preventive Restructuring: Fewer but More Successful Restructurings?', *HERO* 2023/W-004 4.5.4, Denmark: L. Lankjaer, 'The PRD 2019 in Denmark: There is a First for Everything', *HERO* 2022/W-007, Austria: G. Wabl & M. Trenker, 'The Austrian Implementation of the PRD 2019: Game Changer or Missed Opportunity?', *HERO* 2022/W-005, par. 4.5.2, and under Dutch law art. 374 Dutch Bankruptcy Code.

that is, only to the amount that the secured creditor would be able to recover under his security right in a liquidation proceeding.[77]

41. Second, the Directive on Restructuring and Insolvency protects secured creditors through the requirement that a cross-class cram-down is only possible if a secured class or preferred class has approved the plan (unless the plan only binds out of the money creditors).[78]

42. Last, and most crucially, the Directive on Restructuring and Insolvency protects secured creditors through the best interest of creditors test. Just as any other creditor, secured creditors can only be bound to a restructuring plan (against their will) if under the plan they receive at least what they would receive without the plan.[79] For secured creditors, this means that they can block confirmation of the plan if under the plan they do not receive at least as much as they would be able to recover without the plan, by foreclosure of their security rights and pursuing possibly unsecured parts of their claim. This sets a threshold of value that each (secured) creditor must receive under the plan.

43. This best interest of creditors test also directly raises the question under what alternative scenario this threshold of value must be calculated, which in literature on the Scheme of Arrangement is known as the question of the correct comparator.[80] As restructuring plans are envisioned to be the alternative for liquidation proceedings, generally, the chosen comparator is liquidation in insolvency.[81] The best interest of creditors test for secured creditors therefore protects the value that they may realize in insolvency proceedings, such as through foreclosure on the assets that the security rights rest on. Hence, the best interest test safeguards that a secured creditor can only be bound to a restructuring plan if that creditor receives more than those proceeds of the security right that art. 8 EIR aims to protect.

77 § 506 U.S. Bankruptcy Code.
78 Art. 11 (1)(b) Directive on Restructuring and Insolvency.
79 Art. 10 (2-d) Directive on Restructuring and Insolvency.
80 Compare J. Payne, Schemes of arrangement – Theory, structure and operation, Cambridge: Cambridge University Press 2014, par. 2.3.2.2, C. Pilkington, Schemes of arrangement in corporate restructuring, London: Sweet & Maxwell 2013. par. 5.4.3.1.
81 One might argue the Directive on Restructuring and Insolvency requires this, see recital 49, yet compare recital 52.

44. The best interest test does not protect the nominal value of the secured claim, but it does protect the secured creditor from being put in a worse position than he would be in insolvency proceedings.[82] For secured claims, this means that in restructuring proceedings only that part of the claim is protected which is effectively secured in the sense that the creditor can take recourse for that part. In essence the best interest test protects the recoverable amount, because that is where the interest lies, not with the security right, or with the claim. The security right and in fact the claim itself are only means to the recoverable amount, that is the end.

45. In the best interest test, one can recognize the same principle that underlies bifurcation of secured claims: a secured creditor is not secured for the entire amount of the claim that the security is vested for, a secured claim is secured for the amount that the secured creditor can take recourse for on the encumbered assets.[83]

3.4 An even newer perspective: the proposal for Harmonisation of certain aspects of insolvency law

46. Further to this, inspiration may also be drawn from the newest European insolvency instrument *in statu nascendi*: the proposed Harmonisation Directive.[84] This instrument proposes, among other things, harmonized European rules on pre-pack proceedings, which are intended to promote going-concern sales in liquidation.[85] Going concern liquidations may be considered restructurings through asset-transactions. They allow the business or undertaking of the debtor to (at least partially) continue, albeit within a new corporate entity. The proposed Harmonization Directive aims to support such going-concern sales by, among many other things, providing that Member States may depart from ordinarily required consent from the secured creditor for sale of the encumbered assets that are necessary for the continuation of day to day operations of the business.[86] As a part of the going-concern sale, the insolvency practitioner may sell such assets without the secured creditors

82 Or, in any case, the alternative scenario to the plan, see recital 52 and art. 2 (1) sub 6 of the Directive on Restructuring and Insolvency.

83 Recital 44 of the Directive on Restructuring and Insolvency underpins this further by separating secured claims in secured and unsecured parts: "*It should be possible for Member States to provide that secured claims can be divided into secured and unsecured parts based on collateral valuation.*"

84 Proposal for a Directive of the European Parliament and of the Council, COM(2022) 702 final.

85 Recital 22 of the Proposal.

86 Art. 34 (4) Proposed Harmonisation Directive.

consent, unless – in short – the secured creditor proves that the sale does not meet the best interest of creditors test, or that a better offer is available.[87] Hence, in this context, the European legislator explicitly proposes to limit the rights of secured creditors in order to promote restructurings through asset transactions, and protect the secured creditors' interests with a best interest of creditors test.

4. Art. 8 Insolvency Regulation after the Directive on Restructuring and Insolvency

4.1 Introduction

47. A restructuring plan that aims to bind cross-border secured creditors can show a clear tension between the Directive on Restructuring and Insolvency and art. 8 EIR. As set out in the introduction, consider for example a Dutch WHOA procedure that involves a secured creditor with security rights over assets in other Member States. As the encumbered assets provide recourse for 75% of the secured claim, the proposed plan leaves this 75% unadjusted, but the remaining 25% of the claim, which is effectively unsecured, is largely waived.

48. This is precisely the kind of restructuring plan that the Directive on Restructuring and Insolvency aims for. It satisfies the best interest test and allows the debtor to continue its business after restructuring of its debts. However, because it involves a cross-border secured creditor such plan may be at odds with the hard and fast rule interpretation of art. 8 of the European Insolvency Regulation, and especially its corollary protecting the secured claim. If the hard and fast rule interpretation of art. 8 EIR is to be followed in international restructurings, in the sense that a cross-border secured creditor may not be imposed any haircut, this effectively creates a hold-out position for cross-border secured creditors. Other (secured) creditors may rightfully question whether the cross-border secured creditor should be left out of the restructuring based solely on the fact that the cross-border secured creditor has security rights in assets located outside of the Member State where the COMI of the debtor is located. Such holdout positions threaten the support for the restructuring among creditors.

87 Art. 34 (4) Proposed Harmonisation Directive.

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49. Moreover, restructuring laws are not just relevant for existing failing companies. If a cross-border secured creditor effectively has a holdout position in a restructuring proceeding, as he may have under the hard and fast rule corollary, then this may be used pro-actively by secured lenders to create holdout positions in future restructurings when structuring the financing and security rights. In this way, art. 8 EIR that was created to protect legitimate trust in security rights, is stretched far beyond its intended purpose. It creates security rights that are almost immune from restructuring for creditors that are well aware of the foreseeable location of the COMI in another Member State, and the insolvency law of all involved Member States.

50. In practice, the corollary of the hard and fast rule interpretation is regularly utilized by secured creditors to deliberately create hold-out positions.[88] The so called 'double Luxco' and 'double Dutchco'-structures are advertised by law firms as a way for a creditor to benefit from creditor-friendly insolvency regimes in Luxembourg or the Netherlands while financing underlying companies located in other European Member States where a secured creditor and particularly a share-pledge is less immune to insolvency proceedings.[89] This is done by placing the shares of the elsewhere located financed company in a Luxembourg or Dutch company, which is held by another Luxembourg or Dutch company, that pledges the shares in the first holding company to the lender. If these pledges secure claims against the primary debtor[90], then they are cross-border security rights, because the shares in the holdco are located in another Member State than the primary debtor. In that case, such structures use art. 8 EIR and the hard and fast rule interpretation to establish precisely the kind of hold-out positions that the Directive on Restructuring and Insolvency aims to undermine.[91] They are advertised as an effective means

88 See par. 4.1, Heidelberg-Luxembourg-Vienna report, par. 6.2.5.1.2.6.

89 See for example: https://www.loyensloeff.com/insights/news--events/news/creditor-friendly-structures-for-eu-leveraged-finance-transactions---new-york-office-snippet/#:~:text=The%20typical%20double%20holding%20structure,holding%20company%20(TopCo)%20that%20holds, https://paperjam.lu/article/comeback-of-the-double-luxco?utm_medium=email&utm_campaign=morning-2004&utm_content=morning-2004+CID_7d2316df4aeee13790f8d6f96e01825c&utm_source=Newsletter&utm_term=Comeback%20of%20the%20Double%20Luxco, https://remaress.com/en/double-luxco-structures/#:~:text=Double%20LuxCo%20means%20two%20Luxembourg,ease%20of%20execution%20to%20financiers.

90 If the financing is provided at the level of the top-holding, then this structure does not necessarily rely on art. 8 EIR, it just factually creates new debtors with new COMIs in Member States with more pledgee-friendly insolvency laws.

91 Recital 57 of the Directive on Restructuring and Insolvency.

of circumventing the insolvency law of other Member States, such as French insolvency law.[92]

51. The new viewpoints that the Directive on Restructuring and Insolvency provides suggest revisiting the interpretation of art. 8 EIR and its application in restructuring plans. The Directive on Restructuring and Insolvency clearly intends that all creditors can be bound to a restructuring plan, but has not considered the implications of this in cross-border context. The Insolvency Regulation on the other hand approaches the problem from a cross-border perspective, but focuses solely on the security right and not on the (restructuring of the) underlying debt.[93] This creates a tension between both instruments as the hard and fast rule corollary practically undermines the restructuring plans that the Directive on Restructuring and Insolvency aims for, such as the example given above.

52. Given this tension between the hard and fast rule interpretation corollary and the Directive on Restructuring and Insolvency it is worth to investigate further the relation between the Insolvency Regulation and the Directive on Restructuring and Insolvency (par. 4.2), and particularly the interpretation of art. 8 EIR in the light of the Directive on Restructuring and Insolvency (par. 4.3).

4.2 Relationship between the Directive on Restructuring and Insolvency and the Insolvency Regulation

53. As noted earlier, the Directive on Restructuring and Insolvency aims to be fully compatible with and complementary to the Insolvency Regulation.[94] But the two instruments have different objectives and nearly 25 years of shifting focus from liquidation to restructuring between them. Hence, it can hardly be surprising that these instruments do not blend seamlessly, begging the question how to approach conflicts between the two instruments. Such conflicts are not by virtue of one being a Regulation and the other being a Directive, because no formal hierarchy exists between these types of instruments as such.[95] That leaves two approaches.

92 Henri Wagner and François Guillaume de Liedekerke, Chapter on Luxembourg in: A. Nassiri, *The Lending and Secured Finance Review*, London: Law Business Research 2020.

93 See further par. 4.3.4. below.

94 Recital 13 of the Directive on Restructuring and Insolvency, see also par. 3.2 above.

95 P. Craig & G. De Búrca, *EU Law: tekst, cases and materials*, OUP 2020, p. 137 (https://doi.org/10.1093/he/9780198856641.003.0005): '*Regulations are not 'superior' to Directives, or vice versa*.'

54. On the one hand one may argue that since the Directive on Restructuring and Insolvency clearly states it is meant to be compatible with and complementary to the Insolvency Regulation, it cannot influence the Insolvency Regulation, and not even the interpretation thereof. The reasoning then is that the European legislator has communicated its intention not to encroach upon the Insolvency Regulation, so the Directive on Restructuring and Insolvency may not influence our thinking on the Insolvency Regulation.

55. On the other hand one may argue that the Directive on Restructuring and Insolvency is newer, and better represents the (current) position of the European lawmaker. If the Directive on Restructuring and Insolvency is to be implemented in line with its intended effect, it cannot be encumbered by an implied priority right for the Insolvency Regulation, just because that is older. Moreover, as the Directive on Restructuring and Insolvency reflects 25 years of shifting focus from liquidation to restructuring, one may argue that, akin to the living instrument doctrine applied to the European Convention on Human Rights[96], interpretation of the European Insolvency Regulation may also shift with the times, to reflect the developments in insolvency law. As the Directive on Restructuring and Insolvency represents progress in the thinking on insolvency law, interpretations of the Insolvency Regulation may proceed along with it.

56. Another viewpoint, which is in line with this latter approach, is to consider the Directive as more specific law than the Insolvency Regulation, and apply the common maxim '*lex specialis derogat legi generali*'. One could argue the Insolvency Regulation applies to all insolvency procedures, whereas the Directive is focused on restructuring proceedings, where this issue of the hard and fast rule and its corollary particularly arises. This suggests the rules of the Directive should take precedence, as the more specific law.

4.3 Four Approaches

57. This crossroads between the Insolvency Regulation and the Directive on Restructuring and Insolvency may be navigated with four different approaches.

96 Cf. K. Dzehtsiarou, "European Consensus and the Evolutive Interpretation of the European Convention on Human Rights" (2011) 12 German Law Journal 1730.

4.3.1 Hard and fast rule & corollary

58. The first possible approach is of course to stick to the interpretation of art. 8 EIR as a 'hard and fast' rule and its corollary that cross-border secured debt cannot be crammed down. Authors following this interpretation generally claim to stay close to the intended purpose of art. 8 EIR, as set out in the Virgós-Schmit report.[97] In this view art. 8 EIR means that the cross-border secured creditor cannot be negatively influenced by the foreign insolvency proceeding, thus no haircuts or moratoria can be imposed on the cross-border secured creditor. The stark consequences of this interpretation are then accepted based on the reported intent of the EIR-legislator, and one can almost hear these authors sigh '*lex dura, sed lex*'.[98]

59. An argument in favor of this approach is that the cross-border bonus, and its effects in restructuring were noted in the review of the European Insolvency Regulation that led to the current recast form of the Insolvency Regulation, but no amendments were made at this point.[99] The Heidelberg-Luxembourg-Vienna report proposed to amend the original art. 5 EIR to an 'opposition rule', in which the *lex concursus* would also apply to encumbered assets in other Member States, unless the secured creditor could prove that the (insolvency) law of the *lex rei sitae* would be more favorable to the secured creditor.[100] Along similar lines, Insol Europe proposed to amend art. 5 of the original EIR so that the *lex rei sitae* would govern the impact of insolvency proceedings on security rights.[101] However, the recast Insolvency Regulation does not differ from the original European Insolvency Regulation on this point. It only offers

97 Virgós-Schmit report at 97.

98 A maxim under Roman law, meaning 'The law is harsh but it is the law'. See for a review (and this position) the Heidelberg-Luxembourg-Vienna report, par. 6.2.5.2.2. Cf. McCormack & Bork 2017, at no. 83, Dirix & Sagaert 2001, par. 23, Struycken 2022, p. 256, Wessels & Madaus *Insolventierecht* X-II 2022/10658c, Veder & Kortmann 2000, p. 770, Van Galen 2021, no. 159, Veder 2004, p. 352-353, Veder & van Hees 2017, p. 192.

99 See for example Veder 2011, par. 26: "The approach taken in Article 5 (and 7) EIR should be seriously reconsidered. Article 5 EIR in fact allows secured creditors in a cross-border context to acquire a position that they have under no existing insolvency law. The 'excessive' protection now granted by Article 5 (and 7) EIR [current art. 8 and 10 of the revised EIR, NP] should be replaced by a more balanced approach. The option of applying the insolvency law of the Member State where the asset is located should be given serious consideration. Another option ...". I propose a different option, available under the current text of art. 8 EIR, that is to limit the interpretation of this article and bring it in line with the Directive on Restructuring and Insolvency, see below par. 4.3.3 and 4.3.4.

100 Heidelberg-Luxembourg-Vienna report, par. 6.2.6.

101 Insol Europe, *Revision of the European Insolvency Regulation - proposals by Insol Europe*, p. 50.

the solution of opening secondary insolvency proceedings, just as the original Insolvency Regulation did.[102]

60. Although it must be acknowledged that the hard and fast rule interpretation of art. 8 EIR in the context of restructuring plans would indeed promote secured lending in some way (by safeguarding the cross-border bonus) as the original drafters of the Convention on Insolvency Proceedings intended, it will at the same time disadvantage secured lending by complicating restructurings, and this interpretation also raises many questions, especially in the context of the Directive on Restructuring and Insolvency.

61. Firstly, that the European Insolvency Regulation not only aims to foster the granting of credit by safeguarding the interests of secured lenders, the Insolvency Regulation also explicitly aims to foster rescue-attempts. The stated aim of the Insolvency Regulation is "improving the efficiency and effectiveness of insolvency proceedings having cross-border effects", where 'insolvency proceedings' also includes restructuring plans.[103] In the context of restructuring plans with cross-border secured creditors the hard and fast rule interpretation can hardly be said to promote this stated aim of the Insolvency Regulation.

62. Secondly, the Directive on Restructuring and Insolvency also aims to foster credit, by reducing non-performing loans.[104] Also, it aims to foster cross-border markets for investors.[105] Hence, the Insolvency Regulation is not the only instrument that aims to promote financing. The Directive on Restructuring and Insolvency shares that objective, and creates restructuring options precisely to promote (cross-border) financing. Indeed, because of the best interest test a restructuring plan can only be confirmed if it also is in the interest of the secured creditor, promising greater returns than the alternative liquidation. Effective recovery may need a restructuring plan as foreseen in the Directive on Restructuring and Insolvency, and this may be impeded by the hard and fast rule corollary. As such, the implementation of the Directive on Restructuring and Insolvency is a fitting occasion to re-examine the interpretation of art. 8 EIR as a hard and fast rule.

102 Compare recital 68 of EIR Recast, and 25 of the original EIR.
103 Recital 8 and 10 of the Insolvency Regulation.
104 Recital 3 of the Directive on Restructuring and Insolvency.
105 Recital 12 of the Directive on Restructuring and Insolvency.

63. Thirdly, the problems with the hard and fast rule interpretation noted above still apply. Essentially, it gives the secured creditor an unnecessary 'cross-border bonus', strengthening his position far beyond what can be reasonably expected, both in terms of applicable law and of recovered economic value.

64. Fourthly, since the enactment of the Directive on Restructuring and Insolvency, one may question whether a secured creditor can legitimately expect never to be confronted with a (foreign) restructuring plan. He may face such a plan in a secondary proceeding. Insofar as a secured creditor would argue that he may indeed legitimately expect never to be confronted by any cram-down or infringement on his claim because of the hard and fast rule, then the hard and fast rule is based on a circular legitimacy: it exists, because secured creditors expect it to exist, because it exists.[106]

65. In this context, we will re-examine the hard and fast rule interpretation of art. 8 EIR. Paragraphs 4.3.3 and 4.3.4 consider alternative approaches, but first we will further examine the consequences of continuing the hard and fast rule interpretation after implementation of the Directive on Restructuring and Insolvency.

4.3.2 The hard and fast rule after implementation of the Directive on Restructuring and Insolvency

66. Full application of the hard and fast rule interpretation of art. 8 EIR and its corollary in conjunction with the Directive on Restructuring and Insolvency significantly complicates restructuring in cases with cross-border security rights. In effect, the restructuring debtor will have to choose between three poor options.

67. First, if local restructuring laws allow it, the debtor could choose to leave the cross-border secured creditor entirely outside of the restructuring. This will not be looked upon favorably by the other creditors that are to be bound by the restructuring plan. It may also not comply with the applicable priority rule, as creditors left out of the plan effectively receive full payment.

68. Second, the debtor may seek refuge in restructuring instruments that may not be considered insolvency proceedings under the Insolvency Regulation, such

106 See further above, par. 2.3.

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as the undisclosed[107] versions of the Dutch WHOA or the German StaRUG. The goal may then be to seek recognition of the restructuring plan under other instruments than the Insolvency Regulation and thus still bind the cross-border secured creditor to the plan. Whether this strategy will work remains to be seen. In any case, the essence of such strategy is to circumvent the Insolvency Regulation, because its rules prohibit an effective cross-border restructuring. This seems at odds with the stated goal of the Insolvency Regulation to enhance the effective administration of cross-border insolvency proceedings.[108]

69. Third, a debtor aiming to restructure under the Insolvency Regulation but confronted with cross-border security rights may start multiple simultaneous restructuring proceedings, one main proceeding in the Member State in which the center of main interests of the debtor lies, and secondary proceedings in each state where assets encumbered with cross-border security rights are located. This is the solution envisioned by the Insolvency Regulation, but it comes with its own complications.[109] The debtor then has to offer multiple simultaneous restructuring plans, one in each insolvency proceeding. Not only is this procedurally challenging, the division of proceeds both under the plan and the hypothetical alternative scenario of liquidation proceedings is severely complicated by the opening of secondary proceedings. Such an approach is hardly efficient, and it is what the introduction of the synthetic secondary proceeding in the recast of the Insolvency Regulation tried to prevent. Moreover, opening a secondary proceeding is not always possible, since the Insolvency Regulation requires for the opening of plan proceedings that the debtor has an establishment[110] and the mere presence of (encumbered) assets in a Member State does not necessarily amount to an establishment.[111]

70. At the same time, the possibility of secondary proceedings and infringement on security rights according to the *lex concursus* of secondary proceedings in the Member State in which the encumbered assets are located, shows that even the hard and fast rule interpretation cannot guarantee secured creditors that their claim is immune from insolvency law. As the Heidelberg-Luxemburg-Vienna report concludes:

107 These proceedings are not necessarily entirely secret, although they may be. They are undisclosed because they are not published in the insolvency register.
108 Recital 1 and 8 of the EIR.
109 Recital 68 EIR and Virgós-Schmit report, no. 98. See also Jol 2016, p. 82.
110 Recital 23 EIR.
111 Art. 2 sub 10 EIR.

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71. *"This example [setting up a so-called Double LuxCo structure, NP] clearly demonstrates that the protection the lenders seek is essentially not provided by the substantive restriction rule as a protection shield against any effects of insolvency proceedings, since the opening of secondary proceedings in the Member State in which the assets are situated has always to be taken in consideration."*[112]

72. All in all, application of the hard and fast rule after implementation of the Directive on Restructuring and Insolvency forces the debtor to either leave the secured creditor out of the restructuring, to circumvent the Insolvency Regulation, or to start parallel restructuring proceedings. The first approach leaves the cross-border secured creditor with precisely the hold-out position that the Directive on Restructuring and Insolvency aims to restrict, the last significantly complicates the restructuring process whilst applying largely harmonized rules in different proceedings, thus fostering rather than eliminating the complexity of cross-border security rights. In any case, the effects of art. 8 EIR in such cross-border restructurings can hardly be said to be in line with the policy goals of simplicity of application and legal certainty that underly the choice for art. 8 EIR.[113]

4.3.3 Amendment of the EIR

73. The fundamental conflict between the hard and fast rule interpretation of art. 8 EIR and its corollary and effective restructuring under the Directive on Restructuring and Insolvency would best be addressed by amendment of art. 8 EIR. Only a change in statutory law can offer the certainty that best serves (restructuring) practice on this important point.

74. This consideration *de lege ferenda* begs the question what alternative art. 8 EIR could or should be replaced with, and how that rule would play out in restructuring proceedings. The smallest possible adaptation that would resolve the issues with the cross-border bonus in restructuring proceedings would be to clarify that while art. 8 EIR protects the *rights in rem*, it does not protect the secured claim. One may argue that this is already the case under the current wording of art. 8 EIR[114], but in light of the regularly defended (corollary of the)

112 Heidelberg-Luxembourg-Vienna report, par. 6.2.5.1.2.6.
113 See par. 2.3 above.
114 As I will do in next paragraph.

hard and fast rule interpretation an amendment of art. 8 EIR would be able to provide clarification on this matter.

75. Alternatively, art. 8 EIR could be amended to become a conflict of laws rule. In the proposal of Insol Europe, the *lex rei sitae* would determine the effects of insolvency proceedings on security rights.[115] Similarly, the Heidelberg-Luxembourg-Vienna report proposed an 'opposition rule', in which the *lex concursus* would also apply to encumbered assets in other Member States, unless the secured creditor could prove that the (insolvency) law of the *lex rei sitae* would be more favorable to the secured creditor.[116]

76. Both approaches would simplify international restructuring proceedings somewhat. Since they do refer to the *lex rei sitae*, the restructuring debtor with encumbered assets outside the Member State where his center of main interests lies, would still have to take into account the national laws of where the assets are located. However, as the Directive on Restructuring and Insolvency orders all Member States to create restructuring proceedings that can bind secured creditors[117], the debtor may at least be certain that such would also be possible under the *lex rei sitae*. This approach would therefore be a big step forward.[118]

77. At the same time, such an approach of turning art. 8 EIR into a true conflict of laws rule would trigger the question which aspects of the restructuring are covered by the conflict of laws rule of art. 8 EIR, and which aspects are covered by the *lex concursus*. If art. 8 EIR were to be a conflict of laws rule guaranteeing the secured creditor the rights he is to have under the *lex rei sitae*, amidst the restructuring according to *lex concursus*, what rights would art. 8 EIR then protect? Of course art. 8 EIR would protect the best interest of creditors test in such a way that the secured creditor must in the restructuring plan at least receive payment on his claim equal to the amount he may obtain by foreclosure under *lex rei sitae*, but this already coincides with the best interest

115 Insol Europe, *Revision of the European Insolvency Regulation - proposals by Insol Europe*, p. 50. See also Veder 2011.

116 Heidelberg-Luxembourg-Vienna report, par. 6.2.6. See also Veder 2013. In Borks principled approach, the principles of predictability and efficiency at play in art. 8 EIR can best be satisfied with application of the *lex concursus*, see R. Bork, *Principles of cross-border insolvency law*, Cambride: Intersentia 2017, par. 6.23 et seq.

117 Recital 2.

118 Cf. Heidelberg-Luxembourg-Vienna report, par. 751.

test of the Directive on Restructuring and Insolvency.[119] However, an amended art. 8 EIR would be able to provide further clarity on the scope of the *lex rei sitae* exception. This could clarify whether such exception not only covers the right in rem, but also the secured claim. Moreover, it could, for example, clarify if the *lex rei sitae* also covers other aspects of the involvement of the secured creditor in the restructuring proceedings, such as a possible moratorium or differing rules for class formation. Or would such rules fall under the scope of the lex concursus, since that determines the restructuring plan proceedings?[120]

78. Hence, amendment of art. 8 EIR would provide the opportunity to take away the ambiguity in art. 8 EIR. It would however raise new questions, but those can also be answered in a possible amendment. Such amendment may take a long time to arrive, if at all. The next evaluation of the Insolvency Regulation is planned for June 2027[121], and postponing all restructurings involving cross-border secured debt until then is no feasible option. This begs the question what room the current text of art. 8 EIR provides.

4.3.4 A developing interpretation of art. 8 EIR

79. Given that statutory amendments of art. 8 EIR may not be enacted in the near future, it is also worthwhile to (re)consider the possibility of cramming down cross-border secured debt under the current instruments. That is, is there room for an interpretation under existing law that allows for cramming down cross-border secured debt in restructuring proceedings?

80. Taking all the above into account, it is submitted that after enactment of the Directive on Restructuring and Insolvency, the notion that claims of cross-border secured creditors cannot be amended by a restructuring plan because of the protection art. 8 EIR provides in its hard and fast rule interpretation & corollary is to be re-examined.

119 Compare Heidelberg-Luxembourg-Vienna report, par. 751.
120 See art. 7 (2) sub m EIR.
121 Art. 90 (1) EIR.

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81. As a starting point, we must note that this notion, albeit popular in literature, has little basis in the text of art. 8 EIR or the case law[122], whilst it makes two big steps in the interpretation of art. 8 EIR.

82. First, art. 8 EIR explicitly states that 'the opening of insolvency proceedings' shall not affect cross-border security rights. As noted earlier[123] the confirmation of a restructuring plan is not the opening but rather the closure of the insolvency proceedings.

83. Second, the notion that art. 8 EIR – in its hard and fast rule interpretation – prevents restructuring of cross-border secured debt takes a leap from protection of the security right to protection of the underlying debt. This leap, part of the corollary mentioned above, has been heavily criticized on dogmatic grounds in especially German literature.[124]

84. Proponents of this notion take this leap by arguing that the protection of the security right must of course be meant to serve the protection of the underlying secured claim, or in any case, that art. 8 EIR would be bereft of meaning if it did not also protect the secured claim.[125] They (sometimes implicitly) argue that a security right is only a means to an end – that is, satisfaction of the underlying claim. Art. 8 EIR is – in their mind – intended to protect the end, not just the means. But if this leap means that the secured claim cannot be affected at all by a restructuring plan it fails to recognize that a security right only (effectively) serves to protect a secured claim to the extent that the

122 In ECJ 16 April 2015, ECLI:EU:C:2015:227 (*Lutz/Bäuerle*) the Court does consider that the (original) Insolvency Regulation also serves to protect acts based on cross-border security rights after opening of the insolvency proceeding, but it does not consider the effects of the confirmation of a plan. See above par. 2.4.

123 Par. 2.4 above.

124 See inter alia MüKoBGB/Kindler, 8. Aufl. 2021, EuInsVO Art. 8 Rn. 23-25; Brünkmans/Thole, Handbuch Insolvenzplan
2. Auflage 2020 rn. 42 & 27,and Heidelberg-Luxembourg-Vienna report, par. 6.2.5.2.2 with extensive overview of German literature. Cf. in doubt: Isaacs in Moss, Fletcher, Isaacs, *Moss Fletcher and Isaacs on the EU Regulation in insolvency proceedings*, OUP 2016, at no. 6.136.

125 Moss, Fletcher, Isaacs, *Moss Fletcher and Isaacs on the EU Regulation in insolvency proceedings*, OUP 2016, at no. 6.145, Veder 2011 at par. 30, G. McCormack & R. Bork 2017, *Security rights and the European Insolvency Regulation*, p. 32; Heidelberg-Luxembourg-Vienna report, par. 6.2.5.2.2; P. Smart, 'Rights in rem, Article 5 and the EC Insolvency Regulation: an English perspective', *IIR* 2006/15, p. 33, Van den Broek & Schols, 'De zekerheidsgerechtigde in het grensoverschrijdende WHOA-traject', *TvI* 2023/7, Balz 1996, p. 509, Virgós & Garcimartín 2004, no. 163; Struycken 2022, who – however – also concludes with reference to van Galen 2021, nr. 161, that this means that within the European legal order opposite starting points co-exist.

secured creditor can take recourse for their claim on the encumbered assets. This realization is what prompts bifurcation in restructuring plans. Under the Directive on Restructuring and Insolvency no creditor can be worse off under a restructuring plan than without the plan, and this means that secured creditors must at least receive what they would be able to recover from their security rights without the plan. Yet, that is regularly not the entire amount of the secured claim. So the Directive on Restructuring and Insolvency considers that secured creditors are only entitled to protection insofar as their security rights effectively secure their claim. This consideration is not sufficiently recognized by the leap from the protection of security rights in art. 8 EIR to the immunity of the secured claim in its entire nominal amount.

85. The basis for both these steps from the text of art. 8 EIR to the immunity of cross-border secured claims lies in the (perceived) intention of the drafters of the predecessor of art. 8 EIR to protect cross-border secured creditors from insolvency laws that are foreign to them.[126] In the light of the policy aims as quoted above in par. 2.3., which do not mention complete immunity as a goal, this is a remarkably small and ever shrinking basis, especially as foreign insolvency laws become ever better known and the Directive on Restructuring and Insolvency compels all Member States to have similar restructuring procedures.

86. Moreover, the hard and fast rule interpretation of art. 8 EIR is not necessarily the best protection of the creditors, nor does the hard and fast rule interpretation have a monopoly on protecting the interest of secured creditors. The Directive on Restructuring and Insolvency aims to introduce restructuring plans explicitly in order to maximize the recourse that creditors, including other secured creditors, can receive.[127] Where that interest of all creditors requires cramming down secured creditors, that may very well be in the interest of other secured creditors. In any case secured creditors cannot be crammed down if they are not better off under the plan than in insolvency proceedings. The Directive on Restructuring and Insolvency, also weighing the interest of secured creditors, safeguards that interest in the best interest test, which ensures secured creditors must at least receive the recourse they may take in insolvency proceedings, not the nominal amount of their claim.

126 See par. 2.3 above.
127 Recital 2 of the Directive on Restructuring and Insolvency.

87. Insofar as the basis for the hard and fast rule interpretation of art. 8 EIR is its simplicity, in the sense that any other system may complicate international insolvency proceedings[128], that argument turns 180 degrees in restructuring plans involving cross-border secured creditors. Indeed, in such restructuring plans, it is precisely the hard and fast rule interpretation and its possible corollary that cross-border secured creditors must entirely be left out of the restructuring, that would in practice complicate restructuring proceedings. Such an interpretation effectively creates a holdout position for secured creditors that hinders restructuring proceedings which aim to maximize value for all creditors.

88. In light of all these considerations, the basis for the hard and fast rule interpretation of art. 8 EIR and the notion that it prevents any cramdown of cross-border secured debt is very limited. Therefore, even before enactment of the Directive on Restructuring and Insolvency, the hard and fast rule was controversial.[129] Since the enactment of the Directive on Restructuring and Insolvency there is all the more reason to reconsider the hard and fast rule interpretation, and it is submitted that the Directive on Restructuring and Insolvency should tip the scale where it regards the interpretation of art. 8 EIR and the possibility to cram-down cross-border secured debt in a restructuring plan. Instead, the Insolvency Regulation and the Directive on Restructuring and Insolvency should be reconciled by noting that art. 8 EIR protects the existence of the security right, but not the existence of the secured claim. That claim is protected by the best interests of creditors test as set out in the Directive on Restructuring and Insolvency, and in the context of that best interest of creditors test, the security right serves to secure for the secured creditor payment of at least that what he would be able to recover from his security rights during insolvency proceedings.

89. Such an interpretation would do justice to the development of the European insolvency framework. The hard and fast rule interpretation of art. 8 EIR stems from the background of the Insolvency Convention, the predecessor of the Insolvency Regulation that never came into being, in which, as a matter of policy,

128 See par. 2.3 above.

129 Wessels 2010, p. 349, Dirix & Sagaert 2001, p. 588; Snowden in Bork & van Zwieten, p. 282; Marshall 2011, Dirix & Sagaert 2001, McCormack & Bork 2017, p. 32, Insol Europe, *Revision of the European Insolvency Regulation - proposals by Insol Europe*, p. 50, Heidelberg-Luxembourg-Vienna report, par. 6.2.5; Kortmann & Veder 2000, p. 770, however also note Veder 2004 and Veder 2011 which are more supportive of the hard and fast rule.

secured creditors were to be protected from unknown foreign insolvency regimes. As noted earlier, not only has information of foreign insolvency regimes become much more accessible since then[130], more fundamentally, the Directive on Restructuring and Insolvency sets European standards for restructuring proceedings. In essence, since these proceedings are enacted all over Europe, cross-border secured creditors cannot be surprised by them, and instead they know that regardless of which restructuring regime they will be confronted with, it must comply with the best interest of creditors test. As long as the restructuring proceedings that take place in another Member State than where the encumbered assets lie conforms with the standards of the Directive on Restructuring and Insolvency, it cannot be said that secured creditors rights are infringed by foreign, unknown proceedings.

90. The best interest of creditors test, including the way it plays out for secured creditors, sets the European standard for the protection of individual creditors in the pursuit of the highest value for all creditors, which in restructurings may be realized by unlocking the reorganization value of the debtor's enterprise for recourse by the creditors. In doing so, the best interest test keenly focuses on the interest of the creditors as they take recourse in restructuring proceedings: the payment of their claim. Security rights also strive for payment, but security rights are only a means to that end. Where the hard and fast rule makes security rights immune from insolvency proceedings, and that interpretation is stretched to safeguard the secured claim in its nominal amount from insolvency proceedings, there that hard and fast rule interpretation distorts the means (the security right) to a new end (the continued existence of the claim itself). Only the recourse of the secured creditor is the interest of the creditor that deserves protection (which is granted by the best interest test), not the security right or the claim itself.

91. As noted above, with regards to the problem addressed here the Directive can be seen as a more specific law than the Insolvency Regulation. Hence, the interpretation suggested here is also in line with the principle of '*lex specialis derogat legi generali*'.

130 Both by the fast paced internationalisation of society through improved communication, and by the information mechanisms in the Directive on Restructuring and Insolvency and further in the proposed Harmonization Directive.

92. Such an interpretation that allows restructuring as long as the best interest test is met, is also supported by the goal of art. 8 EIR to protect legitimate expectations of secured creditors. Since enactment of the Directive on Restructuring and Insolvency, secured creditors can no longer legitimately expect that their claim is immune from restructuring proceedings.[131] The legitimate expectation of creditors should be to receive at least what they would receive in an insolvency proceeding. The best interest test protects that legitimate expectation.

93. Moreover, the cross-border bonus that art. 8 EIR creates for secured creditors was never a policy goal. The goal was to protect secured creditors from infringement on their security rights by insolvency proceedings in Member States where the encumbered assets are not located that go beyond what a secured creditor may expect to encounter in the Member State where the encumbered assets are located.[132] As noted, the legitimate expectations have been shifted by the Directive on Restructuring and Insolvency.

94. Further, while the cross-border bonus was never a policy goal of the Insolvency Regulation, the rescue of viable businesses was, and is.[133] Allowing for restructuring of cross-border secured debt, as long as the safeguards of the Directive on Restructuring and Insolvency – including the best interest test – are met, would not only be in line with the Directive on Restructuring and Insolvency[134], but can also be brought in line with the policy goals of the Insolvency Regulation.

95. In objection to the reasoning above, one might argue that the Directive on Restructuring and Insolvency cannot alter the correct interpretation of the European Insolvency Regulation. The argument would then be that the hard and fast rule interpretation and its corollary preventing restructuring of cross-border secured debt has always been the intention of the drafters of the Recast Insolvency Regulation and its predecessors, and that this cannot be

131 Moreover, such immunity was never the aim of (the predecessors of) art. 8 EIR; Virgós-Schmit report, par. 97, see also par. 2.3 above.

132 See Virgós-Schmit report, par. 96 and 97, and the quote thereof in par. 2.3 above.

133 As follows from recital 1 and 10. The EIR is meant to serve the effective administration of cross-border insolvency proceedings (recital 1), including those proceedings aimed at restructuring (recital 10). This is also confirmed by the extensive provisions on cooperation, the powers of the insolvency practitioner in the main proceedings to propose restructuring plans in secondary proceedings, and the abolishment of the requirement that secondary proceedings be liquidation proceedings.

134 See recital 1, 2, 3, 4, 13, 16, 21, 29, 65, 86 and 96 of the Directive on Restructuring and Insolvency.

changed by a later Directive.[135] However, it is submitted that this argument neglects that the hard and fast rule interpretation and especially its corollary on cramming down secured debt is not necessarily written into art. 8 EIR. The correct interpretation of art. 8 EIR has always been topic of debate, and whether art. 8 EIR does prevent cramming down of cross-border secured debt has never been determined by the European legislator or the European Court of Justice. Moreover, if interpretation of European statutes is about determining the intention of the European legislator[136], then why would the Directive on Restructuring and Insolvency as the more recent instrument, and specifically aimed at restructuring proceedings, not provide better insight in the legislators intention?[137]

96. Returning to the examples discussed in the introduction we can see that this interpretation where art. 8 EIR only protects the security right, and not the secured claim, brings a nuanced approach. The cross border secured creditor can take part in the plan proceedings, and in those proceedings invoke all the protection that the Directive, and the national implementation thereof, provide him. In the examples discussed, this means that the secured creditor must under the plan at least receive 75% of his claim as the amount that is covered by the security right, i.e. the amount that the secured creditor could recover by foreclosure on the security, plus the 1.25% of his claim that he would receive as payment on the remaining unsecured claim in liquidation proceedings. In total the bank would in liquidation receive 76.25%, and under the plan the bank receives 80%. This passes the best interest test. Hence, assuming the plan meets all other confirmation criteria, the bank could in this interpretation be bound by the plan. That means the remaining 20% of the claim can be crammed down. Hence after payment of the amounts offered under the plan, the bank has no remaining claim and can no longer foreclose on the encumbered assets.

97. This interpretation can be adopted under the current text of the European Insolvency Regulation. It does not require amendment of the law, although the clarity that an amendment of art. 8 EIR can bring is preferable. Practically the correct interpretation of art. 8 EIR is not likely to be found in the European Court of Justice as in restructuring proceedings it is incumbent to achieve

135 Cf. par. 4.2 above.
136 Which by itself is a debatable notion, but outside the topic of this paper.
137 Cf. par. 4.2 above.

certainty as quickly as possible. This leaves little incentive for litigation up to the European Court of Justice, although a national court may soon be called upon for a decision on this point. In large restructurings, parties will presumably rather opt for parallel secondary proceedings. Mainly for that reason, it is recommendable to clarify art. 8 EIR on this point.

5. Conclusion

98. The European Insolvency Regulation and the Directive on Restructuring and Insolvency are intended to work side by side in the European insolvency landscape, but some friction between the two is unavoidable. The Directive on Restructuring and Insolvency marks a change in European insolvency policy. It shifts the focus from matters of private international law to matters of substantive insolvency law, as well as shifting focus from liquidation to restructuring. This new focus challenges to rethink old debates. It shows that both legal and practical developments may challenge the assumptions underlying the familiar interpretations of long standing rules.

99. As international insolvency law develops, other legal systems become more accessible, Europe becomes increasingly connected, European instruments further develop insolvency laws in harmonized rules for restructuring proceedings, and insolvency law moves away from mere liquidation to a true rescue culture, the need for protection of a secured creditor against foreign unknown insolvency laws has diminished.

100. At the same time the Directive on Restructuring and Insolvency sets a new European common standard for restructuring proceedings. It creates a degree of uniformity, setting clear expectations for what foreign insolvency law might entail. Moreover, the Directive on Restructuring and Insolvency does that in order to promote restructurings which are in the interest of the creditors. Restructurings that would not be in the best interest of creditors are not permitted under the Directive on Restructuring and Insolvency.

101. This suggests that the Directive on Restructuring and Insolvency can provide new insight into an older debate on whether a restructuring plan can cram-down the claim of a cross-border secured creditor. In addition to older arguments about the scope of art. 8 EIR, and the leaps that have to be made in the interpretation that art. 8 EIR prevents a cram-down of cross-border secured debt, the Directive on Restructuring and Insolvency gives impetus to the interpretation that such cram-down is possible under existing law, and

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should be confirmed to be possible by amendment of art. 8 EIR in the future. The Directive on Restructuring and Insolvency clearly envisions restructuring proceedings that can bind secured creditors. Under the Directive on Restructuring and Insolvency cross-border secured creditors can count on the same protection as all other secured creditors, ensuring *inter alia* that they will under the restructuring receive at least what they would receive in liquidation, i.e. the value that they can obtain by foreclosure.[138] It is submitted that taking into account the developments since the drafting of the predecessors of art. 8 EIR, its interpretation should now not prevent a cram-down on the debt of a cross-border secured creditor that meets the best interest of creditors test. However, statutory clarification on this matter is preferable over the current uncertainty as to the interplay between art. 8 EIR and the Directive on Restructuring and Insolvency.

102. As European insolvency law moves from a focus on liquidation to restructuring, its development provides new insights into existing debates. The hard and fast rule interpretation and its corollary on limiting the secured claim is one such occasion. The Directive on Restructuring and Insolvency may thus not only bring new live to ailing companies, but also restructure existing debates on legal instruments struggling to adapt to new realities.

138 This is usually full payment of their claim, or at least the full liquidation value of the collateral, unless – as is the case in some Member States – other creditors can have a higher rank than the secured creditor.

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