

COMI Shifts in Europe – New Developments

Final decision in the Galapagos case brings clarity on the recognition and effects of COMI shifts

23 February 2023

Contact

Dr. Mathias Eisen,
Partner
+49 69.71914.3434
meisen@milbank.com

Yushan Ng,
Partner
+44 20.7615.3341
yng@milbank.com

Karen McMaster,
Partner
+44 20.7615.3266
kmcmaster@milbank.com

Robert Kastl,
Associate
+49 69.71914.3438
rkastl@milbank.com

At a glance – Key takeaways

With its decision to dismiss the appeal against the commencement of insolvency proceedings in Germany, the German Federal Court of Justice¹ finally concluded the legal dispute over the centre of main interest ("**COMI**") of Galapagos S.A. and thus the correct forum for insolvency proceedings over its assets. This judgment followed the decision of the European Court of Justice² ("**ECJ**") on certain questions on the interpretation of the European Insolvency Regulation referred to the ECJ by the German Federal Court of Justice³.

The verdicts of the ECJ and the German Federal Court of Justice are highly relevant as they clarify the recognition and effects of COMI shifts:

- COMI shifts are permissible and can be recognised.
- There is no minimum residency period required to establish the COMI in another jurisdiction.
- It is possible to COMI-shift a pure holding company.
- Any insolvency petition filed with a court of a Member State⁴ blocks the jurisdiction of courts of other Member States to institute insolvency proceedings without any exceptions. This is a material deviation from the previous application of the European Insolvency Regulation pursuant to which only actual orders for the institution of insolvency proceedings had such blocking effect.
- Insolvency petitions filed in Third States⁵ will not block the institution of insolvency proceedings in Germany. Only actual orders for the institution of insolvency proceedings by a Third State authority of competent jurisdiction (to be determined by autonomous German insolvency law and subject to full judicial review by German courts) are to be recognised in Germany.

¹ Decision of the German Federal Court of Justice dated 8 December 2022, docket no. IX ZB 72/19.

² Decision of the European Court of Justice dated 24 March 2022, docket no. C-723/20.

³ Decision of the German Federal Court of Justice dated 17 December 2020, docket no. IX ZB 72/19.

⁴ Member states of the EU other than Denmark, the "**Member States**".

⁵ Non-EU member states including the United Kingdom following Brexit and Denmark, the "**Third States**".

Background – The COMI dispute in the Galapagos case

The facts and history of the case

The Galapagos COMI dispute unfolded in 2019. Galapagos S.A. was the holding company of the Galapagos group, a provider of heat exchanger solutions, and acted as its financing and acquisition vehicle. Galapagos' financing structure mainly consisted of credit and guarantee facilities, senior secured notes (SSN) and senior unsecured notes (SUN).

The dispute over the COMI of Galapagos S.A. emerged when Galapagos S.A. attempted to shift its COMI from Luxembourg to England and applied for administration proceedings at the English High Court to implement a non-consensual restructuring. Certain SUN holders then enforced a share pledge over Galapagos S.A. and replaced the management of Galapagos S.A. The newly appointed management then immediately established the head office of Galapagos S.A. in Düsseldorf/Germany and withdrew the insolvency petition pending with the English High Court. This insolvency petition was then converted into a creditor petition by certain SSN holders, who continued the petition at the English High Court. SUN holders then filed an insolvency petition in Germany, and the local court of Düsseldorf concluded, after having taken evidence, that the COMI had been validly shifted to Germany and thus confirmed its jurisdiction and instituted insolvency proceedings. The English High Court, however, did not decide on the converted creditor-initiated insolvency petition until 2022.

The institution of German insolvency proceedings was then challenged. The Regional Court of Düsseldorf dismissed the challenge as unfounded but allowed the challenge to proceed to the German Federal Court of Justice.

The legal questions

The European Insolvency Regulation stipulates that COMI is the place where the debtor conducts the administration of its interests on a regular basis, and which is ascertainable by third parties. Various jurisprudence of the ECJ has refined the principles for determining the COMI over the last decades.

However, neither the effect of competing insolvency petitions nor the exact requirements for establishing the COMI of holding companies were yet subject to the jurisprudence of the ECJ or the German Federal Court of Justice.

In addition, the recast version of the European Insolvency Regulation, which came into force on 26 June 2017, expressly sets out the objective of preventing forum shopping and defines it as the transfer of assets or judicial proceedings from one Member State to another, seeking to obtain a more favorable legal position to the detriment of the general body of creditors. It was, however, unclear if this legislative objective implied restrictions which went beyond those specifically set out in the recast European Insolvency Regulation. The recast European Insolvency Regulation neither expressly prohibits COMI shifts nor requires a certain minimum residency period.⁶

Consequently, when called to adjudicate on the challenge against the institution of insolvency proceedings in Germany, the German Federal Court of Justice decided to refer certain questions on the interpretation of the European Insolvency Regulation to the ECJ. Essentially, the ECJ was asked by the German Federal Court of Justice in late 2020, i.e., prior to the expiry of the transition period for the withdrawal of the United Kingdom from the EU ("Brexit") on 31 December 2020, if:

- (i) the insolvency petition pending with the court of a Member State (i.e. England) precluded a shift of the COMI to, and thus the establishment of jurisdiction of, another Member State, and

⁶ In the course of the legislative process to amend the predecessor version of the European Insolvency Regulation, certain proposals to expressly restrict COMI shifts such as a minimum residency period and denial of recognition of abusive COMI shifts were discussed, but not reflected in the wording of the now applicable recast version of the European Insolvency Regulation, cf. EU Parliament, Committee on Legal Affairs, Report on the proposal for a regulation of the European Parliament and of the Council amending Council Regulation (EC) No. 1346/2000 on insolvency proceedings, 20 December 2013, A7-0481/2013, Amendment 27 and EU Council, Proposal for a Regulation of the European Parliament and of the Council amending Council Regulation (EC) No. 1346/2000 on insolvency proceedings – Proposals from the delegations of the Netherlands, Germany and Spain on abusive COMI-transfers, 10 June 2014, 10306/14, S. 3, respectively.

- (ii) if the courts of the exit state retained jurisdiction to decide on a pending insolvency petition following such COMI shift and if such jurisdiction was exclusive and precluded the jurisdiction of the courts of the destination state into which COMI was shifted.

The ECJ and German Federal Court of Justice decisions

ECJ: Blocking effect of insolvency petitions pending with the court of a Member State

In a previous decision, the ECJ had ruled that the courts of the exit state retain jurisdiction where COMI is shifted after the filing of an insolvency petition.⁷ The ECJ remained silent on the question whether such retained jurisdiction is an exclusive one which precludes the jurisdiction of the courts of the destination state. The prevailing view in German legal literature was that the courts of the exit state retained only non-exclusive jurisdiction, competing with the jurisdiction of the courts of the destination state. According to this view, any conflicts of jurisdiction would have been solved by the principle of priority of decisions, i.e., any decision instituting insolvency proceedings by the first court would have had to be recognised by other courts and precluded them from instituting competing insolvency proceedings.

In the Galapagos decision, the ECJ ruled that a court of a Member State with which an insolvency petition has been filed retains exclusive jurisdiction to institute insolvency proceedings even if the debtor's COMI has been shifted to another Member State after the filing of the insolvency petition with such court, but before such court (with which the insolvency petition has been filed) has delivered a decision on such petition. Consequently, courts of other Member States are precluded from instituting insolvency proceedings until the first court has delivered its decision and declined jurisdiction.

On this basis, the ECJ determined that the German courts initially did not have jurisdiction to institute insolvency proceedings over Galapagos S.A. since a prior insolvency petition, i.e., the creditor-converted petition, had been filed with the English High Court. This prior English petition awarded exclusive jurisdiction to the English High Court and therefore blocked the international jurisdiction of the German courts, despite COMI of Galapagos S.A. having been in Düsseldorf/Germany at the relevant time. However, the ECJ also determined that the blocking effect of such English petition ceased upon the end of the Brexit transition period on 31 December 2020, when the European Insolvency Regulation ceased to apply in relation to the United Kingdom, unless an actual order for the institution of insolvency proceedings had been issued by an English court.

The ECJ assumed that a COMI shift to Germany, which was capable of establishing the jurisdiction of the German courts once the blocking effect of the insolvency petition pending with the English High Court fell away, took place prior to the insolvency filing in Germany. Since no order for the institution of insolvency proceedings had been issued by the English High Court on or before 31 December 2020, the creditor-converted English petition ceased to block jurisdiction of the German courts.

German Federal Court of Justice: No blocking effect of insolvency petitions pending with the court of a Third State

Based on the referral decision by the ECJ, the German Federal Court of Justice ruled that the assessment of the German courts that the debtor's COMI had been validly shifted to Germany had been accurate and that the German courts did have international jurisdiction once the blocking effect of the English insolvency petition fell away upon the end of the Brexit transition period. As the English High Court had instituted insolvency proceedings only in 2022, i.e., after the end of the Brexit transition period, these insolvency proceedings are also not capable of precluding the jurisdiction of the German courts.

The German Federal Court of Justice then examined international jurisdiction under autonomous German insolvency law which applied in this case since the end of the Brexit transition period (see above). It concluded that insolvency petitions pending in Third States (i.e., where the European Insolvency Regulation does not apply) are not capable of blocking the jurisdiction of German courts.

Consequently, any insolvency proceedings instituted by a German court take precedence over Third State insolvency proceedings. Such Third State insolvency proceedings will not be recognised in Germany. This

⁷ Decision of the European Court of Justice dated 17 January 2006, docket no. C-1/04 (*Staubitz-Schreiber*).

principle applies even if the insolvency petition was filed with the Third State court before any petition is filed with the German court, and if the Third State court had jurisdiction pursuant to autonomous German insolvency law at the time the insolvency petition was filed with it. Consequently, the English insolvency proceedings will not be recognised in Germany as the English High Court instituted these only after the German insolvency proceedings were instituted.

What the decisions mean in practice

Recognition of COMI shifts

- The decisions of the ECJ and the German Federal Court of Justice implicitly confirm that COMI shifts are possible and can be recognised.
- While the European Insolvency Regulation explicitly aims at preventing abusive forum shopping and includes certain safeguards in this respect, it does not impose any additional requirements on the establishment of COMI and thus the applicable forum for insolvency proceedings.
- COMI can in principle be established, and award jurisdiction for the institution of insolvency proceedings, from day one, i.e., there is no minimum residency or look-back period.

Determination of COMI of holding companies

- Not only operative companies, but also holding companies can shift their COMI to another jurisdiction. This is especially relevant for acquisition and financing SPVs which intend to restructure their financial liabilities in a certain forum.
- Holding companies have a narrower range of activities, so visibility of the location of such activities to creditors of the holding company is limited from the outset. However, this does not require the holding company to take any additional measures or unfold any specific activities to establish its COMI in a different jurisdiction. Especially, the activities carried out at the new COMI do not need to go beyond the activities carried out at the previous COMI.
- In Galapagos, the COMI shift was recognised on the basis that an office for the management, which was visible for third parties, was established in the destination jurisdiction. In addition, the company notified its creditors via an ad-hoc release of its new postal address and that its head office, principal place of business and effective place of management had been relocated to Germany.

Blocking power of insolvency petitions

- Insolvency petitions filed with a court of a Member State prevent the opening of insolvency proceedings and the ordering of safeguarding measures to protect the debtor's assets in other Member States.
- This applies even if the relevant Member State court with which the petition has been filed does not have jurisdiction. Any jurisdictional challenge would need to be filed in the relevant Member State in which the insolvency petition is pending.
- It remains to be seen how courts will deal with this new jurisprudence in practice, especially since there is no public register of pending insolvency petitions. Only orders for the institution of insolvency proceedings need to be published by the Member States.
- It also remains to be seen if courts lacking jurisdiction dismiss insolvency petitions quick enough to reduce the risk of creditors or companies making filings aimed at preventing the commencement of insolvency and/or restructuring proceedings by the competent courts.

Practice/Group Contacts

Frankfurt | Neue Mainzer Straße 74, 60311 Frankfurt/Main
London | 100 Liverpool Street, London EC2M 2AT

Dr. Mathias Eisen	meisen@milbank.com	+49 69.71914.3434
Yushan Ng	yng@milbank.com	+44 20.7615.3241
Karen McMaster	kmcmaster@milbank.com	+44 20.7615.3266
Robert Kastl	rkastl@milbank.com	+49 69.71914.3438

Please feel free to discuss any aspects of this Client Alert with your regular Milbank contacts or any member of our Financial Restructuring Group.

This Client Alert is a source of general information for clients and friends of Milbank LLP. Its content should not be construed as legal advice, and readers should not act upon the information in this Client Alert without consulting counsel.

© 2023 Milbank LLP

All rights reserved. Attorney Advertising. Prior results do not guarantee a similar outcome.