Hermann Lutz v Elke Bäuerle
Case C-557/13 *Hermann Lutz v Elke Bäuerle, acting as liquidator of ECZ Autohandel GmbH* 16th April 2015
EU: Germany and Austria
European Court of Justice by Reference for a preliminary ruling

Key Words
Payment after opening of insolvency proceedings; rights *in rem*; a*ctio pauliana*; transaction avoidance; detrimental acts.

Summary of Facts of the Case

ECZ GmbH was a German company with its registered office in Tettnang (Germany). In order to trade in Austria, it used a subsidiary established in Bregenz (Austria). Mr Lutz purchased a car from the Austrian company and when the car was not delivered, he brought an action before the District Court in Bregenz, seeking reimbursement of the money. The District Court so ordered, issuing an enforceable payment order against that company. After the order had been made but before payment, the District Court in Ravensberg (Germany) opened insolvency proceedings against the debtor (subsidiary in Austria). The debtor's bank that had been attached by the court order paid Mr Lutz the specified money and the then liquidator of the company informed Mr Lutz that he was challenging both the enforcement authorised by the District Court in Austria and the payment that followed. This challenge was mounted in Ravensburg Regional Court, wherein the action brought by the liquidator was upheld. Mr Lutz then unsuccessfully appealed the decisions and appealed further a point of law to the German Federal Court of Justice.

The Federal Court of Justice referred the matter to the CJEU and sought clarification on 3 issues:

(i) Was Article 13 of the EIR applicable to a situation in which an attachment order made prior to the opening of insolvency proceedings was satisfied after the opening of insolvency proceedings?
- Article 13 provided that Article 4(2)(m) of the EIR did not apply where the person who benefited from an act detrimental to all the creditors provides proof that the act was subject to the law of a Member State other than that of the State of the opening of proceedings and that law did not allow any means of challenging that act.

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- Article 4(2)(m) provided that the law of the State in which proceedings were opened determined the rules relating to the voiding or unenforceability of legal acts detrimental to all the creditors.

(ii) If Article 13 of the EIR was applicable, did the defence under it also apply to limitation periods or other time-bars relating to actions to set aside transactions under the law which governs the dispute concerning the contested legal transaction (*lex causae*)?

(iii) If the reply to that question was also in the affirmative, were the relevant procedural requirements for asserting a claim for the purpose of Article 13 of the EIR also to be determined according to the *lex causae* or by the *lex fori concursus*?

Although it was not specifically posed as one of the three questions by the German Court to the CJEU, the issue of rights *in rem* did arise as it was one of the premises upon which the primary questions were based.

Cooperation and / or Coordination Issue

Rights *in rem* – which law takes precedence in matters concerning the avoidance of transactions; the law of the Member State in which the insolvency proceedings were opened or the law in which the transaction took place? From a coordination perspective, this is important as there may be situations in which similar transactions are treated differently within the same insolvency proceeding based on the relevant domestic rules. In *Hermann Lutz*, there was a substantial difference between the law in Germany and Austria vis-á-vis the limitation period for bringing an action to set a transaction aside; the former was three years and the latter was one.

Resolution

On the issue of rights *in rem*, the CJEU found that the right arising from the attachment of the bank accounts could constitute a right *in rem* provided that right was exclusive in relation to the other creditors of the debtor company under national law (Austria). This is because Article 5(2)(b) of the EIR stated "the exclusive right to have a claim met" when outlining some the particular rights referred to in Article 5(1). This, in conjunction with Recital 25 of the EIR – "[t]he basis, validity and extent of a right *in rem* should normally be determined according to the *lex situs"*, in other words, the law of the place in which the property is located, led the CJEU to come to the aforementioned conclusion. On the issue of whether the right *in rem* is automatically invalidated as a result of the opening of insolvency proceedings against the debtor, Article 5(4) of the EIR excluded the application of Article 5(1) only in the case of an 'action' for voidness, voidability or unenforceability as referred to in Article 4(2)(m). With that said, per the Advocate General's opinion, 'actions' in that article should not be read as limited solely to 'court actions'. Instead, it should be in conjunction with Article 4(2)(m), which refers to 'rules'. Thus, the competent *lex fori concursus* (law of the State of the opening of proceedings) was relevant in determining the rules relating to voidness, voidability or unenforceability (Article 4(2)(m)). So, while Article 4(2)(m) of the EIR provides that the *lex fori concursus* determines the rules relating to the voidability of legal acts detrimental to all the creditors, Article 13 allows an exception to that rule, since it rules out the application of Article 4(2)(m) and applies the law governing the act challenged by the liquidator ('the *lex causae*'), when certain conditions are satisfied. In summary, the CJEU determined that the question for the German Federal Court of Justice was whether the application of Paragraph 88 of the InsO (the automatic invalidity of the attachment of the bank accounts) is not excluded because of the application of Austrian law under Article 13 of the EIR.

With regard to the three questions posed by the Federal Court of Justice, the CJEU came to the following conclusions:

(i) Article 13 of the EIR applies to a situation in which a payment, which was challenged by an insolvency administrator, was attached before the opening of the insolvency proceedings was made after the opening of those proceedings.

(ii) The defence established in Article 13 of the EIR also applies to limitation periods or other time-bars relating to actions to set aside transactions under the law governing the act challenged by the liquidator.

(iii) For the purposes of the application of Article 13, the relevant procedural requirements for the exercise of an action to set a transaction aside are to be determined according to the law governing the act that is challenged by the liquidator.

Applicability to Preventive Restructuring

Given that one of the primary issues related to whether the opening of insolvency proceedings voided an attachment of bank accounts, *Hermann Lutz* is applicable in the context of preventive restructuring. Furthermore, an inability to supply a product that has been purchased by a consumer would not be unusual for a business in or near to entering insolvency.

Actions in relation to the avoidance of transactions entered into prior to insolvency may not be as prevalent in preventive restructuring procedures given the nature of those proceedings occurring notionally *prior to functional insolvency.* However, if a restructuring framework is included in Annex A it will equally benefit from the potential exceptions under what is now Article 16 of the EIR Recast in relation to detrimental acts, giving scope for disputes that might fall within the definition.

Further, where there is an *actio pauliana* in relation to a transaction connected to a restructuring, but not directly a part of a procedure falling within the scope of Annex A of the EIR Recast, this and other cases such as *Trachte, Feniks,* and *BNP Paribas* seem to indicate that courts will find such actions as falling outside of the insolvency procedure and being covered instead by the Brussels Regulation or other Conventions or Regulations where relevant, potentially splintering a process among multiple courts.

Applicability of Existing Rules and Guidelines

The EIR Recast

First and foremost, as the EIR was interpreted to mean that a bank account to which there was an attachment could be subject to a right *in rem*, so too would the EIR Recast. The wording is virtually the same in both articles. The wording of Article 13 of the EIR, which Mr Lutz relied upon in this case, did not change either when the EIR was recast (it is now Article 16). The same is true for Article 4(2)(m) – now Article 7(2)(m) – in that there have been no changes to the Article. Thus, were a similar case to arise in the future it would likely hinge on point (iii) of the CJEU judgment, as laid out above; in other words, the procedural requirements for the setting aside of a transaction under the EIR (Recast) are dictated by the law that governs the act that is being challenged (by the liquidator), which in cross-border matters is may well not to be the state in which the primary proceedings have been opened, as was the case in *Hermann Lutz*.

In a broader since, there is some significance to this. The EIR Recast and its predecessor have allowed a situation where a particular action – in this case an Article 16 (formerly Article 13) action – is governed by the law of a Member State in which there are no insolvency proceedings opened and regardless of where primary proceedings are being conducted. It is key to state, however, that in *Hermann Lutz* the court had ordered payment before the commencement of insolvency proceedings; thus, were it occurring today, there would be no opportunity for Austrian court to co-operate under the EIR Recast, as the Austrian proceedings had already concluded. Furthermore, there was no opportunity for the Austrian court to consider the appropriateness of making such an order in light of ongoing insolvency proceedings in another jurisdiction, as those proceedings had not yet started. Moreover, there was clearly no stay of individual enforcement in place. Still, the ruling that the law of a Member State in which insolvency proceedings are not being opened to dictate an action that may impact on those proceedings may well weaken and undermine the concept of cross border co-ordination. As a result, the Regulation may have created a category of cases that are exceptions to the broader principle of co-ordination and co-operation. Thus, the decision also gives credence to the importance of the *principles* of cooperation that should permeate all levels of EU regulation wherever there is a cross-border element to consider.