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Report of Working Group V (Insolvency Law) on the work of its thirty-fourth session (New York, 3-7 March 2008)

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I. Introduction

1. At its thirty-ninth session, in 2006, the Commission agreed that the topic of the treatment of corporate groups in insolvency was sufficiently developed for referral to Working Group V (Insolvency Law) for consideration in 2006 and that the Working Group should be given the flexibility to make appropriate recommendations to the Commission regarding the scope of its future work and the form it should take, depending upon the substance of the proposed solutions to the problems the Working Group would identify under that topic.

2. The Working Group agreed at its thirty-first session, held in Vienna from 11 to 15 December 2006, that the UNCITRAL Legislative Guide on Insolvency Law (the Legislative Guide) and the UNCITRAL Model Law on Cross Border Insolvency (the Model Law) provided a sound basis for the unification of insolvency law, and that the current work was intended to complement those texts, not to replace them (see A/CN.9/618, para. 69). A possible method of work would entail the consideration of those provisions contained in existing texts that might be relevant in the context of corporate groups and the identification of those issues that required additional discussion and the preparation of additional recommendations. Other issues, although relevant to corporate groups, could be treated in the same manner as in the Legislative Guide and Model Law. It was also suggested that the possible outcome of that work might be in the form of legislative recommendations supported by a discussion of the underlying policy consideration (see A/CN.9/618, para. 70).

3. The Working Group continued its consideration of the treatment of corporate groups in insolvency at its thirty-second session in May 2007, on the basis of notes by the secretariat covering both domestic and international treatment of corporate groups (A/CN.9/WG.V/WP.76 and Add.1). For lack of time, the Working Group did not discuss the international treatment of corporate groups contained in document A/CN.9/WG.V/WP.76/Add.2.

4. At its thirty-third session in November 2007, the Working Group continued its discussion of the treatment of enterprise groups, previously referred to as corporate groups, in insolvency, on the basis of notes by the secretariat covering domestic treatment of enterprise groups (A/CN.9/WG.V/WP.78 and Add.1). Following a preliminary discussion of the timing of its consideration of international issues relating to the treatment of enterprise groups in insolvency, the Working Group decided to consider those issues at its thirty-fourth session in March 2008.

II. Organization of the session

5. Working Group V (Insolvency Law), which was composed of all States members of the Commission, held its thirty-fourth session in New York from 3 to 7 March 2008. The session was attended by representatives of the following States members of the Working Group: Australia, Belarus, Benin, Cameroon, Canada, Chile, China, Czech Republic, El Salvador, Fiji, France, Germany, Guatemala, India, Iran (Islamic Republic of), Italy, Japan, Kenya, Latvia, Madagascar, Malaysia, Mexico, Mongolia, Nigeria, Norway, Pakistan, Paraguay, Poland, Republic of Korea, Russian Federation, Senegal, Singapore, South Africa, Spain,

Switzerland, Thailand, Uganda, United Kingdom of Great Britain and Northern Ireland, United States of America, and Venezuela (Bolivarian Republic of).

6. The session was also attended by observers from the following States: Belgium, Croatia, Denmark, Holy See, Ireland, Mali, Mauritania, Netherlands, Peru, Romania, Slovenia, Trinidad and Tobago, and Turkey.

7. The session was also attended by observers from the following international organizations:

(a) **Organizations of the United Nations system**: the World Bank;

(b) **Intergovernmental organizations**: Asian-African Legal Consultative Organization (AALCO), Council of the Interparliamentary Assembly of Member Nations of the Commonwealth of Independent States (CIS), European Commission (EC), International Association of Insolvency Regulators (IAIR);

(c) **International non-governmental organizations invited by the Working Group**: American Bar Association (ABA), American Bar Foundation (ABF), Asian Clearing Union (ACU), Commercial Finance Association (CFA), INSOL International (INSOL), International Bar Association (IBA), International Credit Insurance and Surety Association (ICISA), International Insolvency Institute (III), International Women's Insolvency & Restructuring Confederation (IWIRC), International Working Group on European Insolvency Law (IWGEIL), and National Law Center for Inter-American Free Trade (NLCIAFT).

8. The Working Group elected the following officers:

Chairman: Mr. Wisit Wisitsora-At (Thailand)

Rapporteur: Mr. Rodrigo Rodriguez (Switzerland)

9. The Working Group had before it the following documents:

(a) Annotated provisional agenda (A/CN.9/WG.V/WP.79); and

(b) A note by the secretariat on the treatment of enterprise groups in insolvency (A/CN.9/WG.V/WP.80 and Add.1).

10. The Working Group adopted the following agenda:

1. Opening of the session;
2. Election of officers;
3. Adoption of the agenda;
4. Consideration of the treatment of enterprise groups in insolvency;
5. Other business;
6. Adoption of the report.

III. Deliberations and decisions

11. The Working Group continued its discussion of the treatment of enterprise groups in insolvency on the basis of documents A/CN.9/WG.V/WP.80 and Add.1,

and other documents referred therein. The deliberations and decisions of the Working Group on this topic are reflected below.

IV. Treatment of enterprise groups in insolvency

A. Glossary

12. The Working Group considered the glossary on the basis of document A/CN.9/WG.V/WP.80.

General remarks

13. It was noted that the function of the glossary should not be to provide statutory definitions of the relevant terms, but rather to provide readers with a general idea of how the concepts were used. The Working Group was reminded that the terms included in the glossary could be used in various ways for a range of purposes, including in the insolvency law context, and that different jurisdictions could have different viewpoints on those terms. It was suggested that the explanation of the terms in the glossary should be drafted as simply as possible and that related policy issues and relevant examples should be addressed in the commentary or the explanatory note to those terms. After discussion, the Working Group agreed that an introductory section similar to that found in paragraph 6 of the glossary section of the Legislative Guide should be included to inform readers of the purpose of the glossary along with an explanatory note that would provide more detailed information about the policies underlying the individual terms.

(a) Enterprise group

14. A proposal to delete the reference to incorporation on the basis that it was addressed in the explanation of "enterprise" was supported.

15. A further proposal to delete the reference to capital and to substitute the notion of ownership was also supported. It was noted that capital was an example of what might lead to control and it was control that should be the focus of the explanation. In response, a view was expressed that reference to "ownership" should not be used in the explanation of the term "enterprise group" as the concept of "ownership" was just one of the methods of obtaining "control" and should not be a separate criterion.

16. Several proposals were made to revise the draft explanation. Those included that an enterprise group could be (a) two or more enterprises that were connected because they were subject to full or partial ownership or control; (b) two or more enterprises that constituted related persons pursuant to paragraph (jj) of the glossary of the Legislative Guide; or (c) two or more enterprises that could be subject to insolvency proceedings (as indicated in the second sentence of footnote 1 to the explanation of "enterprise") and were linked by factors such as significant capital participation and unity of management.

17. After discussion, the Working Group agreed that the term enterprise group should be explained as two or more enterprises that were bound together by means of ownership or control and that the reference to "capital" should be deleted.

(b) Enterprise

18. Proposals made to revise the explanation included: limiting the reference to economic activities to those that were conducted for profit; replacing the word “entity” with “productive unit” or “establishment”; and moving the reference to consumers in the footnote to the text of the explanation.

19. Reference was made to recommendation 8 of the Legislative Guide, which addressed those debtors eligible for insolvency. It was noted that that recommendation might inform the discussion of the terms of the glossary and in particular, since it included economic activities that were not conducted for profit, that approach should be maintained. The proposals with respect to the use of the word “entity” and the reference to consumers did not receive support.

(c) Capital

20. The Working Group agreed that the term “capital” should be deleted from the glossary.

(d) Control

21. With regard to the explanation of the term “control”, it was widely felt that the explanation in its present form was too broad and ambiguous. Another concern expressed was that the term encompassed not only the actual exercise of control but also the capacity to control and that the focus should be on the former, not the latter. In response, it was noted that whether control was exercised or not could prove difficult to verify. What could be included in the draft was a presumption that there might be control where there was major ownership and a requirement for proof where there was actual exercise of control.

22. Several proposals were made to simplify the explanation. Those included: (a) deleting all of the text after the words “decision-making authority”; (b) deleting the words “normally associated with the holding of a strategic position within the enterprise group”; (c) deleting the reference to “strategic position”; and (d) revising the explanation to “the ability or power derived from law, by-laws or contract to determine – directly or indirectly – the management of an enterprise or a group of enterprises.” In response to the last proposal, it was noted that there was a need to differentiate between exercising power over the management body of the enterprise and the day-to-day management of the enterprise; the former might constitute control, the latter would not. It was also suggested that control derived through contractual arrangements should be included in the commentary or an explanatory note.

23. After discussion, the Working Group agreed to simplify the explanation of the term “control” by deleting the word “normally” and adopting the proposal noted in paragraph (a) above, with further explanation to be included in an explanatory note.

(e) Procedural coordination

24. A concern was raised as to whether procedural coordination addressed the situation of a single court dealing with various insolvency proceedings of various members of a group or whether it addressed various courts coordinating with each other. In response, it was pointed out that procedural coordination included both

situations and that footnote 3 on the explanation of the term included the reference to "cooperation between two or more courts". After discussion, the Working Group agreed to move that reference in footnote 3 into the explanation under paragraph (e).

25. In that context, the importance of communication between courts was also emphasized. Although a suggestion was made to include a reference to communication in the text of the explanation of procedural coordination, it did not receive sufficient support. However, it was agreed that a reference be included in the footnote and the issue discussed in the commentary.

26. With regard to the terms in square brackets "separate" and "individual", one view expressed was that both should be included to reflect the flexibility of procedural coordination. Another view expressed was that both terms should be deleted, because they did not add any substance to the explanation and might be confusing. In response, the concern was expressed that the deletion might not fully reflect that there were different insolvency proceedings taking place at the same time. However, that concern did not find support, because the term coordination in itself implied different proceedings. The Working Group agreed to retain the terms in square brackets.

(f) Substantive consolidation

27. The Working Group agreed to consider the explanation of the term "substantive consolidation" in the context of discussing draft recommendations 16 to 23, but did not commence that discussion because of lack of time.

(g) Parent enterprise

28. The Working Group agreed to delete the term "parent enterprise" from the glossary.

(h) Subsidiary enterprise

29. The Working Group agreed to delete the term "subsidiary enterprise" from the glossary.

B. The onset of insolvency: domestic issues

1. Application and commencement: joint application

30. The Working Group discussed the application and commencement of insolvency proceedings in enterprise groups in the domestic context on the basis of draft recommendation 1 of document A/CN.9/WG.V/WP.80.

Purpose of legislative provisions

31. The Working Group agreed that the purpose clause was useful and should be retained.

Draft recommendation 1

32. Concerns were expressed that the scope of the chapeau of draft recommendation 1 was not sufficiently clear with respect to what was contemplated

by a joint application. In response, it was explained that the chapeau covered two different situations: a single application with respect to multiple debtors and multiple applications with respect to multiple debtors in the enterprise group. It was stated that since the first scenario should be covered by draft recommendation 2, the reference to the first situation could be deleted from the chapeau. After discussion, the Working Group agreed to delete the words beginning “an application” to “Legislative Guide or”.

33. Some concerns were raised that draft recommendation 1 should clarify the competent court to which the joint application should be made. It was suggested that an additional recommendation was needed that would require the local insolvency law to address that issue. It was observed that although recommendation 13 of the Legislative Guide referred the issue of the competent court to the local insolvency law, it might not be sufficient to address the issue of judicial competence over a joint application in the enterprise group context. After discussion, it was generally agreed that recommendation 13 of the Guide was not sufficient and did not provide any guidance to legislators on criteria for the determination of the competent court.

34. It was suggested that an additional recommendation could be included to indicate criteria for such determination or that the first sentence of footnote 14 to draft recommendation 3 could be revised as a recommendation. After discussion, the Working Group agreed to include an additional recommendation along the lines of the first sentence of footnote 14 and to discuss examples of possible criteria in the commentary.

35. In the context of commencement of insolvency proceedings on the basis of a joint application, it was discussed whether an additional recommendation was needed to specify the factors that linked the group together and the position in the group of each member covered by the application, particularly where one of them was the controlling entity or parent. A concern was expressed that provision of such detail might be difficult in the case of a creditor application under subparagraph (b), because a creditor might not be in a position to know the relationship between the group members. After discussion, it was noted that since the basis of the joint application was that the debtors were members of a group, information substantiating the existence of the group would generally be required in order for the court to commence insolvency proceedings. It was agreed that an additional recommendation was not required, but that the issue should be discussed in the commentary.

2. Procedural coordination

36. The Working Group considered procedural coordination on the basis of draft recommendations 2-8 of document A/CN.9/WG.V/WP.80.

Purpose of legislative provisions

37. The Working Group approved the substance of the purpose clause and agreed to remove the square brackets.

Draft recommendations 2 and 3

38. The Working Group considered the revised draft recommendations 2 and 3 and approved them in substance.

Draft recommendation 4

39. General support was expressed in favour of subparagraphs (a) and (b) of draft recommendation 4 as currently drafted. It was suggested that subparagraph (c) should be aligned with paragraph 14 of document A/CN.9/WG.V/WP.80, making it clear that a creditor could make an application for procedural coordination only in respect of those members of the group of which it was a creditor. It was also suggested that the draft recommendation should include the possibility for the court to initiate procedural coordination, subject to the relevant notice provisions. The substance of the second sentence of footnote 14 to draft recommendation 3 might be included in draft recommendation 4.

Draft recommendation 5

40. It was widely agreed that draft recommendation 5 might cover a number of different variants of procedural coordination and should therefore be as flexible as possible, including references to proceedings that were not only simultaneous, but also joint, concurrent or coordinated.

Draft recommendations 6 and 7

41. The Working Group considered whether, in addition to draft recommendation 6, provision should be made for notice of an application for procedural coordination to be given to relevant creditors. One view was that since procedural coordination was not intended to affect the substantive right of creditors, notice of the application was not required. Another view was that a distinction could be drawn between applications heard at the time of the application for commencement of insolvency proceedings and those heard subsequent to commencement of insolvency proceedings. In the former case, notice was not required, but in the latter case giving notice would be appropriate. It was proposed that a flexible approach could be adopted, prescribing the need for notice but leaving it to domestic law to determine whether that notice should relate not only to the order for procedural coordination, but also to the application for procedural coordination. After discussion, that flexible approach was supported.

42. Concern was expressed with respect to the meaning of the closing words of draft recommendation 7 “of relevance to creditors”. The view was expressed that those words did not make it clear what information, in addition to the types of information set forth in recommendation 25 of the Legislative Guide, should be included in the notice. One view was that the notice of an application should include the content of the application and that notice of the order should set forth the terms of the order. After discussion, support was expressed in favour of the draft recommendation requiring the insolvency law to prescribe the content of the notice.

Draft recommendation 8

43. While general support was expressed in favour of the current text of draft recommendation 8, it was suggested that reversal of an order for procedural coordination might also be included. It was pointed out that a distinction could be drawn between reversal of an order for procedural coordination and an order for substantive consolidation. Reversal of an order for procedural coordination might be possible since it should not affect the rights of interested parties in the same way as

they would be affected in the case of substantive consolidation. It was noted that reversal of an order for procedural coordination would occur in rare circumstances and might be acceptable if it was without prejudice to rights already affected by the initial order. After discussion, a proposal to address that issue in the commentary received some support.

44. The question of giving notice of an application to modify or terminate an order for procedural coordination and the order modifying or terminating was raised. While some support was expressed in favour of giving notice of the application as well as the order, support was also expressed in favour of giving notice only of the order. It was proposed that the same flexible approach could be adopted as with respect to procedural coordination, prescribing the need for notice but leaving it up to domestic law to determine whether that notice should relate not only to the order for modification or termination, but also to the application for modification or termination. The secretariat was requested to prepare a draft recommendation for consideration by the Working Group at a future session.

3. Post-commencement finance

45. The Working Group considered post-commencement finance on the basis of draft recommendations 9-13 of document A/CN.9/WG.V/WP.80.

Purpose of legislative provisions

46. It was suggested that although the purpose clause relating to post-commencement finance from the Legislative Guide was relevant, it did not specifically address the enterprise group context and, in particular, the provision of finance by one member of a group to support another member of that group. After discussion, the Working Group agreed that the purpose clause from the Legislative Guide should be included before draft recommendations 9-13 and further paragraphs should be added to reflect the provision of post-commencement finance in the enterprise group context.

Draft recommendations 9 and 10

47. After discussion, the Working Group approved draft recommendations 9 and 10 in substance.

Draft recommendation 11

48. The Working Group considered various ways in which financing might be provided to a group member subject to insolvency proceedings. That finance might be provided by a lender external to the group and by another member of the group, where that member might be either solvent or subject to insolvency proceedings. The Working Group agreed that post-commencement finance provided by a lender external to the group or by a solvent member of the group would be covered by the recommendations of the Legislative Guide. Draft recommendations 11-13 were intended to address the situation where post-commencement finance was provided to one member subject to insolvency proceedings by another member also subject to insolvency proceedings.

49. It was recalled that recommendation 64 of the Legislative Guide specified the need to establish the priority to be accorded to post-commencement finance and the

level of that priority. Whilst noting the importance of priority as an incentive for such financing, it was questioned whether the level of priority recommended would be appropriate in the context of the provision of finance by members subject to insolvency proceedings to other members also subject to insolvency proceedings. One view was that the same priority would be appropriate; other views suggested it might not be appropriate. After discussion, the Working Group agreed that the draft recommendation should specify the need for the insolvency law to accord priority to such lending, but that the recommendation itself should not specify the level of that priority.

50. A further proposal with respect to draft recommendation 11 was that it should contain the same safeguards as provided in draft recommendation 13. It was noted in response that since the focus of draft recommendation 11 was the priority that might be accorded to lending rather than the process for approval of such lending, safeguards concerning approval were not required. After discussion, the proposal to add safeguards was not supported.

Draft recommendations 12 and 13

51. It was suggested that draft recommendations 12 and 13 might be combined as the safeguards established in draft recommendation 13, subparagraphs (a) and (b), should also apply to draft recommendation 12. It was noted that although recommendations 66 and 67 of the Legislative Guide provided certain safeguards with respect to the provision of a security interest for post-commencement finance, they were not sufficient for the enterprise group context as they did not contemplate the provision of cross-entity support. The proposal to combine the two draft recommendations was not supported, but the Working Group agreed that the safeguards of draft recommendation 13 should also apply to draft recommendation 12. As a matter of drafting, it was noted that both members of the group referred to in draft recommendation 12 should be subject to insolvency proceedings.

52. It was observed that the provision of post-commencement finance in the situations contemplated by these draft recommendations raised important issues of the balance to be achieved between sacrificing one member of the group for the benefit of other members and achieving a better overall result for all members. The general view was that although the appropriate balance might be difficult to achieve, the goal should be a fair apportionment of the harm in the short term with a view to the long term gain, rather than a sacrifice of one member for the benefit of others.

53. With respect to the words in square brackets in subparagraphs (a) and (b) of draft recommendation 13, support was expressed in favour of the word “determines” and the words “are not likely to be”. A suggestion was made that the test of adverse effect be replaced by a test of unfair prejudice. Various views were expressed with respect to whether the subparagraphs should be cumulative or exclusive. Agreement was reached on the need for flexibility, recognizing the possibility that approval of the insolvency representative might be sufficient without the need for court approval. However, support for a subsequent proposal to combine the paragraphs and adopt a more general test that the rights of creditors should not be harmed removed the necessity of considering that issue further. It was proposed that the commentary should address the question of who should make the determination with respect to harm to creditors e.g., the insolvency representative, the court or

both according to national law or the creditor committee. It was recalled that recommendation 137 of the Legislative Guide addressed rights of appeal with respect to decisions taken by the insolvency representative. With respect to the role of the creditor committee, it was observed that although important, the creditor committee should not be given authority to decide on the granting of post-commencement finance.

54. The Working Group agreed that subparagraphs (a) and (b) should be deleted and the draft recommendation revised to focus on the need to protect creditors from harm. The Working Group further agreed that the commentary should explain the details of the safeguards, including the role to be played by the insolvency representative, the court and the creditor committee.

4. Avoidance proceedings

55. The Working Group considered avoidance proceedings on the basis of draft recommendations 14 and 15 of document A/CN.9/WG.V/WP.80/Add.1 and approved the substance of those two recommendations.

5. Substantive consolidation

56. The Working Group considered substantive consolidation on the basis of draft recommendations 16-17 of document A/CN.9/WG.V/WP.80/Add.1.

Purpose of legislative provisions

57. It was observed that the purpose clause was very useful and should be retained in substance. In order to emphasize the permissive character of the provisions with respect to substantive consolidation, it was suggested that in subparagraph (c) the word "is" should be replaced with "may be made available". That proposal was supported.

58. A further proposal was made to insert the words "and predictability" at the end of subparagraph (d). It was noted that the concepts of transparency and predictability were used together in the Legislative Guide as key objectives in paragraph 7, part one. Although predictability was agreed to be an implicit goal of all of the draft recommendations, it was noted that with respect to substantive consolidation a distinction could be drawn between the question of whether the standards were predictable or whether the situations in which substantive consolidation would be ordered would always be predictable, given that there was an element of judicial discretion in the applicable standards. After discussion, the Working Group agreed to add the words "and predictability" to the end of subparagraph (d).

Draft recommendation 16

59. Support was expressed for the draft text, as it established the basic principle of the separate entity and the exception. However, a suggestion was made to delete the words in square brackets and insert a second sentence as follows: "The insolvency law may provide for exceptions in accordance with recommendation 17." That suggestion found broad support on the basis that it would enhance the clarity of the provision and the Working Group agreed to revise draft recommendation 16 accordingly. It was observed that the reference to the separate legal identity of each

member of the enterprise group might need to be reconsidered in light of the explanation of the term "enterprise" and the flexibility of the legal form of the entity.

Draft recommendation 17

60. A proposal to delete the phrase "to proceed together as if they were proceedings with respect to a single entity", retain the words in square brackets in the chapeau and add the words "substantive consolidation of" after the words "the court may order" was widely supported. It was noted that there might be situations where the proceedings might need to be kept separate to resolve certain issues even when the assets were pooled to create a single estate. It was proposed that a connection between draft recommendations 17 and 23 should be made in order to emphasize that the rights of secured creditors would not be prejudiced by an order for substantive consolidation.

61. Various concerns were expressed with respect to the standards established in subparagraph (a). Those were: (a) that the standard of impossibility was too high and would be hard to satisfy before identification had been attempted; and (b) that the meaning of the word "undue" was uncertain and should be replaced with a concept of disproportionality of expense and delay to the amount that could be recovered for creditors or to the benefit to be derived from undertaking the identification. Although some support was expressed in favour of retaining standards of both impossibility and disproportionality, after discussion it was agreed that a standard based upon disproportionality of expense and delay should be used.

62. A number of issues were raised with respect to the scope of substantive consolidation. In particular, it was questioned whether the assets of a solvent or apparently solvent group member might be included in the assets substantively consolidated. It was agreed that paragraph (a) could result in that inclusion and should be permitted. It was further questioned whether draft recommendation 17 should refer to both assets and liabilities, as it might only be necessary to refer to liabilities. Support was expressed in favour of retaining the reference to both assets and liabilities.

63. Concerns were expressed with respect to the terms used in subparagraph (b) and in particular with the conduct sought to be addressed in each case. It was agreed that those terms should be explained in the commentary. After discussion, it was generally agreed that "simulation" might be deleted, with an explanation to be included in the explanation of fraudulent schemes in the commentary.

64. A proposal to delete subparagraph (c) on the basis that it did not meet the standard of objectivity was widely supported. It was observed that the concepts referred to in subparagraph (c) of appearance and reliance might give rise to other remedies, but should not lead to substantial consolidation. Though some views were expressed in favour of retaining subparagraph (c), the Working Group agreed to its deletion. It also agreed that no reference to the concept contained in paragraph (c) should be included in any commentary to draft recommendation 17.

65. The Working Group considered the proposal in paragraph 15 of document A/CN.9/WG.V/WP.80/Add.1 to add a recommendation addressing the consequences of an order for substantive consolidation. It was generally agreed that such a recommendation would be useful. As to its content, it was agreed that such

an order would extinguish intra-group claims and debts, but would not establish a single consolidated entity. Consideration of a more general proposal to include in the recommendation some of the effects addressed in draft recommendations 18-23 was deferred, pending discussion of the content of those draft recommendations.

6. Additional recommendations on substantive consolidation

66. The Working Group considered additional recommendations on substantive consolidation on the basis of draft recommendations 18-23 of document A/CN.9/WG.V/WP.80/Add.1.

Draft recommendation 18

67. With respect to the scope of draft recommendation 18, it was clarified that partial substantive consolidation provided the possibility of excluding certain assets or claims from an order for consolidation, but did not refer to the exclusion of certain group members from that order. What was intended, for example, was that where ownership of an asset was clear in the case of intermingling of assets, it could be excluded from the consolidation. Although it was acknowledged that in some cases the same result might be achieved through other remedies available under the Legislative Guide, for example, the provisions on abandonment, it might be simpler to provide for those assets to be excluded from the order for consolidation. In response to a concern with respect to the protection of encumbered assets and the wording of paragraph 17, it was agreed that a clearer explanation of partial consolidation would be provided in the commentary. Deletion of the text in square brackets was supported. The Working Group approved the substance of draft recommendation 18 with that deletion.

Draft recommendation 19

68. A proposal to align draft recommendation 19 with draft recommendation 4 was not supported on the basis that procedural coordination could not be equated with substantive consolidation and although it might be appropriate to permit the debtor to apply for the former, it would not be appropriate in the circumstances supporting substantive consolidation under draft recommendation 17. With respect to a proposal that the court might initiate substantive consolidation, the Working Group recalled that it had agreed at its thirty-third session that the court should not be permitted to do so (see A/CN.9/643, para. 83).

69. A suggestion was made to replace the word "should" in the latter part of the paragraph with the word "could" or "may" to broaden the scope of applicants permitted to make the application. Another drafting suggestion was to end draft recommendation 19 after the term "substantive consolidation", so that it would be left to local insolvency law to specify the persons permitted to make the application. After discussion, the Working Group agreed to substitute the word "may" as proposed and approved the substance of the draft recommendation.

Draft recommendation 20

70. After discussion, the Working Group agreed that draft recommendation 20 should be simplified to provide that in the event substantive consolidation was ordered, a single or first meeting of creditors (where such a meeting was required

under the insolvency law) might be convened. It was also agreed that the commentary should address the flexibility of approaches adopted by insolvency laws to the participation of creditors and, in particular, to meetings of creditors.

Draft recommendation 21

71. Broad support was expressed in favour of subparagraph (a) based on recommendation 89 of the Legislative Guide. Some concerns were expressed with respect to subparagraph (b). One view expressed was that the court should be given the flexibility to decide upon the suspect period in such situations. In response, it was pointed out that the Legislative Guide recommended that the date from which the suspect period would be calculated should be stipulated in the insolvency law. Another view was that subparagraph (b)(ii) would be hard to apply and the result unpredictable. In response, it was observed that subparagraph (b)(ii) did no more than state the usual approach based on subparagraph (a) and recommendation 89 of the Legislative Guide, that there would be a suspect period with respect to each member of the group subject to insolvency proceedings. Subparagraph (b)(i), on the other hand, provided an exception, establishing a common date for all enterprise group members when substantive consolidation was ordered subsequent to commencement of insolvency proceedings. After discussion, the Working Group approved the substance of draft recommendation 21 with: (a) the order of subparagraphs (b)(i) and (b)(ii) to be reversed; and (b) the word “single” in subparagraph (b)(ii) to be replaced with the word “different.”

Draft recommendation 22

72. In response to a suggestion that an order for substantial consolidation might be difficult to modify, the Working Group recalled that it had agreed in its previous session to include such a recommendation, on the basis that it might be necessary when there were circumstantial changes or new information became available. Broad support was expressed for draft recommendation 22. It was suggested that notice should be provided when modification of an order for substantive consolidation was ordered and that a recommendation along the lines of recommendation 6 should be included. The Working Group approved the substance of draft recommendation 22 and agreed that the issue of notice should be addressed.

Draft recommendation 23

73. It was suggested that draft recommendation 23 should follow draft recommendation 17, as it addressed an important issue. Another suggestion made was that the commentary should note that a secured creditor could surrender its security interest following consolidation and the debt would become payable by all of the consolidated entities. Both suggestions found support. It was further proposed to include in subparagraph (b) after the term “fraud” the phrase “in which the creditor had participated”. It was noted that since recommendations 4 and 88 of the Legislative Guide would also apply in the group context, subparagraph (b) might not be required. In response, it was suggested that a reference to recommendation 88 should be made in subparagraph (b). A further suggestion made was to extend draft recommendation 23 to include other rights giving priority or advantages over other creditors such as priorities, as well as guarantees and liens. After discussion, the

Working Group agreed to all of the proposals made with respect to draft recommendation 23.

74. Recalling the proposal to include a recommendation addressing some of the effects of substantive consolidation referred to in draft recommendations 18-23, the Working Group agreed that such a recommendation should be included and should address the effect on intra-group claims, security interests and other rights as noted above.

Competent court

75. The Working Group discussed the necessity of defining the competent court for purposes of substantive consolidation. It was suggested that the approach provided in recommendation 13 of the Legislative Guide and the conclusion reached with respect to procedural coordination that local insolvency law should determine the competency of the court, should be followed. Consequently, the Working Group agreed that the recommendation on the competent court with respect to procedural coordination, which the Working Group had agreed to base on footnote 14 of document A/CN.9/WG.V/80, should also include substantive consolidation.

7. Appointment of the insolvency representative

76. The Working Group considered the appointment of the insolvency representative on the basis of draft recommendations 24-28 of document A/CN.9/WG.V/WP.80/Add.1.

Purpose of legislative provisions

77. The Working Group approved the substance of the purpose clause.

Draft recommendation 24

78. The Working Group approved the substance of draft recommendation 24, with the text currently included in square brackets to be retained without the brackets. It was observed that the commentary should make it clear that the concept of a single insolvency representative might be interpreted as meaning that the same insolvency representative was appointed to each group member.

Draft recommendation 25

79. It was proposed that the text in square brackets should be retained without the brackets, with the words “or may exist” being added at the end of the draft recommendation. That proposal was supported and the Working Group approved the substance of draft recommendation 25. It was noted that a reference to the recommendations of the Legislative Guide addressing requirements for disclosure in relation to conflicts of interest should be included in the commentary.

Draft recommendations 26-28

80. The Working Group approved the substance of draft recommendations 26-28. It was noted that some revision might be required to ensure consistency of the language of subparagraph (d) of draft recommendation 28 with the context.

Draft recommendation 29

81. The Working Group agreed that the focus of draft recommendation 29 was that a single reorganization plan covering two or more members of an enterprise group might be approved in insolvency proceedings concerning those members. To that end, it was agreed that the text in the first and second sets of square brackets should be deleted and the text in the third set of square brackets be retained without the brackets. It was noted that the recommendations of the Legislative Guide with respect to approval of the reorganization plan would apply to the separate approval of the plan by the creditors of each group member covered by the plan.

Draft recommendation 30

82. With respect to the second sentence, it was agreed that the text in the first set of square brackets should be retained without the brackets and that the text in the second and third sets of brackets should be deleted. The Working Group approved the substance of draft recommendation 30.

83. Concern was expressed with respect to whether draft recommendations 29 and 30 referred to both procedural coordination and substantive consolidation, since reorganization in the latter context had not been discussed. For lack of time that issue was not considered, although it was noted that a third possibility included a single reorganization plan being used where there was neither procedural coordination nor substantive consolidation.

84. For lack of time, the issues raised in paragraphs 33 and 34 with respect to post-application financing and treatment of contracts were not considered.

C. The onset of insolvency: international issues

85. The Working Group considered the treatment of enterprise groups in a cross-border context on the basis of the issues raised in documents A/CN.9/WG.V/WP.74/Add.2 and A/CN.9/AG.V/WP.76/Add.2. The Working Group noted developments with respect to the project to compile practical experience on negotiation, use and content of cross-border protocols and agreements on the basis of document A/CN.9/629 and the foreshadowed report to the forty-first session of the Commission to be contained in document A/CN.9/654.

86. At the outset, it was suggested that the Working Group should consider the objectives it wished to achieve in the international sphere. The formulation of minimum recommendations on the exercise of jurisdiction, substantive issues and conflict of laws were identified as potential objectives. Whilst acknowledging that conflict of laws rules might be the most difficult of those goals, it was suggested that the formulation of minimum recommendations on the first two might be achievable.

87. A different approach suggested taking the UNCITRAL Model Law on Cross-Border Insolvency as the starting point and considering how it might be supplemented to address the enterprise group context, following the Working Group's approach with the Legislative Guide. That approach might include issues of coordination, involving, for example, procedural coordination of insolvency proceedings and cooperation between courts and insolvency representatives, the

benefits of which were widely acknowledged. Other issues proposed for consideration in addition to those addressed by the Model Law included commencement of proceedings, centre of main interests with respect to a group, and post-commencement finance.

88. With respect to coordination, it was questioned how the approach of the Model Law might apply to a group context, given that it operated only as an interface between different legal regimes, respecting the differences between national procedural laws and not seeking to unify insolvency laws. It was suggested that that approach disregarded the economic reality of the group. A different view suggested that the principles of the Model Law, which could be used to address a single debtor with assets in more than one country, might be extended to address two or more debtors with assets in multiple countries. In response, it was pointed out that the example of the single debtor with assets in more than one country involved coordinating different parts of one insolvency estate, while the group situation required coordination of different insolvency estates, unless the notion of a unified group estate could be developed.

89. On the topic of post-commencement finance, it was suggested that some of the structural impediments encountered included issues of authority, personal liability on the part of office holders and insolvency representatives with respect to new debt, the application of avoidance provisions, and issues of priority and its cross-border recognition. It was noted that finance in the group situation might involve the provision of finance from an external lender that was structured as intra-group finance, being channelled by the initial borrower to other group members, with security provided on the assets of group members, some of which may not receive any of the financing. In the event of the insolvency of two or more members of the group, post-commencement finance might be provided by an external lender and used in the same way. It was observed that that scenario raised issues not considered in the Legislative Guide or in the Working Group's consideration of post-commencement finance in the context of a group in a domestic situation. In response, it was suggested that the recommendations of the Legislative Guide and draft recommendations 9-13 addressed that situation – the Legislative Guide applying where one of the parties to the post-commencement financing transaction was solvent and draft recommendations 11-13 applying where both parties were insolvent.

90. It was proposed that one approach to addressing international issues might be to identify the barriers to facilitating the coordinated treatment of international enterprise groups in insolvency and consider whether it was possible to address those barriers and in what manner. For that purpose, the Model Law, the Legislative Guide and the working papers prepared for Working Group V might be helpful in terms of identifying issues and considering the applicability of solutions already adopted or proposed in order to identify possible gaps. It was suggested that the focus of that task might include issues of commencement of proceedings, jurisdiction, provision of finance, centre of main interests, and coordination and cooperation between courts and insolvency representatives. It was also suggested that the objective of that task would be to consider how to maximize the value of the group and the importance, in that regard, of reorganization.

91. The Working Group agreed with that approach and requested the secretariat to proceed with the preparation for the thirty-fifth session of the Working Group on that basis.