

# European Insolvency Regulation

## 13. International aspects of consumer insolvency

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# Concept of consumer insolvency

- ▶ Traditional approach of bankruptcy law – intended for traders/entrepreneurs, as collective enforcement of debts → concentrated on creditor interest
- ▶ Problem of excessive indebtedness of natural persons („debt trap”):
  - puts the persons in question outside the scope of the formal economy → social exclusion, stigmatization, negative consequences for families
  - eliminates the debtors as consumers and taxpayers
  - surge of consumer debt in developed market economies

# Concept of consumer insolvency

- ▶ answer of (national) legislators: „fresh start” into life without debts
- ▶ Negative consequences of rigid and liberal approaches:
  - too rigid → see previous slide
  - too liberal → moral hazard (encouragement to run into more debt), increased risk for banks (and for depositors), increased cost of credit


# National consumer bankruptcy law

- ▶ different answers of national legislators
- ▶ usually some possibility of discharge of debts
  - within insolvency proceedings (or a specific type of insolvency proceedings), main role of the court: e.g. Germany, Poland
  - within separate (non-insolvency) proceedings, main role of specific administrative bodies created for this purpose: e.g. France, some of the earlier draft laws in Poland

# National consumer bankruptcy law

- ▶ varying extent of the discharge (some debts may be left unaffected; in some cases debts are not fully discharged but transformed into natural obligations)
- ▶ more or less stringent requirements for the opening of proceedings
  - lack of fault of the debtor at his own insolvency (concept of „deserving debtor”)
  - limitations as regards frequency of discharge (e.g. no more often than once in 10 years, once in a lifetime)
- ▶ diverse procedural approaches:
  - discharge on basis of a one-off decision
  - discharge only after a certain period under supervision/period of regular payments to the creditors (payment plans, „good behaviour period”)

# Consumer bankruptcy in Polish law

- ▶ Introduced in 2009 but initially barely used in practice because of stringent requirements (only 120 cases in 2009–2014)
  - ▶ Substantially reformed in 2014 to reduce barriers and improve access. New provisions entered into force on 31.12.2014.
  - ▶ From ca. 2100 cases in 2015 the number grew to 6500 in 2018 and continues to grow. In average 500 new cases are opened per month.
  - ▶ Consumer bankruptcy as a specific type of bankruptcy proceedings. After the distribution among creditors and conclusion of the proceedings a payment plan is adopted for up to 3 years. The debtor is discharged after the payment plan has been carried out.
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# Consumer insolvency under the EIR

- ▶ consumer bankruptcy proceedings are included in the EIR, provided they are listed in Annex A and an insolvency practitioner listed in Annex B is appointed.

Polish proceedings – under the old EIR until 31.12.2015 included as winding-up bankruptcy (*upadłość obejmująca likwidację*)

Reform of the Polish insolvency law – from 1.1.2016 *upadłość obejmująca likwidację* no longer applied → Annex A required amendment to list Polish proceedings under changed names.

The reformed Polish consumer bankruptcy is included only from 12 October 2016 as bankruptcy proceedings (*postępowanie upadłościowe*), listed in Annex A as amended by Regulation 2016/1792 amending Annexes to the old EIR. Annex A to the recast EIR has also been amended by Regulation 2017/353. From the date of application of the recast EIR (26 June 2017) amended Annex already applies and includes Polish proceedings.

A gap exists → Polish consumer bankruptcy proceedings opened between 1.1.2016 and 11.10.2016 were not covered by the old EIR

# Consumer insolvency under the EIR

German proceedings – included both under the old EIR and the recast EIR as *Insolvenzverfahren*

French proceedings – *procédure de rétablissement personnel* under the *Code de consommation* is NOT included in Annex A to the old EIR nor to the recast EIR → the EIR does not apply but „Brussels Ia” Regulation No. 1215/2012 may apply (but note that „bankruptcies... compositions and analogous proceedings” are excluded from the scope of „Brussels Ia”).

Swedish proceedings – *skuldsanering* was NOT included in Annex A to the old EIR → the EIR did not apply and „Brussels Ia” Regulation No. 1215/2012 did not apply, as the decision is not issued by a „court or tribunal” (→ see Radziejewski case below)

However, the *skuldsanering* IS included to Annex A of the recast EIR → the EIR applies from 26 June 2017 (cf. wider definition of „court” under Art. 2(6)(ii) of the recast EIR)



# COMI in consumer bankruptcy

- ▶ standard rules for natural persons apply – see Art. 3(1) EIR
- ▶ for debtors not conducting any business activity: habitual residence (→ cf. cases of Jan Kowalski in Słubice/Frankfurt in presentation 5)
- ▶ incentives for forum shopping → cf. ECJ in Case C-1 /04 (Staubitz-Schreiber)
- ▶ existence of specialized advisors arranging discharge in a selected jurisdiction
- ▶ Polish provisions on consumer bankruptcy in force since the 2014 reform in the context of forum shopping – is Poland likely to attract consumers intending to obtain discharge of their debts?

# Foreign income in consumer insolvency

- ▶ Case: Józef K, living in Poland and earning a minimum wage of ca. 1650 PLN at the time, applies for the opening of consumer bankruptcy proceedings in Poland. After the opening of proceedings he moves to Germany and finds a job there, earning approx. 1600 EUR per month.
- ▶ According to Polish law, half of income from an employment relationship but no less than the minimum wage, is free from attachment from enforcement proceedings (Art. 87(4) and Art. 87[1] of the Polish Labour Code). Consequently, that part of the debtor's income is exempt from the bankruptcy estate and should be left to the debtor (Art. 63(1)(2) BL).
- ▶ According to German law the minimum income protected from attachment (and exempt from insolvency estate) is ca. 1140 EUR

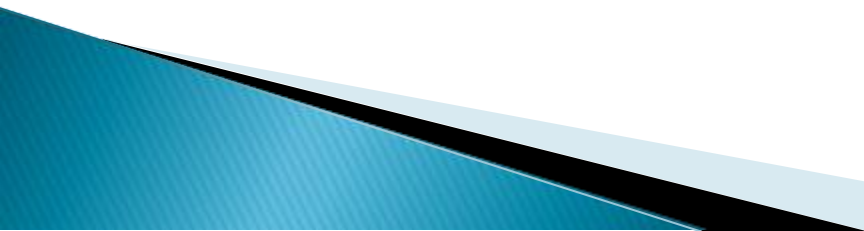
# Foreign income in consumer insolvency 2

- ▶ What part of Józef K.'s wages is exempt from the estate in Polish consumer bankruptcy proceedings if he works in Germany?
- ▶ Art. 7(2)(b) EIR – law of the state of the opening of proceedings (*lex fori concursus*) determines what assets are included in the insolvency estate --> Polish law
- ▶ Art. 63(1)(2) of Polish BL – the part of the debtor's income from employment which is not subject to attachment is also exempt from the bankruptcy estate.
- ▶ What is the meaning of "not subject to attachment" in this case --> under Polish law (*lex fori concursus*) or German law (*lex fori executionis*)?
- ▶ Polish law: Józef K. would be allowed to keep only 800 EUR per month
- ▶ German law: Józef K. would be allowed to keep ca. 1140 EUR per month

# Foreign income in consumer insolvency 3

- ▶ Economic argument for *lex fori executionis* – Józef K. works in Germany and should be allowed to keep the minimum enabling him to cover his living expenses in Germany. Otherwise he would have no motivation to look for a better-paying job in Germany which is beneficial for his creditors as it improves his ability to pay at least a part of his debts.
- ▶ Legal argument (upheld by the German Supreme Court (BGH) in a decision of 20.07.2017, Case IX ZB 63/16) – *lex fori concursus* should apply to the entire question.
- ▶ Practice of some Polish insolvency courts: a higher amount than allowed by Polish Labour Code is left to a debtor working abroad if justified by higher living expenses. Legal basis: Art. 152 BL (the judge-commissioner leads the course of bankruptcy proceedings). An explicit provision in this regard envisaged in a draft amendment law.

# Effectiveness of discharge in consumer bankruptcy under the EIR

- ▶ law of the State of the opening of proceedings applies to creditors' rights after the closure of proceedings (Art. 7(2)(k) EIR)
  - ▶ judgment on discharge is usually automatically recognized under Art. 32(1) EIR
  - ▶ such discharge applies and is effective for claims accross the EU even if the claims in question are not governed by the law of the State of opening of proceedings!
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# Effectiveness of discharge in proceedings outside the scope of the EIR

- ▶ what happens if the proceedings in question are not covered by the EIR (e.g. *procédure de rétablissement personnel* under the French *Code de consommation*)?
- ▶ Tentative answer:
  - discharge of debts is effective only under French law
  - discharge is effective abroad only for those claims which are governed by French law under general rules of private international law (as French law is applicable to determine whether the claim exists/has been extinguished)
  - discharge is not recognized in respect of claims governed by law of another jurisdiction (i.e. non-French), as that law will be applied to determine whether the claim exists and French proceedings are not recognised under the law in question
  - discharge may be recognized under separate provisions such as Brussels Ia Regulation (but Brussels Ia most probably does not apply because of exclusion of bankruptcies and similar proceedings)

# Example 1

Herbert H. lived near Opole, Poland. In 2007 he divorced his wife Bożena H. Custody of their 2 children (born 2003 and 2006) was awarded to Ms. H. The court also awarded her and the children alimony payments of 3000 PLN per month.

In 2008 Mr H. moved to Germany. His alimony payments were irregular. Altogether in 2015 he owed more than 50.000 PLN in unpaid alimony. In August 2010 Mr H. requested the opening of insolvency proceedings in Germany and applied for a discharge of his debts. Following a „good behaviour period”, the German court granted him discharge in 2016. According to German law, no exception is provided for alimony claims, which are fully discharged in consumer insolvency proceedings.

Can Ms H. claim unpaid alimony from Mr H. before a Polish court?

# Practical example – CJEU in Case C-461 / 11

## Ulf Kazimierz Radziejewski

- ▶ CJEU judgment of 8 November 2012, Case C-461 / 11, Ulf Kazimierz Radziejewski
- ▶ Facts in the case:
  - Mr Radziejewski is a Swedish national, residing and working in Belgium since 2001, employed there by a Swedish employer
  - he had substantial debts in Sweden dating prior to 1996. From 1997 he was subject to earnings attachment order in Sweden.
  - In 2011 Mr Radziejewski applied to KFM (a Swedish administrative body competent for consumer insolvency) for debt relief in *skuldsanering* proceedings. KFM rejected the application on 29 June 2011 based on the fact that the applicant was not resident in Sweden. Under Swedish law at the time, residency in Sweden was a condition for debt relief.
  - Mr Radziejewski appealed against the rejection on the grounds that the requirement of residency in Sweden is contrary to the freedom of movement for workers in the EU → reference to the CJEU



# Practical example – CJEU in Case C-461/11

## Ulf Kazimierz Radziejewski

- ▶ *Skuldsanering*, Swedish debt relief proceedings – not listed in Annex A at the time and without divestment of the debtor → the old EIR did not apply
- ▶ Based on decision of an administrative authority, which cannot be considered „court or tribunal” in the meaning of Article 32 of the „Brussels I” Regulation No 44/2001 [similarly currently under Art. 2(a) of „Brussels Ia” Regulation No. 1215/2012] → „Brussels I” Regulation does not apply
- ▶ EU law at the time did not oblige Member States to recognize Swedish debt relief
- ▶ A requirement of Swedish law that the debtor resides in Sweden to obtain debt relief is an unlawful restriction of the freedom of movement, prohibited by Article 45 TFEU, as it precludes or deters a national of a Member State from leaving his country of origin in order to exercise his right to freedom of movement → by moving out of the country the debtor would be denied the possibility of debt relief in Sweden

# Case C-461 / 11 – subsequent changes in the recast EIR

- ▶ the *skuldsanering* is added to the list of proceedings in Annex A
- ▶ The definition of „court” includes also non-judicial bodies empowered to open insolvency proceedings, to confirm such opening or to take decisions in the course of such proceedings (Art. 2(6)(ii) EIR-r)
- ▶ wider definition of „insolvency proceedings” in Art. 1(1) EIR-r → inclusion of proceedings with „debtor-in-possession” schemes

# Example 2

- ▶ Sven D. lives near Lund, Sweden. He had substantial debts from a period in the past (2010–2013) when he lived in Rome, Italy, for 3 years. Claims of Italian creditors against Sven D. from that period were governed by Italian law. Sven D. had also some debts to Swedish creditors governed by Swedish law.
- ▶ in June 2014 Sven D. applied for the *skuldsanering* (the same proceedings as in the Radziejewski case). In result of the proceedings a decision on discharge of his debts was issued on 4.4.2015.
- ▶ What are the effects of the decision on discharge?
  - in relation to claims governed by Swedish law?
  - in relation to claims governed by Italian law?
  - in Sweden?
  - in Italy?
- ▶ What would be the situation if he applied for the *skuldsanering* in August 2017?

# Secondary proceedings in consumer cases?

- ▶ not excluded in theory, but an exception in practice:
- ▶ Secondary proceedings are possible only where the establishment of the debtor is situated (Art. 3(2) EIR), defined as place of operations where the debtor carries out a non-transitory economic activity with human means and assets (Art. 2(10) EIR)
  - „economic activity” is understood in a broad manner, not necessarily as business or commercial activity (non-profit activities are also included),
  - „human means and assets” – requires a minimum degree of organisation, including hiring persons for whom the debtor is responsible as employer or principal → usually done in the context of a business activity
  - example of a construction site belonging to the debtor and managed by him

# Special rules for consumer proceedings under the recast EIR

- ▶ related to the envisaged interconnection of insolvency registers
- ▶ intended to protect personal data of individuals not exercising an independent business or professional activity
- ▶ possibility for Member States to opt out of compulsory publication of information on consumer bankruptcy in on-line insolvency registers or of making them available through the system of interconnection of insolvency registers (Art. 25(4) EIR), subject to two limitations:
  - known foreign creditors need to be informed individually pursuant to Art. 54;
  - foreign creditors not informed individually will not be affected by insolvency proceedings (including by the discharge).
- ▶ if provided via interconnected registers, the access to information on consumer bankruptcy may additionally be restricted:
  - by additional search criteria (Art. 27(3))
  - by making it available only on request of a competent authority or only for those demonstrating legitimate interest in obtaining such information (Art. 27(4))