Promoting global solutions against fundamental inefficiencies of national civil procedure law: a case for international harmonization.

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SUMMARY

Insolvency and restructuring are strongly court-driven proceedings in the majority of developed and developing countries. In many of those countries, such proceedings are governed by broader frameworks of procedural rules for the administration of private law disputes. To the extent invested with a stay of action, insolvency proceedings are genuine substitutes to individual recourse to justice, and must therefore comply with the well understood fair trial imperatives set out in international law, such as art 6 of the European Human Rights Convention and art 47 of the Charter of Fundamental Rights of the European Union.

This note briefly sets out the thesis that well-designed and well-functioning systems of domestic procedural law are essential for dealing efficiently and effectively with cross-border insolvency and creditor rights: not only because insolvencies with cross border elements most frequently involve corporate groups, and are therefore “domestic” in the eyes of the forum, but also because any substantive insolvency law is only as good as the procedural framework for its application and enforcement. International harmonization of insolvency law and the refinement of existing, and creation of new, legal tools specific to insolvency, are likely to always fall short of expectations, unless more fundamental issues of justice administration systems are also addressed, and procedural laws harmonized internationally with the aid of model laws and legislative guides, and, where possible, with the enactment of unified legislation.

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The “new law”: insolvency law reform of 2007

In 2007 a new Insolvency Code ("IC") was enacted in Greece and proclaimed to be the “outcome of reform efforts for over 70 years”, and “one of the most critical reforms for the modernization of Greek law”. In 2010 the UNCITRAL Model Law was adopted, and in 2011 we “perfected” the IC (by re-enacting previously abolished 1990’s restructuring law, which had not worked very well when in the first place).

The market test during the crisis

Some Greek and European jurists, debtors, bankers, consultants and other market professionals tend to think that Greece does now have a modern and comprehensive legislative framework governing domestic gross border insolvency. The greater part of the international professional and investment community – the helmsmen to capital deployed in the periphery of Europe (including in manners which qualify as Foreign Direct Investment) seems to disagree.

It is perhaps a trivial observation that Greece’s fiscal and financial revival depends critically on foreign direct investment, since none of the other three components of its GDP (consumption, which has declined drastically, public spending, which is constricted under current EU fiscal policies, and the balance of trade, which presupposes domestic capital expenditure and production) hold much promise for the foreseeable future.

This trivial observation is a useful point of departure for highlighting the failure of Greek insolvency and creditor rights laws to attract distressed investment in viable and profitable operating assets, when that investment was most needed – during a domestic banking crisis, which drove the operations of many over-indebted, but viable and profitable enterprises, to a standstill. Not many investors felt comfortable to deploy capital under the aegis of domestic insolvency and creditor rights laws, even when sovereign risk subsided, and widely available investment opportunities should, ceteris paribus, have become more attractive than alternative uses of that capital.

A high-level look at the record of insolvency proceedings and transactions since the inception of the crisis in 2009, and of the reactions of stronger domestic enterprises, is quite telling.

Since early 2009, the professional community engaged in distressed investment and restructuring community, on macroeconomic considerations alone, has been anticipating a “wave” of court-assisted restructurings in banking, tourism, shipping, manufacturing, agriculture, energy and natural resources, and other sectors, and many investors and advisors has been establishing aggressively in Greece.

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2 Law 3588/2007

3 Replacing, as it did insolvency legislation, whose models dated back to the year 1673: before the IC, the main corpus of Greek insolvency law had been among the oldest bodies of rules currently in force. In it survived for the most part the chapter on bankruptcy of the Napoleonic Code de Commerce of the year 1807 (itself based on the French Ordonnance de Commerce of 1673).

4 Law 3858/2010,
Very few of those investors have been able to deploy capital in distressed circumstances, and none with the assistance of the insolvency courts, while, at the very same time, many illiquid, but viable potentially profitable enterprises from the secondary5 and tertiary6 sectors have either simply shut down without getting liquidated, or sustained significant losses as a result of the unavailability of domestic finance coupled with the inability to attract international debt and equity finance with the promises of efficient and effective restructuring of old debt and displacement of old equity.

Debtors with sizeable balance sheets seem to restructure abroad, or fail to restructure at all, sometimes with dire consequences.

In late 2009, the 3rd largest Greek mobile operator was restructured by way of a prepack restructuring of holding companies under UK administration, even though no COMI and not a single asset was located outside Greece; the global creditors of ca. €4bn apparently had little faith in the efficiency of restructuring in the true COMI, under Greek law and process.

Since 2013 the restructuring of a formerly large plastics group, with subsidiaries in Germany, the UK, Spain, Italy, South Africa and the USA, was permanently frustrated, because international bondholders were uncomfortable with the idea of leading a group restructuring, in which Greek law and the Greek court system would play the dominant role; in 2014 not a single of a dozen factories remains in operation.

Of a long list of debtors operating as private corporations, whose equity is owned the Hellenic Republic7, which are not legally exempt from general insolvency law, none sought, or was targeted for distressed acquisition with, the assistance of the insolvency court. While there is obviously something to be said about investor reluctance to arm-wrestle the State as controlling shareholder of utilities, such as water or railways, it is hard to see how the same considerations could explain the absence of proceedings for insolvent motorways and marinas.

During the same time, larger enterprises, which are able to borrow internationally, have effectively relocated their balance sheet to Luxembourg, the UK or the US8, as if to make sure that their borrowing or restructuring initiatives never have to pass the tests of Greece insolvency and creditor right laws or the Greek court process.

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5 E.g. steel, wind and solar power, waste management, aquaculture, agriculture, fertilizers, construction.
6 E.g. hotels, shipping, media & entertainment
8 By borrowing at parent and holding company level, by restricting the powers of management and shareholders to dispose of operating company assets and then pledging its equity to international lenders, and by other creative mechanisms designed to entirely circumvent the application of Greek insolvency law and the Greek court system.
Greece nowhere near the avenues of cross-border restructuring

The above examples – of few major restructurings in general; of successful cross-border restructurings of Greek debtors simple done outside of Greece; of failed cross-border restructurings opened in Greece – demonstrate that Greek insolvency law and process neither is, nor is perceived to be, an efficient and effective tool for addressing problems of financial distress.

This is reflected in the impressively scarce jurisprudence applying the EIR and the Model law: less than a dozen judgements have applied the EIR since 2002, and only one reported judgement has applied the Model Law since its enactment in 2010⁹.

Regulatory reaction: reforming without a guiding paradigm

It is fair to say today that post-crisis reform to the basic framework adopted since 2007 not only lacked a solid theoretical basis and guiding paradigm, but paid little heed to the real life functioning of credit markets and to the law making imperatives of certainty and predictability.

The 2011 Insolvency Code Reform Bill originally toyed with the idea of permitting the opening of an insolvency proceeding not only when a debtor became unable to meet financial obligations as the fall due, but also ‘regardless of present or threatened inability to meet obligations as they fall due, if, in the court’s judgement, the debtor faces serious economic problems, which may be addressed by this proceeding’. It is fortunate that this bad idea of deferring the key substantive condition for the opening of insolvency proceedings, invested with a stay of action, to the unguided judgement of each insolvency court, did not find its way into law and did not threaten quintessential foundations of an open market economy, including vested property rights and the right of recourse to a court of law for the enforcement of private rights set out in the Greek Constitution (art 20§1), the ECHR (art 6§1) and the Charter of Fundamental Rights of the European Union (art 47).

Another bad idea from the same bill did find its way into law, namely the idea that, because the word “bankruptcy” was perceived to be associated with failure and loss of goodwill, it is appropriate to reintroduce a dualist system, with separate rules for insolvency and restructuring, and to exempt restructuring proceedings from the general framework of rules governing collective proceedings.

A few good ideas set out in the 2007 fell victims to this reform, and vis attrativa concursus was one of them. As a result, it became (again) possible to derail a restructuring proceeding by arresting estate assets in the course of individual creditor actions, which are tried by the general courts, rather than the insolvency court, with the great delays of ordinary trial.

Other good ideas were poorly implemented, such as the simple universal that when equity drops to or below zero, and the rights of creditors are already impaired, shareholders as such

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⁹ Athens CFI 437/2013, recognising a Florida Middle District bankruptcy proceeding insolvency of a natural person and ordering the relief of art 21 of the Model Law.

¹⁰ The constitutional and international law rules, which this idea would violate, are set out in Klissouras, “The pending reform of the Greek Insolvency Code”, Insolvency and Restructuring International, 2011:27.
must not control (through appointed management) the debtor’s decision to apply or not for a court-assisted restructuring. This principle is also set out in the Legislative Guide11. Under the IC reform, equity may indeed be crammed down towards the end of a court-assisted workout proceeding, if it refuses to vote corporate action (most often, its own dilution) set out in the court-approved plan; but only the debtor, i.e. management invariably elected by existing equity, can file for the opening of restructuring proceedings or propose a plan.

As a result, the entire legal framework for court assisted restructuring immediately degraded into a set of pre-emptive, mostly sham, debtor remedies, which were abused to fend off creditor enforcement for extremely long periods of time. As a further result, equity holders across the board have been able to shut down operations, hold on to their title to operating assets, and hope that creditor rights enforcement can be delayed until the advent of better days for the market as a whole. No employment, no consumption, and no direct and indirect tax revenues are generated in the meantime from the operation of those assets by new investors.

Finally, some very bad ideas crept in the fringes of insolvency law, such as the enactment in statutes governing civil process of hidden substantive rules purporting to subordinate secured claims to generally preferred claims (for wages and taxes), in effect purporting to expropriate security interests against the prohibition of expropriation (art 17§1 of the Greek Constitution, art 1 of the First Additional Protocol to the European Convention on Human Rights). Not only did this stave off a number of significant distressed investment initiatives nascent in 2011 (by effectively ending the secondary trading of secured debt into the hands of specialist restructuring funds), but, by reducing expected recovery on secured debt, it removed the motives on old creditors to pursue such enforcement. In Q4 2014, domestic banks are still in search of administrative solutions to the administration of their bad asset portfolios.

These are just some of the reasons why Greek insolvency and creditor rights law did not dampen the deleveraging of the economy, or assisted in the transition to healthier economic activity, when this was most needed.

More fundamental inefficiencies: the general rules of civil process

The shortcomings of domestic insolvency law and creditor rights law and related reform must not be viewed in isolation from the more fundamental shortcomings of the court system and the general rules of civil process, which apply to insolvency proceedings and define the formal framework for the administration of justice in general, and of insolvency proceedings in particular.

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11 UNCITRAL Legislative Guide on Insolvency Law (2005), paras. 48-53, esp. para 48: "[...] Given that one of the objectives of reorganization proceedings is to enhance the value of assets and thereby increase the return to creditors on their claims through the continued operation and reorganization of the debtor's business, it is highly desirable that the ability to apply not be given exclusively to the debtor. A further reason for allowing creditor applications is that there will be cases where the debtor will not or cannot apply for commencement because, for example, management has resigned. The ability of creditors to apply for reorganization is also central to the question of whether creditors can propose a reorganization plan (see chap. IV, paras. 8-14) and may significantly influence their support for any plan proposed."
To give a few brief examples:

- In the most "complete" type of trial envisaged in the Greek Code of Civil Procedure, so-called "ordinary proceedings", an action filed is set for hearing at a date falling after between 16 and 30 months; nothing happens for these 16-30 months, until 20 days before the hearing date, when pleadings and evidence documents are filed; since there has been no prior determination of issues of law and fact, which are disputed, parties are obliged to argue and prove all points of fact, even if admitted by the adversary; rebuttals are filed 15 days before the hearing, which may mean as little as 3 days after the pleadings; at the hearing the parties and the court for the first time learn the identity and hear the testimony of witnesses; cross examination is rudimentary, since it is devised on the spot; assessment of witness testimony is filed 8 days after the hearing and this completes the trial in the first instance.

- Litigants or lawyers can, and regularly do, cause 12, 14 or 18 month “adjournments” of a hearing, by showing up on the day and pleading “obstacle to participate” or “important reasons to adjourn”. In addition to ordinary proceedings, a dozen or more “special proceedings”12, with trivial or non-existent differences, complicate the procedural landscape, and having the wrong procedure applied is frequently enough to have judgement set aside in the second instance.

- A law suit can run a course of 10 years or more from first instance to the Supreme Court (one or more times), and result in a judgement basically saying that the claim was not properly specified in the first place, in essence telling the plaintiff to return with a properly formulated claim.

In fairness to the legislative committee presently at work on an extensive overhaul of the existing rules of civil process, many of these remnants of successive fragmentary amendments of the basic law on process are likely to be abolished in the near future, perhaps within 2014.

However, it is not contemplated at present that this reform will address other fundamental shortcomings of the rules of fair, efficient and effective, trial, some of which are given a cursory overview below.

Public trial

The letter of the Greek Constitution (art 93§2) mandates a public hearing, but, read literally, not necessarily public access to trial proceedings conducted almost exclusively in writing. Little does it matter today that, when this constitutional rule was conceived, the entire trial took place at the hearing, where documents were read out aloud, witnesses testified, argument was orally made, and everything was transcribed into the court’s public record of the hearing.

Under the weight of widespread misconstruction of personal data protection laws, today it often takes a mini-trial to obtain copies of court judgements, court hearing transcripts and party pleadings and documents, subject to showing compelling reasons, and without a reasoned decision

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12 Marital Disputes; disputes between parents and children; payment orders; repossession orders for leased property; labour disputes; contractor disputes, disputes from the operation of vehicles; alimony and custody disputes; conservatory measures in adversary proceedings; voluntary jurisdiction; conservatory measures in voluntary jurisdiction; enforcement trial proceedings;
when such applications are denied. It is not an infrequent phenomenon that interested parties are unable to secure access, by leave of the court administrator (a judge, exercising administrative functions), to judgements, party filings and evidentiary documents, which may be critical for arguing or proving (especially) in insolvency proceedings.

In practical terms, the rules governing access to court documents tolerate the same debtor pleading imminent insolvency in support of an application for a stay order against creditors, and stellar financial strength and performance as a defence in an individual creditor action for conservatory measures; the falsity of a document in one proceeding, and the authenticity of the same document in another; the validity of an agreement in one, and the nullity of the same agreement in another proceeding. The debtor’s opponents in any of those proceedings are not by default entitled to obtain the debtor’s own pleadings to plead against the debtor in the other proceeding.

Insolvency judges with a strong predilection for personal data protection have sometimes gone so far as to deny creditors properly participating in an insolvency proceeding of the right to obtain evidence of claims filed by other creditors, although this is manifestly a necessary precondition for the exercise of a creditor’s right to oppose the filing of claims by any other creditor.

**Reasoning of judgements**

The Greek constitution (art 92§3) also mandates that judgements must be fully and specifically reasoned, in law and in fact, and many of them are indeed exemplary. Yet any judge, arbitrator or litigation lawyer will immediately recognize the difficulty of carrying this imperative consistently into practice (even without external pressures, such as the overwhelming case load facing the Greek court system, in great measure due to the system’s own inefficiency), without good rules on the drafting of documents to bring, plead and prove an action before court.

Procedural laws, which allow the gradual specification and, where applicable, quantification of claims, and discourage litigants from disputing moot or indisputable issues of law or fact (through rules on costs, penalties on parties and lawyers for procedural misconduct and rules on lawyer conduct), do perhaps provide more tools, and a more natural procedural framework, for a judge to examine complex issues in an analytical manner and sequence, and to deliver properly reasoned judgement at each stage of the process.

Procedural laws, such as Greece’s, which envisage a single hearing and a single, all-encompassing, judgement on all disputed issues, ranging from jurisdiction, standing, merit in law, admissibility and evidentiary value of each piece of evidence, adjudication of objections, and detailed assessment of the quantum, pose a much more formidable task.

As a consequence, the formidable efforts, erudition and bench experience of Greek judges notwithstanding, the vast majority of judgements are in fact not reasoned in law and fact in any strict logical sense. For instance, the standard wording of judgements in the opening section on the assessment of facts is something to the effect that “from the entirety of the evidence submitted, bar none, it was proven that [...]”, followed by the judge’s composition of the evidentiary basis (minor clause of the syllogism) of the ordering part (conclusion). Some judgements are good, some are not, but most are not reasoned in any strict logical sense, and this fact alone has far ranging consequences.
Impact on the appellate trial

Under Greek law, an appeal is a complaint of error in the first instance judgement. Therefore, by logical necessity, an appeal ought to specify the error, and this is indeed the theoretical description on an appeal. The appellate trial is conducted entirely in writing, exclusively on the basis of claims, documents and pleadings made in the first instance. The right to appeal is not articulated in the law as a carte blanche to seek a different or more favourable judgement, but as a remedy against errors of the first instance judgement. But it is logically perplex to identify and specify errors in a judgement, which is not logically reasoned in law and fact.

In order to avail themselves of the power to set aside manifestly wrong first instance judgements, the courts of appeal have developed case law, which runs against the letter of statute, holding that an appeal need not be reasoned, and that it is sufficient if it specifies the alleged error, without further explanation, as “wrong interpretation or application of the law” and “wrong assessment of evidence”. As a result, the vast majority of appeals don’t specify any actual error of the first instance judgement, and are therefore extremely hard or impossible to defend.

It is highly questionable today if this affords to defendants in appellate trials the defendant’s right “to have knowledge of and comment on all evidence adduced or observations filed with a view to influencing the court’s decision” as a key pillar of the fundamental right to fair trial (identical in this respect to art 20§1 of the Greek Constitution).

An appeal also suspends the enforceability of the first instance judgement. Therefore, appeals are filed invariably, against all first instance judgements, as if no first instance court ever made a right decision in this country, simply in order to delay res judicatur and enforceability.

Impact on objective impartiality & faith in the court system

Equally important in theory, regardless of the limited number of cases raising such suspicions, is the impact of inadequate reasoning (a) on the ability of parties and supervising authorities to single out instances of lack of judicial impartiality, (b) on the faith and confidence of citizens and market participants in the court system as a whole, through the increased transparency and predictability built by properly reasoned jurisprudence.

Fragmentation of jurisdiction: alternating courts & conservatory and interim measures

The flawed manner, in which trials hearings are scheduled, described above, and the ease of causing the adjournment of a hearing for an unspecified future date, have the further conse-

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13 ECHR C 8/1996/627/810, Mantovanelli v. France:
« 33. The Court notes that one of the elements of a fair hearing within the meaning of Article 6 para. 1 (art. 6-1) is the right to adversarial proceedings; each party must in principle have the opportunity not only to make known any evidence needed for his claims to succeed, but also to have knowledge of and comment on all evidence adduced or observations filed with a view to influencing the court’s decision”

quence that several different judges are routinely called to try the same matter, since the composition of single and multi-member courts is defined administratively by reference to the calendar, and a judge or court first seized of an action is not called on the bench to try the action at subsequent hearings. The same occurs in the case of interim judgements, ordering e.g. further evidence: one court will have ordered this, but another court will hear and examine it. Finally, jurisdiction for a main action is largely unconnected with jurisdiction for conservatory measures, and the judge of the main trial practically has no authority over measures and injunctions ordered by a different judge in conservatory and interim proceedings.

It is easy to see how this multiplies effort and costs for litigants, multiplies proceedings and reduces the speed and efficiency of trial. But less obvious side effects are equally important: parties given the opportunity to manipulate the trial schedule for the purpose of effectively "selecting" the judge or court, which they consider most favourable to their case, will use this opportunity, and, whether or not such tactics do end up in violations of objective or subjective impartiality, they introduce suspicion of bias in the process.

**Multi-member courts**

Courts of first instance sit in two alternative compositions: one judge for the simpler and lower value matters, and three judges for higher value matters and matters implicitly considered more complex. At the time this system was designed, a multi-member composition was deemed to be a token of greater certainty of a correct judgement. Today, the system has degraded into a bureaucratic burden on judges, who must sit on three member courts, but whose workload allows no genuine involvement in the making of all judgements handed down by three-member court; rather, the matters heard in a public hearing by the three-member court are split between the judges (semi-formally, by the appointment of a so-called reporting judge, i.e. a judge theoretically responsible for reading the case file more fully and reporting to the other judges), and each of them in effects makes a part of the judgements.

Two sides effects of this system for the organisation of first instance courts are perhaps not thought of as much as they should: the concomitant dissipation of judicial responsibility (neither good, nor less good, judges are readily recognisable), and the verifiability of objective impartiality by recourse to a judges prior rulings on matters of law. As the ECHR has held in a number of important decisions conflicting positions in the jurisprudence are only tolerable under art 6 ECHR to the extent they are inherent in geographically divided systems for the organisation of courts (and further provided that there are superior courts with the task of establishing the appropriate single and unitary position on such matters).

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14 See e.g. ECHR C 17056/06 Micalief v. Malta; C 47533/99 Ergin v Turkey.
15 See e.g. ECHR C 38155/02 Stefanica et al v Romania;C 63252/00 Paduraru v Romania, C 44698/06 and 29 others, Vincic v Serbia;
Cross-border insolvency: a test case in support of international harmonization of civil procedure laws

The formidable difficulties of achieving consensus towards, or of actually implementing, international harmonization of national procedural laws, one of the classical domains of sovereignty, are well understood and exemplified by the absence of international treaties, model laws and legislative guidance. This is in stark contrast with the extensive international harmonization of private substantive law, which has been particularly pervasive in Europe.

Verging as it does on both substantive and procedural law, cross border insolvency provides perhaps the strongest theoretical and practical arguments for revisiting the issue of harmonization of the rules of civil process: not only because insolvencies with cross border elements most frequently involve corporate groups, and are therefore "domestic" in the eyes of the forum, but also because any substantive insolvency law is only as efficient as the procedural framework for its application and enforcement.

A number of voices in Europe\(^{16,17}\) have long been advocating the need for European harmonization, primarily from a common market / elimination of barriers to intra-European trade perspective. Since the 1997 Treaty of Amsterdam (61 EC, now art 3§2 of the Treaty of the European Union), the Commission and the Council, in consultation with the European Parliament, have been mandated to gradually establish a European area of freedom, security and justice, and European Union harmonisation on this basis is already pervasive in the areas of recognition and enforcement (Brussels I & IIa, EIR), judicial co-operation, service of documents, taking of evidence, legal aid, and uniform European procedures (Small Claims and European Payment Order).

International harmonization initiatives, such as the \(ALI – Unidroit Principles of Transnational Civil Procedure\), embraced and in further development by Unidroit and the \(ELI\), exemplify the international concern with the issue of harmonisation, and the World Bank’s extensive work on the impact of the rule of law and of efficient justice systems on growth and development, underscores the importance of efficient and effective justice for the resolution of private disputes from a broader perspective.

The wisdom of fiscal austerity measures required of Greece over the past four years by its international emergency lenders is the subject of heated debate all across Europe and beyond. Much fewer people and organisations seem to have focused of the dire consequences on


\(^{17}\) One of the brightest minds of Greek and European civil procedure law, Professor Konstantine Kera- meus, had joined his voice in noting since 1999 that “[…] cross-border harmonisation of procedural laws […] becomes necessary whenever the various jurisdictions cooperate closely with each other or governments seek economic, social and/or political integration.” European Parliament, DG for Research Working Paper, “The Private Law Systems in the EU: Discrimination on Grounds of Nationality and the Need for a European Civil Code”, Legal Affairs Series Legal Affairs Series, JURI 103 EN (http://www.europarl.europa.eu/workingpapers/juri/pdf/103_en.pdf)
growth of inefficient and ineffective insolvency, creditor rights and civil procedure laws, in the fierce global competition for finance.

The EU, Greece's EU partners and international organisations with deep and proven understanding of the necessary parameters of rule of law and justice systems reform, would certainly be able to assist with this kind of much needed structural change.