

## Rethinking Insolvency Fragmentation in the EU

### A structural reform strategy for capital market integration

Anastasia Kotowski



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The European Union continues to face significant fragmentation in insolvency law, despite decades of market integration. While cross-border business activity has intensified, insolvency regimes remain largely national, producing legal uncertainty, higher transaction costs, and inconsistent outcomes in complex cases. At the same time, full-scale harmonisation faces political and legal constraints. This cepStudy proposes a four-pillar strategy to reduce fragmentation in a legally feasible, economically sound, and politically realistic manner:

- ▶ **Pillar 1 – Targeted harmonisation:** Instead of comprehensive codification, the EU should focus on selective alignment of key friction points where cross-border spillovers are strongest and subsidiarity can be satisfied.
- ▶ **Pillar 2 – Systemic stability through financial market regulation:** Strengthening EU prudential supervision and resolution mechanisms indirectly stabilises insolvency outcomes by reducing disorderly failures and mitigating systemic spillovers.
- ▶ **Pillar 3 – Transparency and soft law:** A European Insolvency Portal, harmonised performance indicators, and model frameworks (i.e. for SME restructuring) can reduce information asymmetries and foster convergence.
- ▶ **Pillar 4 – An optional “28th Regime”:** For complex cross-border cases, the EU should establish an optional European insolvency regime. This regime would complement, not replace, national systems, offering predictability for multinational corporate groups while preserving regulatory diversity for domestic cases.

Rather than pursuing uniformity for its own sake, the proposed strategy combines convergence, transparency, supervisory integration, and regulatory choice. This balanced approach strengthens the Capital Markets Union while respecting constitutional limits and Member State sovereignty.

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## 1 Introduction

Insolvency law plays a critical role in shaping the financial and economic landscape of the European Union (EU). Corporate insolvency crises carry substantial long-term repercussions, potentially resulting in diminished employment, economic growth, and overall economic performance and financial depth. Robust insolvency procedures are one of the key instruments to mitigate those risks in the long run. Insolvency law determines how distressed businesses are handled, whether they are liquidated or restructured, and how assets and liabilities are distributed among creditors. The importance of insolvency law in promoting efficient capital allocation, supporting economic recovery, and fostering sustainable growth cannot be overstated.<sup>1</sup> Beyond its allocative function, insolvency law also serves a crucial incentive-setting role. Well-designed insolvency frameworks encourage responsible risk-taking, facilitate access to finance, and promote timely restructuring of viable businesses, while ensuring the orderly exit of non-viable firms.<sup>2</sup> Particularly in times of economic stress, insolvency systems must possess sufficient procedural capacity and institutional resilience to manage an increased volume of cases without undermining legal certainty or value preservation.

Despite reform efforts at the national and EU level<sup>3</sup>, significant deficiencies persist within the fragmented insolvency landscape of the EU.<sup>4</sup> Divergent national rules on restructuring tools, creditor priorities, procedural design, and asset recovery continue to generate legal uncertainty, increase transaction costs, and discourage cross-border investment.<sup>5</sup> These shortcomings pose structural obstacles to the completion of the Capital Markets Union (CMU) and the effective functioning of the internal market.<sup>6</sup> The approximation of certain aspects of national corporate insolvency laws is considered as a necessary step toward deeper market integration.

This cepStudy analyses the evolution and scope of EU action in the field of insolvency law, with particular attention to recent legislative initiatives aimed at targeted harmonisation of corporate insolvency rules. This cepStudy identifies the principal legal and political barriers to comprehensive insolvency harmonisation and, on that basis, proposes an alternative and more differentiated regulatory strategy that supports. The proposed four-pillar approach includes: (i) targeted and realistic harmonisation of core insolvency rules; (ii) the indirect convergence of insolvency outcomes through enhanced financial market regulation; (iii) strengthened transparency, information, and coordination mechanisms; and (iv) the introduction of an optional, voluntary European insolvency regime (the so-called “28th regime”) for cross-border cases.

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<sup>1</sup> European Parliament (2010), Harmonisation of insolvency law at EU level, Study, Policy Department C - Citizens' Rights and Constitutional Affairs, p.7.

<sup>2</sup> UNCITRAL Model Law on Cross-Border Insolvency (1997).

<sup>3</sup> Proposal for a Directive of the European Parliament and of the Council harmonising certain aspects of insolvency law, COM/2022/702 final.

<sup>4</sup> European Commission (2020), Capital markets union 2020 action plan: A capital markets union for people and businesses, Action 11.

<sup>5</sup> European Parliament (2025), Report on the proposal for a directive of the European Parliament and of the Council harmonising certain aspects of insolvency law (COM(2022)0702 – C9-0410/2022 – 2022/0408(COD)), Recital 2.

<sup>6</sup> See Conclusions of The European Council of 17-18 April 2024.

## 2 The unresolved challenge of insolvency law fragmentation in the EU

### 2.1 Fragmentation as a persistent barrier to economic integration

The fragmentation of insolvency law across the EU poses substantial challenges for businesses operating across borders and influences overall efficiency and predictability of insolvency proceedings.<sup>7</sup> Disparate national frameworks create legal uncertainty, increase procedural costs and delays, and diminish the recovery rates for creditors. These inefficiencies undermine the EU's goal of creating a unified internal market and negatively impacts cross-border business operations, foreign investments, and economic growth within the EU.

Insolvency proceedings within the EU vary significantly, with durations ranging from 1.5 to 3.5 years compared to an OECD average of 1.7 years.<sup>8</sup> This prolonged process erodes the value of insolvent estates due to the "ice cube melting" effect: the longer a proceeding drags on, the more the value of the insolvent entity's assets diminishes.<sup>9</sup> This happens because business assets lose value over time, especially in industries that rely on intellectual property or technology. Consequently, creditors recover less from the insolvency estate, and viable parts of businesses may be lost due to unnecessary delays in resolution. The value of recoveries is therefore directly tied to the speed and efficiency of insolvency proceedings.<sup>10</sup> Inconsistent treatment of creditor claims across jurisdictions can also lead to unequal or unfair outcomes for creditors depending on where the insolvency case is filed. Lengthy and costly insolvency procedures keep resources tied up in unproductive businesses (often called as "zombie companies") which continue to operate despite being financially unsustainable.<sup>11</sup> These companies expose banks to non-performing loans (NPLs), which reduce the availability of credit for other, innovative and growing businesses.<sup>12</sup> Zombie companies distort competition and prevent the reallocation of capital and other resources to more productive uses.<sup>13</sup> Additionally, court costs often reach 9% to 15% of the estate's value, further exacerbating losses.<sup>14</sup> Court costs in the EU are also disproportionately high, compared to 5% in the most efficient non-EU countries.<sup>15</sup>

Cross-border insolvencies are particularly problematic. They often require navigating multiple legal regimes, each with different rules on creditor rankings, asset distribution, and procedural

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<sup>7</sup> Eidenmüller H. (2011), *The Transnational Law Market, Regulatory Competition, and Transnational Corporations*, *Indiana Journal of Global Legal Studies* 18 (2011), pp. 707, 724-725.

<sup>8</sup> *Doing Business* (2009), World Bank-IFC report: *Closing a Business*; European Commission (2022), *Impact Assessment Report accompanying the document Proposal for a Directive of the European Parliament and of the Council harmonising certain aspects of insolvency law* {COM(2022) 702 final} - {SEC(2022) 434 final} - {SWD(2022) 396 final}, p. 21.

<sup>9</sup> European Commission (2022), *Impact Assessment Report accompanying the document Proposal for a Directive of the European Parliament and of the Council harmonising certain aspects of insolvency law* {COM(2022) 702 final} - {SEC(2022) 434 final} - {SWD(2022) 396 final}, p. 9.

<sup>10</sup> European Law Institute (2017), *Rescue of Business in Insolvency Law*, p. 290.

<sup>11</sup> OECD (2017), *Insolvency regimes, zombie firms and capital reallocation*, Economics department working papers No. 1399, ECO/WKP(2017)31.

<sup>12</sup> Campbell A. (2007), *Bank insolvency and the problem of nonperforming loans*. *J Bank Regul* 9, p. 25-45.

<sup>13</sup> European Systemic Risk Board (2021), *Preventing and managing a large number of corporate insolvencies*, April.

<sup>14</sup> European Commission (2022), *Impact Assessment Report accompanying the document Proposal for a Directive of the European Parliament and of the Council harmonising certain aspects of insolvency law* {COM(2022) 702 final} - {SEC(2022) 434 final} - {SWD(2022) 396 final}, p. 21.

<sup>15</sup> Bork R. & Mangano R. (2022), *European Cross-Border Insolvency Law* (2nd ed., Oxford University Press, 2022). P. 201.

requirements. Businesses face conflicting laws, divergent creditor priorities, and inconsistent procedural requirements, leading to increased costs and administrative burdens.<sup>16</sup> Fragmentation in insolvency laws also poses obstacles to the restructuring and recovery of distressed businesses, particularly those operating as part of corporate groups across multiple member states.<sup>17</sup> National insolvency laws often focus on the treatment of individual entities rather than considering the needs of corporate groups as a whole. This can prevent the effective reallocation of liquidity within a group and limit intra-group support measures, both of which are critical during times of financial distress. For instance, the inability to transfer funds between group entities due to legal restrictions in certain member states can hinder a successful restructuring strategy. As a result, it can lead to the unnecessary liquidation of viable parts of the business.

Moreover, different EU states have different approaches in insolvency outcomes. For instance, one member state may prioritise restructuring and recovery, while another may emphasise liquidation and creditor protection.<sup>18</sup> These discrepancies can delay the resolution of cross-border insolvencies and create situations where businesses and creditors are unsure of their rights, which undermines the predictability of outcomes. This fragmentation reduces confidence in the EU as a stable environment for investment and impedes the effective restructuring of multinational enterprises. Moreover, foreign investors may be hesitant to invest in EU-based businesses, particularly those operating in multiple member states, due to the unpredictability of insolvency outcomes and the complexity of national insolvency laws.<sup>19</sup> Investors prefer jurisdictions where insolvency procedures are transparent, allowing them to assess risks accurately and recover their investments in the event of financial distress. This complexity may also hinder the ability of failing businesses to access cross-border financing, as creditors become wary of the legal and procedural barriers they may face in different jurisdictions. The resulting reduction in foreign investment can slow economic growth and limit the development of the EU's single market.<sup>20</sup>

These structural deficiencies are increasingly problematic in the context of the CMU.<sup>21</sup> A central objective of the CMU is to facilitate the free flow of capital across Member States by reducing regulatory and legal barriers to cross-border investment. Yet European capital markets remain largely nationally segmented, and differences between Member States' legal frameworks are in many respects more pronounced than the transatlantic differences between Europe and the United States.<sup>22</sup> From a CMU

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<sup>16</sup> European Court of Auditors (2020), Special Report 25/2020: Capital Markets Union – Slow start towards an ambitious goal.

<sup>17</sup> European Parliament (2025), Report on the proposal for a directive of the European Parliament and of the Council harmonising certain aspects of insolvency law. 1.7.2025 - (COM(2022)0702 – C9-0410/2022 – 2022/0408(COD)).

<sup>18</sup> Lynch-Fannon I., Gant J.L., Finnerty A. (2022), Corporate recovery in an integrated Europe: harmonisation, coordination and judicial cooperation. Edward Elgar Publishing, Northampton, MA, p. 247.

<sup>19</sup> European Commission (2015), Initial reflections on the obstacles to the development of deep and integrated EU capital markets, SWD(2015) 13 final, , p. 19.

<sup>20</sup> Leea S.-H, Yamakawab Y., Penga M.W., Barneyc J.B. (2001), How do bankruptcy laws affect entrepreneurship development around the world?

<sup>21</sup> Draghi M. (2018), Risk-reducing and risk-sharing in our Monetary Union, Speech at the European University Institute, Florence, 11 May 2018.

<sup>22</sup> Ghio, E. (2017), The EU Incremental Approach to Cross-Border Insolvency Regulation: a Critical Analysis, 28 International Company and Commercial Law Review 369.

perspective, predictable and efficient insolvency regimes are a precondition for integrated capital markets, as insolvency law ultimately determines the downside risk faced by investors and creditors.<sup>23</sup>

Despite the growing recognition of insolvency law as a key enabler of the CMU, progress towards harmonisation in this area has long remained limited.<sup>24</sup> While recent years have seen increased political attention, insolvency reform has advanced more slowly than other CMU-related measures. This asymmetry is not accidental. Amending EU financial market regulation is institutionally and politically easier than harmonising national insolvency and contract laws. The EU enjoys clear treaty-based competences in financial regulation, supported by a dense body of secondary legislation and long-established supervisory frameworks. By contrast, insolvency and contract law remain deeply embedded in national legal traditions and closely linked to domestic economic and social policies. Harmonisation in these areas directly touches upon sensitive issues of national sovereignty, creditor-debtor balances, and social policy choices. Whereas financial regulation often involves technical adjustments to an already integrated framework - such as capital adequacy, disclosure standards, or market infrastructure - insolvency law reform requires Member States to reconsider foundational aspects of their private law systems.

Against this background, the continued fragmentation of insolvency law emerges not merely as a technical legal problem but as a systemic constraint on the completion of the internal market and the realisation of the CMU.

## 2.2 Potential economic gains from reducing fragmentation

Reducing the fragmentation of insolvency regimes across the EU offers substantial economic and legal benefits. A more coherent European insolvency landscape would strengthen the functioning of the internal market by addressing uncertainties that currently arise from widely divergent national rules.<sup>25</sup>

A less fragmented environment would generate several key advantages:

- 1) **Improved recovery outcomes:** Greater coherence between national procedures would help limit the erosion of asset value during cross-border insolvencies and reduce procedural delays.<sup>26</sup> Clearer and more coordinated rules would support quicker stabilisation of distressed entities, thereby increasing the returns available to creditors and reducing systemic disruptions.<sup>27</sup>

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<sup>23</sup> European Parliament, (2010), Note of the Directorate-General for Internal Policies, Policy Department Citizens' Rights and Constitutional Affairs (C), Legal and Parliamentary Affairs (No. PE 419.633), "Harmonisation of Insolvency Law at EU level".

<sup>24</sup> European Commission (2022), Impact Assessment Report accompanying the document Proposal for a Directive of the European Parliament and of the Council harmonising certain aspects of insolvency law {COM(2022) 702 final} - {SEC(2022) 434 final} - {SWD(2022) 396 final}, p. 38.

<sup>25</sup> André C. and Demmou L., (2022) Enhancing insolvency frameworks to support economic renewal, OECD Economics Department Working Papers, No. 1738, Organisation for Economic Co-operation and Development (OECD), December.

<sup>26</sup> Degryse H., Ioannidou V., Liberti J. M. and Sturgess, J. (2014), When Do Laws and Institutions Affect Recovery Rates on Collateral?

<sup>27</sup> Kliatskova T., Savatier L. B., Schmidt, M. (2023), Insolvency regimes and cross-border investment decisions, Journal of International Money and Finance, Volume 131, 2023, 102795, ISSN 0261-5606.

- 2) **Increased investor confidence:** A more predictable insolvency landscape would enhance legal clarity and risk assessment, making the EU a more attractive destination for both internal and external investment.<sup>28</sup>
- 3) **More efficient allocation of capital:** When insolvency outcomes become more predictable and burdensome conflicts between national laws are reduced, capital can flow more readily to productive firms.<sup>29</sup> Efficient exit and restructuring mechanisms ensure that unviable businesses leave the market swiftly while viable firms can reorganise, strengthening innovation and competitiveness across the EU.
- 4) **Stronger restructuring prospects:** A reduction in regulatory fragmentation would support earlier and more coordinated restructuring efforts, especially for corporate groups operating in multiple jurisdictions.<sup>30</sup> Clearer pathways to negotiate restructuring plans across borders would help preserve economic activity, protect jobs, and reduce the broader social costs of business failure.

### 3 Harmonisation of insolvency law in the EU

#### 3.1 General stand

In the EU, insolvency law primarily remains under the jurisdiction of individual Member States. Harmonisation at the EU level is mostly reserved for issues arising in international cases, i.e., those affecting more than one Member State. These areas include conflict-of-law rules, the extraterritorial application of insolvency proceedings, and rules for determining the competent courts and applicable law in such proceedings. Furthermore, it includes the mutual recognition and enforcement of insolvency decisions across Member States, facilitating the efficient resolution of cross-border insolvency cases.

A further difficulty lies in the absence of harmonised fundamental legal concepts.<sup>31</sup> Key terms, such as “insolvency,” “likelihood of insolvency,” “secured claim,” “reorganisation plan,” or “commercial transaction”, have no uniform meaning across the Union. For instance, the Preventive Restructuring Directive<sup>32</sup> deliberately refrained from defining “insolvency,” thereby preserving national discretion, but at the cost of making substantive convergence practically impossible. This approach underscores the importance of maintaining Member States' sovereignty in this sensitive area, while also enhancing the efficiency and coherence of handling cross-border insolvency matters.<sup>33</sup> The balance between national

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<sup>28</sup> European Parliament Research Service (2023), Harmonisation of Insolvency Law in the EU: State of Play and Policy Options (EPRS Briefing, 2023), assessable under [https://www.europarl.europa.eu/Reg-Data/etudes/BRIE/2023/745671/EPRS\\_BRI\(2023\)745671\\_EN.pdf](https://www.europarl.europa.eu/Reg-Data/etudes/BRIE/2023/745671/EPRS_BRI(2023)745671_EN.pdf).

<sup>29</sup> Banque de France (2023), Speeding up the process of harmonising European insolvency law to strengthen financial integration, Bulletin de la Banque de France. 249/3 - November-December 2023.

<sup>30</sup> International Monetary Fund (2021), Restructuring and Insolvency in Europe: Policy Options in the Implementation of the EU Directive (IMF Working Paper WP/21/144), assessable under <https://www.imf.org/en/Publications/WP/Issues/2021/05/27/Restructuring-and-Insolvency-in-Europe-Policy-Options-in-the-Implementation-of-the-EU-50235>

<sup>31</sup> Enriques L. (2017), A harmonised European company law: are we there already? *International & Comparative Law Quarterly* 66, p. 771.

<sup>32</sup> Directive (EU) 2019/1023 on preventive restructuring frameworks (2019), OJ L172/18.

<sup>33</sup> Wessels B. (2016), The Place of Insolvency Law in the European Union Legal Order, *13 European Company and Financial Law Review* 573, p. 75.

autonomy and supranational coordination defines the existing legal landscape of insolvency law within the EU.

### 3.2 Historical overview of the harmonisation efforts

The journey towards the harmonised insolvency regulation approach in the EU began in the early 1960s with attempts to unify international insolvency law among member states. The focus was primarily on international cases, addressing issues such as international jurisdiction, conflict of laws, and the extraterritorial application of national laws.<sup>34</sup>

The Treaty establishing the European Economic Community (1957) played a pivotal role by including an obligation for member states under Article 220 to conclude agreements on “the formalities governing the reciprocal recognition and execution of judicial decisions”. This clause was broadly interpreted to encompass insolvency law matters. However, despite this foundation, member states did not succeed in concluding a comprehensive convention on these matters.

Throughout the 1970s and 1980s, there were ambitious attempts by the European Commission to draft a “Convention on bankruptcy.”<sup>35</sup> These drafts aimed at comprehensive harmonisation but ultimately failed due to legal complexities and disagreements among member states. In 1995, a less ambitious and overly simplified attempt to create an EU Convention on insolvency proceedings was made.<sup>36</sup> However, that project was also unsuccessful, this time due to political reasons.<sup>37</sup>

A breakthrough occurred in 2000 with the adoption of the EU Regulation on Insolvency Proceedings<sup>38</sup>, which closely mirrored the 1995 draft.<sup>39</sup> This regulation aimed to provide a framework for cross-border insolvency proceedings and finally entered into force in 2015. This marked a significant step in the journey toward harmonising insolvency laws across the EU, although it primarily addressed procedural aspects rather than substantive law.

Efforts to harmonise substantive insolvency law have been ongoing since 2000 but have met with limited success. Key milestones include the report by INSOL Europe<sup>40</sup> to the European Parliament and the EU Parliament resolution with recommendations on insolvency proceedings within the context of EU company law.<sup>41</sup> These efforts aimed to create a more cohesive legal framework but did not result in comprehensive harmonisation.<sup>42</sup>

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<sup>34</sup> Fletcher I. F. (2023), Historical Overview: The Drafting of the Insolvency Proceedings Regulation and Its Precursors, in Tom Smith K.C., Stuart Isaacs K.C., and Christoph Paulus (eds), *Moss, Fletcher and Isaacs on The EU Regulation on Insolvency Proceedings*, 4th Edition (2023), p. 1-15.

<sup>35</sup> European Commission (1982), Commission Opinion of 10 December 1981 on the draft Convention on bankruptcy, winding-up, arrangements, compositions and similar proceedings (81 / 1068/EEC).

<sup>36</sup> Banque de France (2023), Speeding up the process of harmonising European insolvency law to strengthen financial integration, *Bulletin de la Banque de France*. 249/3 - November-December 2023.

<sup>37</sup> Jokubauskas, R. (2024), *Cross-Border Insolvency Proceedings Policies and Directives in the European Union*. p. 7.

<sup>38</sup> Regulation (EU) 2015/848 on Insolvency Proceedings (2015), OJ L141/19.

<sup>39</sup> Torremans, P. (2002), *Cross Border Insolvencies in EU, English and Belgian Law*, Wolters Kluwer.

<sup>40</sup> European Commission, Study on a new approach to business failure and insolvency – Comparative legal analysis of the Member States’ relevant provisions and practices (submitted by INSOL Europe), 2014.

<sup>41</sup> Commission Recommendation on a new approach to business failure and insolvency, 12 March 2014, C(2014) 1500 final.

<sup>42</sup> Wessels B. (2012), On the Future of European Insolvency Law, *The Academic Forum of INSOL Europe*. P. 16.

Notable progress has been made in peripheral areas of insolvency law. Existing framework - most notably the European Insolvency Regulation (EIR) and the Restructuring Directive - has improved the handling of cross-border cases and pre-insolvency restructuring, yet they leave core elements of substantive insolvency law largely within Member State competence.<sup>43</sup> EIR established a unified EU framework for dealing with cross-border insolvency proceedings by coordinating national insolvency laws rather than harmonising their substance. Its core content consists of rules on international jurisdiction, based on the debtor's centre of main interests (COMI),<sup>44</sup> the applicable law to insolvency proceedings, and the automatic recognition of insolvency proceedings opened in one Member State throughout the EU. The Preventive Restructuring Directive<sup>45</sup> introduced a significant shift in EU insolvency policy by focusing on early intervention and business rescue rather than ex post liquidation. Its central objective is to enable financially distressed but viable businesses to restructure at an early stage, before formal insolvency proceedings become unavoidable, thereby preserving economic value, employment, and entrepreneurial activity. Rather than harmonising insolvency law in a comprehensive manner, the Preventive Restructuring Directive pursues targeted substantive convergence in a pre-insolvency context.<sup>46</sup> Its implementation marks an important step towards a more rescue-oriented insolvency culture within the EU, while leaving significant discretion to Member States. These steps indicate a gradual but piecemeal approach to harmonising insolvency law within the EU.<sup>47</sup> Therefore, divergent national rules on insolvency triggers, avoidance actions, claim ranking, and asset realisation continued to create legal uncertainty and uneven outcomes in cross-border scenarios.

The latest phase of EU insolvency-law harmonisation is characterised by a clear shift from purely coordination-based instruments toward targeted substantive convergence, driven primarily by the objectives of the CMU. Whereas earlier initiatives focused on judicial cooperation and cross-border procedural rules, current efforts explicitly seek to reduce legal fragmentation that impedes the free movement of capital and undermines investor confidence. This policy reorientation is embedded in the CMU Action Plans of 2015 and 2020. The Commission no longer frames harmonisation as a qualitative improvement of national insolvency systems but as a necessary precondition for efficient capital allocation within the internal market. In this context, Action 11 of the 2020 CMU Action Plan announced legislative measures to enhance the predictability of insolvency outcomes. These efforts resulted in the Commission's proposal of 7 December 2022 for a Directive harmonising selected aspects of insolvency law<sup>48</sup> that was politically agreed between the European Parliament and the Council on 20 November 2025.<sup>49</sup>

The Directive targets three key aspects of corporate insolvency law. First, it enhances asset recovery by introducing minimum harmonised standards on avoidance actions, thereby protecting the

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<sup>43</sup> Magnus U. (2025). European Insolvency Regulation 2015, De Gruyter. Pp. 66.

<sup>44</sup> Wessels, B. (2003), International Jurisdiction to open Insolvency Proceedings in Europe, in particular against (groups of) Companies, Working Paper Series No. 17, p. 7.

<sup>45</sup> Directive (EU) 2019/1023 on preventive restructuring frameworks (2019), OJ L172/18.

<sup>46</sup> van Zwieten, K. (2014), Restructuring law: recommendations from the European Commission, Law in Transition, pp. 1-9.

<sup>47</sup> Moustaira E. (2019), International Insolvency Law, pp. 47-72.

<sup>48</sup> European Commission (2022), Proposal for a Directive of the European Parliament and of the Council Harmonising Certain Aspects of Insolvency Law COM(2022) 702 final (7 December 2022).

<sup>49</sup> Council of the European Union (2025), Insolvency Proceedings: Council and European Parliament Reach Political Agreement (Press Release, 20 November 2025), assessable under <https://www.consilium.europa.eu/en/press/press-releases/>.

insolvency estate and reducing disparities in creditor protection across Member States. Secondly, it seeks to improve procedural efficiency through rules on asset tracing, enabling insolvency practitioners and courts to better identify and recover assets, particularly in cross-border cases. Thirdly, it promotes a more predictable and equitable distribution of value by strengthening collective creditor participation, notably through the introduction of creditors' committees in complex proceedings.

In addition, the Directive establishes a common framework for pre-pack proceedings, facilitating the sale of a debtor's business as a going concern within liquidation and aiming to maximise value and preserve employment, while introducing safeguards against abuse. More broadly, the Directive reflects a targeted approach to harmonisation, introducing minimum standards in areas most relevant to cross-border investment without displacing national insolvency systems.

Whereas this reform shows moving beyond procedural coordination towards substantive convergence in carefully selected sub-areas of insolvency law, the proposal deliberately follows a minimum-harmonisation approach. Full substantive harmonisation was explicitly avoided, reflecting the deep interconnection of insolvency law with national company, property, labour, and procedural laws. Political negotiations confirmed these limits. For instance, the Council removed the proposed harmonised microenterprise liquidation regime, demonstrating Member States' strong resistance to EU intervention in domestically sensitive insolvency structures. Other elements, such as avoidance actions and asset tracing, were retained only as minimum standards, leaving room for national divergence.

The latest EU insolvency law reform is undoubtedly a milestone for the harmonisation of insolvency law in the EU and a victory for the targeted, incremental approach. However, the difficult negotiations, and particularly the complete removal of the chapter on simplified procedures for microenterprises, prove that this approach alone is not enough. This selective harmonisation strategy reflects a broader structural reality: not all components of insolvency law are equally suitable for EU-level regulation. Procedural coordination, avoidance rules, asset tracing, and cross-border mechanisms lend themselves to harmonisation, whereas asset distribution, creditor hierarchies, and debtor governance remain closely tied to national legal traditions and social policy choices.

The emerging framework is therefore a hybrid architecture combining minimum EU standards with national flexibility. The current reform thus confirms the necessity of a differentiated governance model. EU-level intervention can enhance predictability, reduce transaction costs, and support cross-border investment where fragmentation is most harmful.

#### **4 Political and legal barriers to harmonisation**

While the EU has made significant efforts in addressing certain aspects of insolvency law, particularly in cross-border cases, the design of the substantive insolvency law remains within the mandate of the Member States. Consequently, insolvency laws vary widely across Europe, reflecting different policy objectives and legal cultures. As such, the ongoing disparities and challenges underscore the need for continued efforts towards greater cooperation in this critical area of law.<sup>50</sup>

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<sup>50</sup> EU Commission Action plan der Kommission 24.9.2020, COM(2020) 509 final, p. 16.

The European Commission has frequently emphasized the importance of creating a strong CMU, aspiring to replicate the success of the U.S. capital markets.<sup>51</sup> However, the U.S. model is not directly transferable to Europe due to inherent differences in systems. American federalism accommodates variations across jurisdictions, while the European framework must account for the distinct characteristics of its Member States. Consequently, the CMU cannot merely imitate the U.S. model but must reflect the unique features of the European capital market.

Harmonising insolvency law in the EU faces significant political, economic, and cultural challenges.<sup>52</sup> While a greater uniformity could bring benefits, achieving this goal requires navigating entrenched national interests, legal traditions, institutional persistence, and political-economic disincentives.

#### 4.1 The clash of legal traditions and cultures

Despite the numerous efforts towards a harmonised approach to insolvency in the EU, political resistance to the harmonisation is still strong, rooted in the sovereignty of member states and the diversity of legal traditions. Each of these traditions approaches insolvency differently, from the process of filing for bankruptcy to the hierarchy of claims.<sup>53</sup> Insolvency laws are in fact deeply connected to broader legal and social systems, reflecting national values and policy priorities. These laws intertwine with broader legal principles and cultural attitudes towards debt, financial failure, and business restructuring. Consequently, even seemingly similar legal systems may exhibit substantial differences in specific insolvency provisions.<sup>54</sup>

For example, some countries prioritize protecting creditors' rights, while others emphasize preserving jobs or ensuring fairness in the distribution of a company's remaining assets. For example, creditor-friendly regimes in Germany and the Netherlands may resist adopting debtor-oriented reforms similar to those in France or Italy.<sup>55</sup> Member States that adopt debtor-friendly approaches are focussed on restructuring and recovery and prioritize preserving jobs and business continuity, while others tend to liquidation and stronger creditor protection. These differences complicate efforts to establish uniformity, as legal traditions are deeply ingrained and politically sensitive.

Economic structures across the EU also vary widely, influencing attitudes toward insolvency law. Some countries rely heavily on small and medium-sized enterprises (SMEs), while others have a larger presence of multinational corporations. Harmonised insolvency laws may not address the needs of all economies equally, raising concerns that reforms could disproportionately benefit certain countries. For

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<sup>51</sup> See COM (2015) 63 final, p. 2; COM (2015) 468 final, p. 4.

<sup>52</sup> Burdette D., Kastrinou A. and Omar P. (2017), Benchmarking Insolvency Practice Frameworks: The Challenge of Creating Norms, In: Gant, J. (2017). Harmonisation of European Insolvency Law. p. 235.

<sup>53</sup> Valiante D. (2016), Harmonising insolvency laws in the euro area: rationale, stock taking and challenges. What role for the eurogroup?, European Parliament, PE 574.428, July.

<sup>54</sup> Boon G.-J. & Madaus S. (2017), Toward a European Business Rescue Culture, in: Adriaanse J. and van der Rest J.-P. (eds), Turnaround Management and Bankruptcy, New York: Routledge.

<sup>55</sup> Davydenko S. & Franks J. R. (2008), Do Bankruptcy Codes Matter? A Study of Defaults in France, Germany, and the U.K., The Journal of Finance 63 (2008), p. 565.

example, Southern European nations might fear that creditor-friendly rules would disadvantage their debtor-reliant economies.

Full harmonisation would require countries to cede control over a critical area of their legal framework, which many are reluctant to do. This reluctance is especially pronounced in member states with well-established insolvency traditions, which fear that harmonisation would force them to adopt less favorable or less effective rules. In some countries, insolvency law reforms may be perceived as benefiting foreign creditors or large corporations at the expense of local businesses and workers, making it a politically sensitive issue.

For instance, avoidance laws, which allow for reversing certain transactions prior to insolvency, vary significantly across the EU. Dutch law minimally addresses avoidance, whereas Germany and Austria<sup>56</sup> have comprehensive regulations for transactions made up to ten years before insolvency. Harmonising these divergent systems demands political and legal alignment far more complex than revising financial market rules. The Wirecard scandal illustrates how courts in different countries interpret avoidance laws differently, underscoring the challenges of achieving uniformity.

Against this background, even more scepticism arises about the feasibility of comprehensive harmonisation.<sup>57</sup> Adopting of new EU directives might not significantly improve the existing landscape, as member states' differing interpretations and implementations will continue to pose challenges.<sup>58</sup> Achieving a true harmonisation indeed requires more significant compromises and a nuanced understanding of the legal and cultural contexts of member states. Furthermore, such harmonisation only makes sense within specific contexts, such as the CMU, where the focus is on whether certain market participants' duties apply in insolvency proceedings.<sup>59</sup>

## 4.2 National economic interests and sovereignty concerns

In the context of cross-border insolvency, member states may have a vested interest in regulating the insolvency proceedings under the national legislation, especially if the involved parties have a significant impact on the local economy due to their size or the nature of their economic activities. The reasons for that are stemming from the willingness for the protection of domestic creditors, the preservation of national sovereignty and local economic stability. Insolvency law is deeply intertwined not only with the national legal system but also with economic and social objectives in broader sense.<sup>60</sup> Additionally, national insolvency laws are tied closely with the contract law. The law must address the failure of a business plan in a way that minimizes significant impacts on the broader market economy. Primarily, it should establish an effective mechanism for negotiating new arrangements to restructure

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<sup>56</sup> Wilfinger A. (2023), Corporate Restructuring in Austria: The Implementation of Directive (EU) 2019/1023 on Restructuring and Insolvency. *European Insolvency and Restructuring Journal*, p. 9.

<sup>57</sup> Fischer, N. (2003), "Rechts-Harmonisierung" – Schlagwort oder Rechtsprinzip? – Kritische Anmerkungen zum Prozess der "Rechts-Angleichung", *10 Verbraucher und Recht*, p. 374.

<sup>58</sup> Ellingsæter S. S. (2024), Optionality and EU harmonisation of restructuring and insolvency law: The case of the Preventive Restructuring Directive and priority rules, p. 35.

<sup>59</sup> Villeroy de Galhau, F. (2021), "The Banking Union: Time to move forward again", speech at the Eurofi Financial Forum, 10 September.

<sup>60</sup> Jackson T. H. (1986), *The Logic and Limits of Bankruptcy Law*. Harvard University Press.

debt. If debt restructuring proves unsuccessful, liquidation should be the appropriate outcome, benefiting both market participants and the economy as a whole. However, bankruptcy proceedings and the management of non-performing assets are closely interrelated but distinct areas of legislation. The latter is predominantly governed by national company law. These laws deal with core issues of economic management and social policy, such as how businesses are treated in financial distress, how creditors are prioritized, and how contracts are enforced. Any effort to harmonise these laws is viewed as a ceding of national control over critical aspects of legal and economic governance.<sup>61</sup> This generates substantial political resistance, particularly from member states that have well-established legal traditions or specific economic structures that are heavily influenced by their domestic insolvency and contract rules.

In fact, insolvency proceedings are often seen as a tool for enforcing national economic policies and regulatory frameworks, making it even more crucial for states to maintain control over cases that could impact their national markets.<sup>62</sup> The choice of the legal instruments in resolving a bankruptcy case can have a severe impact on the protection of local industries and jobs. National insolvency law can be also used as a tool to respond to economic crises or market shifts. By controlling their own insolvency regimes, Member States can tailor laws to suit specific economic conditions, such as providing temporary relief for businesses during recessions or ensuring the protection of strategic industries.<sup>63</sup> A harmonised regime could limit this flexibility. Moreover, member States may fear that harmonisation could reduce the protection of domestic creditors in favour of cross-border interests. EU Member States are therefore often resistant to the idea of a fully harmonised insolvency regime. A harmonised EU-wide insolvency regime would likely diminish national control over critical decisions affecting domestic economies, which is why many Member States prefer to retain the authority to shape insolvency laws in accordance with their own national interests.

The economies of EU Member States vary widely in terms of their size and structure, and insolvency laws reflect these differences. That's why more industrialised countries often have insolvency laws focused on rescuing large corporations, while smaller economies might emphasise creditor protection or quick liquidation processes. Member States are therefore hesitant to adopt a one-size-fits-all approach, fearing that a harmonised regime would have a negative impact on their national economy due to not taking into account their economic distinctions.

Apart of that, jurisdictions with more favourable insolvency frameworks, particularly those offering quicker resolution processes or more protective restructuring options, may be against the coherent insolvency regime since it can directly affect investments in their economy.<sup>64</sup> A favourable insolvency regime can be in fact seen as a competitive advantage over other jurisdictions that helps to attract

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<sup>61</sup> Armour J. (2001), *The Law and Economics of Corporate Insolvency: A Review*, ESRC Centre for Business Research Working Paper No. 197, p. 35.

<sup>62</sup> LoPucki L. M. (2005), *Courting Failure: How Competition for Big Cases Is Corrupting the Bankruptcy Courts*. University of Michigan Press., p. 123.

<sup>63</sup> Bork R. (2012), *Principles of Cross-Border Insolvency Law*. Intersentia. p. 46.

<sup>64</sup> Davydenko S. A. & Franks J. R. (2008), *Do Bankruptcy Codes Matter? A Study of Defaults in France, Germany, and the U.K.* *The Journal of Finance* 63(2), 565–608.

more money into national economy. In such case, harmonisation could make them less attractive to multinational companies looking to establish operations or conduct business.

As a result, when multiple jurisdictions come into play to address cross-border insolvencies, each of them reflects the specific legal and economic policies of the respective state.<sup>65</sup> These discrepancies mostly arise can relate to a variety of critical issues, such as the ranking of creditors, the conditions for asset recovery, the treatment of employees, and the scope of a debtor's obligations. The lack of harmonisation between national insolvency laws leads to legal barriers that prevent effective cooperation between jurisdictions. As a result, the current fragmentation of the insolvency law leads to legal uncertainty, delays, and inefficiencies that hinder an effective insolvency resolution.

### 4.3 EU and national competences in the area of insolvency law

The scope and intensity of EU action in the field of insolvency law are fundamentally limited by the allocation of competences between the Union and its Member States. Any assessment of current and future harmonisation efforts must therefore begin with a clear understanding of the constitutional framework governing EU legislative action in this area. That framework reveals not only why insolvency law has remained fragmented, but also why comprehensive harmonisation is structurally constrained under the Treaties. At the same time, it explains why EU action has increasingly focused on selective, functionally justified interventions rather than systemic unification.

#### 4.3.1 National competences

Insolvency law has traditionally formed part of the core of national private and procedural law, closely intertwined with contract law, property law, company law, labour law, and social policy, all of which reflect national legal traditions.<sup>66</sup> The Treaties contain no explicit conferral of a general competence on the EU to regulate insolvency law as such. Under the principle of conferral in accordance with Article 5(1) and (2) TEU, competence in this area therefore remains mostly with the Member States.

Against this background, the question arises whether general principles of company or insolvency law exist at the EU level. In company law, certain core elements - such as the freedom of establishment, the recognition of companies formed under another Member State's law, and some minimum standards on capital, disclosure, and shareholder rights - demonstrate converging principles.<sup>67</sup> By contrast, insolvency laws display far greater diversity. The absence of harmonised rules on priorities, creditor protection standards, group insolvency, or liquidation procedures means that identifying overarching common principles in this domain is considerably more difficult. However, several connected fields have been partially harmonised at EU level because of their relevance for financial stability and the internal market. In the area of company law, EU directives create minimum standards on incorporation, mergers, divisions, cross-border conversions, disclosure obligations, and shareholder rights, all of which shape the corporate framework within which insolvency occurs. Then, for credit institutions and

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<sup>65</sup> Platsas A. (2017), *The Harmonisation of National Legal Systems. Strategic Models and Factors*, Edward Elgar, vii-viii.

<sup>66</sup> Mańko R. (2015), *EU Competence in Private Law - The Treaty Framework for a European Private Law and Challenges for Coherence*, European Parliamentary Research Service, PE 545.711.

<sup>67</sup> Directive (EU) 2017/1132 relating to certain aspects of company law (2017), OJ L169/46.

investment firms, EU legislation (including CRR<sup>68</sup>/CRD<sup>69</sup>, BRRD<sup>70</sup>, and the SRM Regulation<sup>71</sup>) sets out a specialised resolution regime that operates in parallel to national insolvency law, often taking precedence in the event of bank failure. These sector-specific regimes underscore that EU intervention is constitutionally acceptable where insolvency-related rules are functionally linked to market stability and systemic risk, but not as a general replacement for national insolvency systems.

As a consequence, Member States retain primary responsibility for the design of their insolvency systems, including the conditions for opening proceedings, the available types of proceedings, the ranking of claims, the treatment of secured and unsecured creditors, directors' duties in financial distress, and the procedural architecture of insolvency proceedings. These elements are not merely technical rules, but reflect policy choices concerning risk allocation, creditor-debtor balances, and the social consequences of business failure. That explains both the political sensitivity of insolvency law and the persistent resistance to far-reaching EU intervention, particularly where harmonisation would indirectly affect labour protection, taxation, or social security systems.

### 4.3.2 Limits of the EU competence

Although the EU lacks a general competence in insolvency law, it may nevertheless legislate in this field indirectly where divergences between national insolvency regimes impede the functioning of the internal market. The primary legal basis is Article 114 TFEU which empowers the Union to adopt measures for the approximation of national laws that have as their object the establishment and functioning of the internal market. Crucially, Article 114 TFEU does not grant the EU a right to establish comprehensive codification of insolvency law. According to settled case law of the Court of Justice, harmonisation under Article 114 must be functional, proportionate, and demonstrably linked to the removal of obstacles to cross-border trade, investment, or competition.<sup>72</sup> The provision allows the EU to address specific regulatory divergences that distort market integration, but not to replace national legal systems with a uniform European insolvency code.

These limits become particularly visible in the debate on a potential "28th regime". While such a regime is frequently presented as a tool to reduce legal fragmentation, its constitutional basis remains sensitive. Article 114 TFEU permits the approximation of existing national rules, but not the creation

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<sup>68</sup> Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 Regulation (EU) No 575/2013, OJ L176/1.

<sup>69</sup> Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, OJ L176/338.

<sup>70</sup> Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, OJ L173/190.

<sup>71</sup> Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010, OJ L225/1.

<sup>72</sup> Weatherill S. (2011), *The Limits of Legislative Harmonisation Ten Years after Tobacco Advertising: How the Court's Case Law has become a "Drafting Guide."* German Law Journal. 2011;12(3):827-864.

of an autonomous supranational insolvency or company law regime operating independently alongside national systems.<sup>73</sup> Past attempts to introduce optional European company forms, such as the proposed European Private Company (SPE) or the *Societas Unius Personae* (SUP)<sup>74</sup>, illustrate both the legal fragility and the political resistance associated with such projects. Where supranational legal forms have been successfully introduced, notably the *Societas Europaea*,<sup>75</sup> this required recourse to the residual competence clause of Article 352 TFEU and unanimity in the Council.<sup>76</sup> Comparable requirements would arise if an optional insolvency regime were to extend beyond narrowly defined and functionally justified elements.

As a result, the EU sets the framework for cross-border jurisdiction, procedural coordination, preventive restructuring standards, and crisis management in the financial sector, while Member States retain control over liquidation regimes, creditor hierarchies, corporate group insolvency, and enforcement mechanisms. Any attempt to centralise these core elements would exceed the current limits of EU competence.

### 4.3.3 Proportionality and subsidiarity

The constrained nature of EU insolvency harmonisation is further reinforced by the principles of subsidiarity and proportionality laid down in Article 5(3) and (4) TFEU. Given the diversity of national insolvency systems and their close connection to domestic economic and social policies, full-scale harmonisation cannot be justified as either necessary or proportionate. In many instances, the costs of uniform rules - both political and practical - would outweigh their potential benefits.

This explains why EU insolvency policy has increasingly adopted a selective and incremental approach. Rather than pursuing comprehensive unification, the Union focuses on sub-areas deemed particularly relevant for cross-border investment and capital markets. While this strategy has produced tangible progress, it also exposes the inherent limits of regulation-driven convergence.<sup>77</sup> Even well-designed directives cannot eliminate structural fragmentation as long as core elements of insolvency law remain anchored in national systems.

However, fragmentation does not stem solely from divergent substantive rules, but also from informational asymmetries, procedural opacity, and the absence of mechanisms that allow market participants to manage legal diversity effectively. Addressing these issues requires a broader strategic perspective that goes beyond traditional harmonisation.

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<sup>73</sup> Hoffmann A. and Kullas M. (2025), Die neue EU-Binnenmarktstrategie 2025, cepPolicyBrief.

<sup>74</sup> Proposal for a Directive of the European Parliament and of the Council on single-member private limited liability companies, COM/2014/0212 final - 2014/0120 (COD).

<sup>75</sup> Council Regulation (EC) No 2157/2001 of 8 October 2001 on the Statute for a European company (SE), OJ L 294 10.11.2001.

<sup>76</sup> Draghi M. (2024), In-depth analysis and recommendations, (Part B), p. 315, [https://commission.europa.eu/document/download/ec1409c1-d4b4-4882-8bdd-3519f86bbb92\\_en?filename=The%20future%20of%20European%20competitiveness\\_%20Indepth%20analysis%20and%20recommendations\\_0.pdf](https://commission.europa.eu/document/download/ec1409c1-d4b4-4882-8bdd-3519f86bbb92_en?filename=The%20future%20of%20European%20competitiveness_%20Indepth%20analysis%20and%20recommendations_0.pdf).

<sup>77</sup> Eidenmüller H. (2017), Contracting for a European Insolvency Regime, 18 *European Business Organization Law Review* 273, p.278-279.

Beyond constitutional and political constraints, comprehensive harmonisation of insolvency law entails substantive regulatory risks.<sup>78</sup> A fully harmonised insolvency regime would inevitably freeze a particular set of policy choices at Union level, thereby codifying legal standards that may prove suboptimal or become outdated over time. Insolvency law must continuously adapt to evolving economic conditions, business models, and financial instruments. Uniform rules, once adopted through EU legislation, are difficult to revise and may lack the flexibility required to respond to market developments or sector-specific needs. In addition, insolvency law is characterised by a finely balanced interaction between creditor protection, debtor rescue, and broader social considerations. Imposing a single, uniform model risks disrupting this balance by privileging certain interests or economic philosophies at the expense of others.<sup>79</sup> Given the heterogeneity of Member States' economies and financial systems, a one-size-fits-all insolvency code may generate inefficiencies rather than resolve them.

By contrast, regulatory competition among national insolvency regimes can function as a dynamic mechanism for legal innovation and improvement.<sup>80</sup> Diversity allows Member States to experiment with different procedural designs, restructuring tools, and creditor participation models. Over time, effective solutions tend to diffuse through legislative emulation, judicial practice, and market pressure<sup>81</sup>. This process enables the emergence of best practices without the rigidity associated with top-down harmonisation.<sup>82</sup> From this perspective, controlled diversity is not merely a transitional deficiency, but a functional asset. A regulatory environment that preserves national autonomy while facilitating cross-border interaction allows insolvency law to evolve incrementally and responsively. The challenge for EU policy, therefore, is not to eliminate diversity altogether, but to create a framework in which regulatory competition can operate efficiently, transparently, and without generating excessive fragmentation.

All in all, Insolvency law takes a special place within EU law: economically central to the internal market and the CMU, yet legally anchored in national competence. The limits of Article 114 TFEU and the principles of subsidiarity and proportionality make clear that comprehensive harmonisation is neither feasible nor desirable. This does not imply unresolvable problem but rather calls for a reorientation of EU policy towards alternative strategies without overstepping constitutional boundaries.

## 5 A new strategy for the future of EU insolvency law

The core challenge created by the fragmentation of insolvency law in the EU is not diversity as such, but the resulting complexity and lack of predictability. Both undermine the effectiveness of insolvency frameworks and the functioning of integrated capital markets. Given the structural and political limits of comprehensive harmonisation, the EU cannot realistically eliminate this complexity through

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<sup>78</sup> Weatherill S. (2024), *Why Harmonise*, In Tridimas T. and Nebbia P. (eds), *EU Law for the Twenty-First Century: Rethinking the New Legal Order* (Hart Publishing), p. 31.

<sup>79</sup> Giandomenico M. (1998), *Europe's "Democratic Deficit": The Question of Standards*. *European Law Journal* 4(1), 5-28.

<sup>80</sup> Hornuf L. (2011), *Regulatory Competition in European Corporate and Capital Market Law: An Empirical Analysis*. Inaugural-Dissertation. P. 145.

<sup>81</sup> Weatherill S. (2011), *The Limits of Legislative Harmonisation Ten Years after Tobacco Advertising: How the Court's Case Law Has Become a "Drafting Guide"*. *German Law Journal* 12(3), 827–864.

<sup>82</sup> Eidenmüller H. (2005), *Free Choice in International Company Insolvency Law in Europe*. *European Business Organization Law Review* 6(3), 423–447.

unification. Rather than pursuing an unrealistic ideal of full harmonisation, EU insolvency policy should therefore focus on improving predictability and functionality through a broader and more differentiated set of instruments. This does not imply a rejection of harmonisation as such. On the contrary, targeted harmonisation remains an essential component of any efficient EU insolvency strategy and the EU should continue to pursue it where it is both feasible and economically meaningful. However, harmonisation can only ever address selected elements of the broader problem and must be complemented by additional mechanisms capable of reducing fragmentation and uncertainty in practice.

Against this background, this chapter proposes a new strategic framework based on four interrelated pillars. These pillars combine targeted harmonisation with alternative approaches, including enhanced transparency, regulatory coordination, and innovative legal models, to improve the predictability, efficiency, and coherence of insolvency outcomes across the EU. Taken together, they offer a pathway towards mitigating the negative effects of fragmentation while respecting the legal diversity of the Member States.

### 5.1 Pillar 1: Deepening targeted harmonisation

The first pillar of the proposed strategy consists in further deepening the targeted harmonisation of insolvency law at EU level. Rather than pursuing comprehensive codification, this approach focuses on carefully selected legal areas that are of particular relevance for cross-border investment and the functioning of integrated capital markets.<sup>83</sup> The objective is not to replace national insolvency systems or legal traditions, but to identify those core rules that matter most to economic actors and to establish EU-wide minimum standards or common principles. Such an approach provides a predictable legal baseline while preserving Member States' discretion to adapt the rules to their domestic legal and economic contexts.

Building on the 2025 Directive, which introduced harmonised standards on avoidance actions and pre-pack proceedings, a further "second wave" of targeted harmonisation could concentrate on a limited number of high-impact areas. First, the hierarchy of creditor claims represents one of the most decisive factors for risk assessment and recovery expectations in insolvency. Establishing a common order of priority for key categories of creditors, such as secured creditors, employees, public authorities, and unsecured creditors, would create a shared framework for pricing risk across the Union. A harmonised creditor waterfall would reduce legal uncertainty, lower transaction costs, and facilitate cross-border lending and investment decisions.<sup>84</sup>

Secondly, greater convergence in the core triggers for opening insolvency proceedings would enhance legal predictability. At present, Member States apply different criteria for determining when a debtor is insolvent, particularly with regard to illiquidity and over-indebtedness. Harmonising these core

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<sup>83</sup> McGowan A. M. & Andrews D. (2018), *Design of Insolvency Regimes Across Countries*, OECD Economics Department Working Papers No. 1504.

<sup>84</sup> Ghio E. (2017), *Time to Renew the Debate on Cross-Border Insolvency Law: Out with Theoretical Ideals, in with Pragmatism*, In: Gant, J. (2017). *Harmonisation of European Insolvency Law*. p. 174.

definitions would support the timely and consistent initiation of proceedings and contribute to a more uniform application of directors' duties in case of insolvency.

Thirdly, targeted harmonisation could address the enforcement of security interests in insolvency. Although this field is closely linked to national property law, greater clarity and convergence regarding the creation, perfection, and enforcement of security rights would significantly reduce uncertainty for secured creditors, who constitute a central source of corporate financing. Even limited harmonisation in this area could have a positive effect on cross-border credit provision.

Focusing on these narrowly defined areas allows the EU to generate tangible economic benefits without overhauling entire national insolvency systems. Targeted harmonisation can enhance legal predictability, reduce incentives for costly forum shopping, and contribute to a more level playing field within the internal market. However, the inherent limitations of this approach must be acknowledged. By definition, targeted harmonisation leaves the vast majority of national insolvency law untouched. Fundamental differences persist in procedural design, the role and powers of courts and insolvency practitioners, and the interaction between insolvency law and national labour, contract, and tax regimes. Moreover, even where substantive rules are formally aligned, their interpretation and application remain subject to national legal cultures and judicial practices, often resulting in divergent outcomes.<sup>85</sup> The protracted negotiations leading to the 2025 agreement illustrate the political difficulty of advancing harmonisation in particularly sensitive areas, such as creditor ranking. Progress in such areas is therefore likely to remain incremental and slow.

For these reasons, deepening targeted harmonisation can only ever form part of a broader strategy. While it addresses some of the most visible manifestations of fragmentation, it cannot resolve the underlying structural diversity of national insolvency frameworks. Harmonisation should thus be understood as a complementary instrument rather than a comprehensive solution.

## 5.2 Pillar 2: Improvements in financial market regulation

### 5.2.1 Financial market regulation as an indirect driver of coherent insolvency outcomes in the EU

Improvements in EU financial market regulation contribute to greater coherence, predictability, and stability of insolvency outcomes across the Union, despite the persistence of legal diversity.<sup>86</sup> Amending EU financial market regulations is generally easier than harmonising national insolvency and contract laws for several key reasons.

First, the EU holds extensive competence in financial market regulation. Binding EU regulations, directly applicable in all member states, aim to ensure market stability, protect investors, and enhance the single market's efficiency. EU prudential regulation obliges financial institutions and certain large

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<sup>85</sup> Mirela N. N. (2017) The Role of Judiciary for a Greater Convergence of European Insolvency Law, In: Gant, J. (2017). Harmonisation of European Insolvency Law. p. 31.

<sup>86</sup> Avgouleas E. & Cullen J. (2015), Market Discipline and EU Corporate Governance Reform in the Banking Sector: Merits, Fallacies, and Cognitive Boundaries, 41 Journal of Law and Society 28.

firms to maintain adequate capital buffers, liquidity reserves, and robust governance structures. Requirements under the CRR/CRD framework, combined with supervisory review processes, reduce the likelihood of sudden and disorderly insolvencies and limit negative spillover effects within corporate groups. By strengthening ex ante resilience, prudential supervision contributes to insolvency prevention and stabilises corporate structures within the internal market.<sup>87</sup> This legal framework allows for swifter adaptation to market developments or emerging challenges. In contrast, insolvency and contract laws largely remain within the jurisdiction of national legal systems.

Many insolvency challenges arise within complex, multi-jurisdictional corporate groups. EU financial regulation addresses this through consolidated supervision of banking groups and financial conglomerates. Group-wide oversight facilitates coordinated supervisory action and reduces the risk of conflicting national measures that can complicate group insolvency proceedings. Although such coordination does not replace insolvency law harmonisation, it mitigates some of the structural weaknesses of entity-based national insolvency regimes.

Second, financial market regulation in the EU has undergone extensive and sustained harmonisation over the past decades, including critical aspects of financial contracts that are central to insolvency proceedings as well as mechanisms that indirectly support more coherent insolvency outcomes.<sup>88</sup> For example, harmonised prudential requirements (CRR/CRD), early-intervention tools, and supervisory review processes aim to detect financial distress earlier and mitigate insolvency risk. Regulations governing derivatives, securities financing transactions, settlement finality, payment systems, and collateral arrangements (such as EMIR<sup>89</sup>, SFTR<sup>90</sup>, and the Settlement Finality Directive<sup>91</sup>) reduce uncertainty regarding netting, close-out rights, and collateral enforcement. This harmonisation limits divergent national interpretations in insolvency scenarios and enhances legal certainty for market participants.<sup>92</sup> Likewise, harmonised disclosure, auditing, and accounting standards play a crucial role in improving insolvency outcomes. High-quality and comparable financial reporting enables earlier detection of financial distress, facilitates the preparation of restructuring plans, and allows for more accurate valuation of assets and liabilities in insolvency proceedings. By reducing information asymmetries between debtors and creditors, these standards make cross-border insolvency cases less contentious and more predictable, thereby mitigating some of the practical effects of fragmented national insolvency laws.<sup>93</sup> In general, a more integrated CMU improves access to restructuring and rescue finance for distressed

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<sup>87</sup> Hartmann, P., Heider F., Pappaiannou E., and de Luca M. (2007), *The role of financial markets and innovation in productivity and growth in Europe*, The European Central Bank, Occasional Papers Series, No. 70.

<sup>88</sup> Teixeira P.G. (2017), *The legal history of the Banking Union*. *European Business Organization Law Review* 18, p. 535-565.

<sup>89</sup> Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories. OJ L 201.

<sup>90</sup> Regulation (EU) 2019/2088 of the European Parliament and of the Council of 27 November 2019 on sustainability-related disclosures in the financial services sector. PE/87/2019/REV/1. OJ L 317.

<sup>91</sup> Directive 98/26/EC of the European Parliament and of the Council of 19 May 1998 on settlement finality in payment and securities settlement systems. OJ L 166.

<sup>92</sup> Davydenko S. and Franks J. (2008), *Do Bankruptcy Codes Matter? A Study of Defaults in France, Germany, and the U.K.*, *Journal of Finance* 63 (2), p. 565–608.

<sup>93</sup> Castagna P. (2017), *Banking Perspective on Creditor Ranking in Insolvency*, In: Gant, J. (2017). *Harmonisation of European Insolvency Law*. p. 137.

but viable firms.<sup>94</sup> Enhanced availability of debtor-in-possession financing, equity injections, and alternative funding sources reduces reliance on liquidation and supports business continuity.<sup>95</sup> Even in the absence of harmonised insolvency law, deeper capital market integration can significantly influence insolvency outcomes by expanding the range of available restructuring options.<sup>96</sup>

Third, institutional factors further explain this divergence. In the financial sector, the EU has developed powerful centralised actors, including the European Central Bank (ECB), the European Banking Authority (EBA), the European Securities and Markets Authority (ESMA), and the European Insurance and Occupational Pensions Authority (EIOPA). No comparable institutions exist with authority over insolvency or contract law.

However, the scope of financial regulation is inherently sector-specific. Its harmonising effects are strongest in banking, capital markets, and regulated financial institutions, but significantly weaker for small and medium-sized enterprises, non-financial corporate groups, and privately held firms. Against this background, EU financial market regulation constitutes an effective but still limited mechanism for improving insolvency-relevant outcomes in a fragmented legal framework.

## 5.2.2 The interplay between insolvency law and bank resolution in the EU

As mentioned above, banking insolvencies can benefit the most from the improvements in EU financial market regulation. This subchapter highlights the special case of bank resolution.

The global financial crisis exposed fundamental weaknesses in the treatment of failing credit institutions under traditional corporate insolvency law. In response, the EU established a harmonised framework for the recovery and resolution of banks through the Bank Recovery and Resolution Directive (BRRD)<sup>97</sup> and the Single Resolution Mechanism Regulation (SRMR)<sup>98</sup>. These instruments were designed to address the systemic risks revealed by the crisis, in particular the inability of ordinary insolvency proceedings to manage bank failures without triggering contagion, disrupting critical financial functions, or resorting to taxpayer-funded bailouts. The resolution framework therefore pursues distinct public interest objectives, including financial stability, depositor protection, and the continuity of essential banking services.

A central premise of the BRRD and SRMR is that conventional insolvency law is inappropriate to the specific characteristics of banks. Banking failures typically unfold rapidly, involve complex balance

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<sup>94</sup> Romero-Avila D. (2007), Finance and growth in the EU: New evidence from the harmonisation of the banking industry, *Journal of Finance and Banking*, Vol. 31, No. 7, pp 1937-1954.

<sup>95</sup> Baird D. G. (1987), The Uneasy Case for Corporate Reorganizations. *Journal of Legal Studies* 15(1), 127–147.

<sup>96</sup> Ferran E. (2012), Crisis-Driven Regulatory Reform: Where in the World Is the EU Going?, 13 *European Business Organization Law Review* 1.

<sup>97</sup> Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms and amending Council Directive 82/891/EEC, and Directives 2001/24/EC, 2002/47/EC, 2004/25/EC, 2005/56/EC, 2007/36/EC, 2011/35/EU, 2012/30/EU and 2013/36/EU, and Regulations (EU) No 1093/2010 and (EU) No 648/2012, of the European Parliament and of the Council. OJ L 173.

<sup>98</sup> Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010. OJ L 225.

sheets, and generate significant negative externalities. To address these features, the EU introduced a specialised, predominantly administrative resolution regime that empowers resolution authorities to intervene at an early stage and to use tools such as bail-in, bridge institutions, and asset separation. This marked a paradigm shift in many Member States, where failing banks had traditionally been subject to court-led insolvency proceedings.

Notwithstanding this high degree of harmonisation, national insolvency laws remain structurally embedded in the EU resolution framework. The BRRD explicitly relies on national insolvency law as a benchmark in several key respects. Most importantly, the creditor hierarchy applicable in resolution is derived from national insolvency law, as reflected in the “no creditor worse off” principle.<sup>99</sup> This principle ensures that creditors do not incur greater losses under resolution than they would have suffered in normal insolvency proceedings under national law. As a result, resolution outcomes are necessarily shaped by divergent national rules on the ranking and treatment of claims.

Moreover, resolution is reserved for exceptional cases. The BRRD establishes a high threshold for the use of resolution tools, requiring that the institution be failing or likely to fail, that no private sector alternative is available, and that resolution be necessary in public interest. In practice, this public interest test has often limited the application of resolution, with many failing banks instead being wound up under national insolvency proceedings. Even within the Banking Union, liquidation rather than resolution remains the default outcome for a significant number of institutions, including some with cross-border activities.<sup>100</sup>

The continued relevance of national insolvency law is particularly evident in the context of banking groups. Most EU banks operate within complex group structures, characterised by extensive intra-group funding, liquidity flows, and operational interdependence. While the BRRD promotes group-level recovery and resolution planning, national insolvency laws remain largely entity-focused. This structural mismatch complicates the implementation of group-wide strategies, especially where national laws restrict intra-group financial support or impose rigid creditor-protection rules that prioritise the interests of individual entities over the stability of the group as a whole.<sup>101</sup> These tensions are evident in cross-border cases. Divergent national insolvency regimes affect the feasibility of liquidity reallocation, the enforceability of intra-group guarantees, and the consistency of creditor treatment across jurisdictions. Even where resolution authorities pursue coordinated strategies, outcomes remain dependent on national insolvency benchmarks, exposing banking groups to legal uncertainty and undermining the effectiveness of EU-level resolution planning.<sup>102</sup>

Importantly, national insolvency law continues to exert influence even after resolution measures are implemented. Creditors retain the right to challenge resolution actions by reference to the

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<sup>99</sup> Malek H. & Bousfield S. (2016), Bad banks and the “No Creditor Worse Off” compensation scheme. *Butterworths Journal of International Banking und Financial Law*. June 2016, p. 339.

<sup>100</sup> Gortsos C. V. (2019), *The Single Resolution Mechanism (SRM) and the Single Resolution Fund (SRF): Legal Aspects of the Second Main Pillar of the European Banking Union (Fifth- Extended and Fully Updated - Edition)*. S. 162.

<sup>101</sup> Mevorach I. (2009), *Insolvency within Multinational Enterprise Groups*, OUP Catalogue, Oxford University Press, number 9780199544721.

<sup>102</sup> Hüpkes E. (2016), *Insolvency – Why a Special Regime for Banks?* in Jens-Hinrich Binder and Dalvinder Singh (eds), *Bank Resolution: The European Regime*.

counterfactual outcome under national insolvency proceedings. Compensation claims under the NCWO principle further reinforce the centrality of national law, ensuring that resolution remains tightly interwoven with domestic insolvency frameworks.

Taken together, this interaction reveals a structural paradox. Bank resolution represents one of the most harmonised areas of EU financial law, yet its operation remains fundamentally dependent on fragmented national insolvency regimes. This dependence limits the effectiveness of resolution tools, complicates group-level crisis management, and introduces legal uncertainty even within the highly regulated banking sector. The experience of bank resolution thus illustrates both the potential and the limits of EU harmonisation: even in a field characterised by strong centralisation and shared public interest objectives, the absence of a more coherent insolvency baseline continues to shape outcomes in decisive ways.

### 5.3 Pillar 3: Transparency and soft law

The third pillar of a renewed EU strategy for reducing fragmentation in insolvency law focuses on functional alternatives to legislative interventions. Where mandatory alignment of national insolvency regimes encounters constitutional, political, or cultural resistance, the EU can nevertheless achieve significant convergence effects by enhancing transparency and by steering national reforms through soft law instruments.

This pillar rests on the idea that legal uncertainty in cross-border insolvencies does not stem solely from substantive divergence, but also from information asymmetries, opacity, and the high costs of understanding and comparing national regimes. In such a setting, empowering market participants with high-quality, comparable, and accessible information can substantially reduce barriers to cross-border investment and improve predictability without requiring Member States to give up sovereignty over core insolvency rules.<sup>103</sup>

Accordingly, this pillar combines two complementary strategies:

- (1) more transparency through structured and comparable information; and
- (2) policy guidance through non-binding, best-practice-oriented soft law.

#### 5.3.1 The European insolvency portal as an instrument of transparency

The Commission's proposal to require Member States to publish a standardised PDF factsheet on national insolvency law represents a welcome but limited first step.<sup>104</sup> While it improves formal accessibility, such a solution remains static, non-comparable, and quickly outdated. PDF documents do not allow for systematic comparison, automated analysis, or dynamic updating, and therefore fall short of meaningfully reducing legal uncertainty for cross-border investors and creditors.

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<sup>103</sup> Abbott K. W. & Snidal D. (2000), *Hard and Soft Law in International Governance*, 54 (3) *International Organization*, p. 421.

<sup>104</sup> Art. 68 of the Proposal for a Directive of the European Parliament and of the Council harmonising certain aspects of insolvency law COM/2022/702 final.

A more ambitious and functionally effective approach would be the creation of a European insolvency portal, integrated into the existing e-Justice infrastructure. Rather than serving as a passive document repository, the portal should function as an interactive, data-driven tool enabling legal and economic risk assessment across jurisdictions.

Key elements of such a portal should include:

**a) Standardised and machine-readable legal data:** Member States should be required to submit structured information on their insolvency frameworks using a common data format. This would allow users to directly compare, inter alia, creditor hierarchies, avoidance rules, procedural milestones, and the powers of insolvency practitioners. From a CMU perspective, this would reduce due diligence costs and facilitate cross-border lending and investment decisions.

**b) Harmonised reporting standards and performance indicators:** True transparency requires not only theoretical legal knowledge, but also insight into how insolvency systems function in practice. The portal should therefore include harmonised key performance indicators, such as average duration of proceedings, recovery rates by creditor class, and typical administrative costs. This would transform transparency from a qualitative to a quantitative exercise and allow investors to price insolvency risk more accurately.

**c) A centralised repository of case law and practice:** The inclusion of anonymised, representative national court decisions would provide valuable insight into the practical application and interpretation of insolvency rules. Such a repository would mitigate the risk of divergent application and foster informal convergence through judicial dialogue and mutual learning.<sup>105</sup>

By creating a single, dynamic source of comparable information, the EU can lower the informational barriers that currently deter cross-border investment. This is particularly relevant for non-EU investors who often experience difficulties with the EU insolvency landscape. Transparency thus becomes a strategic tool for attracting global capital and strengthening the CMU, at a fraction of the political cost of formal harmonisation.

### 5.3.2 Soft law instruments for SMEs

The limits of mandatory harmonisation became particularly visible during the 2025 legislative negotiations, which resulted in the complete removal of the proposed chapter on simplified procedures for microenterprises. This retreat left a significant policy gap in an area of central economic importance, given that SMEs form the backbone of the European economy. This gap underscores the importance of soft law as a policy instrument. Where binding legislation proves politically challenging, non-binding instruments can still provide orientation, promote convergence, and shape national reforms over time.

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<sup>105</sup> Sadler A. (2012), Practice Obstacles in Cross-border Litigation and Communication between (EU) Courts, 5(3) Erasmus Law Review 151-168.

A particularly instructive model is offered by UNCITRAL's Legislative Guide on Insolvency Law<sup>106</sup>, which contains detailed frameworks not only for liquidation, but also for simplified reorganisation procedures tailored to SMEs. UNCITRAL defines reorganisation broadly as a process aimed at restoring the viability of a business while allowing it to continue operations, through measures such as debt rescheduling, partial debt forgiveness, debt-to-equity conversions, or the sale of the business as a going concern. In contrast, recent EU initiatives have focused predominantly on simplified liquidation, emphasising swift market exit rather than business rescue. This approach stands in tension with the EU's repeatedly stated objective of fostering a "rescue culture" and preserving economically viable enterprises.<sup>107</sup>

Against this background, the EU should develop a non-binding model framework or set of best practices for SME reorganisation adapted to the European legal context and market realities. Such an instrument would not impose uniform solutions but would offer Member States a coherent blueprint for designing simplified judicial or hybrid reorganisation procedures for small businesses.

Crucially, SME reorganisation mechanisms must avoid the procedural and institutional complexity characteristic of large corporate restructurings. Simplification may include streamlined creditor participation, reduced court involvement, standardised restructuring tools, and limited reporting requirements. The aim is not to replicate sophisticated restructuring regimes, but to provide accessible and proportionate rescue mechanisms for smaller firms.

Taken together, transparency and soft law constitute a pragmatic and structurally coherent pillar within a broader EU strategy to reduce insolvency fragmentation and remove barriers to the CMU integration. While they cannot replace substantive harmonisation at the distributional core of insolvency law, they can significantly enhance predictability, reduce information asymmetries, and foster functional convergence. By mandating radical transparency and guiding national reforms through carefully designed soft-law instruments, the EU can achieve meaningful progress in a politically feasible manner.

#### 5.4 Pillar 4: An optional "28th regime" for cross-border insolvency

The first three pillars of the proposed strategy address fragmentation within the existing legal framework. Targeted harmonisation refines specific points of friction, improvements in financial market regulation align incentives and outcomes across jurisdictions, and transparency instruments enhance predictability without formal legal unification. Yet even in combination, they cannot fully resolve the structural problems that arise in complex cross-border insolvencies.

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<sup>106</sup> UNCITRAL Model Law on Cross-Border Insolvency Law, 1997, with Guide to Enactment and Interpretation, 2013, , available at: [http://www.uncitral.org/uncitral/en/uncitral\\_texts/insolvency.html](http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency.html); UNCITRAL Practice Guide on Cross-Border Insolvency Cooperation, 2009, available at: [http://www.uncitral.org/uncitral/en/uncitral\\_texts/insolvency.html](http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency.html); UNCITRAL Model Law: the Judicial Perspective, 2011, available at: [http://www.uncitral.org/uncitral/en/uncitral\\_texts/insolvency.html](http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency.html).

<sup>107</sup> Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks (Restructuring Directive), OJ L 172/18, Recitals 1-16.

In such cases, coordination between multiple national insolvency regimes remains inherently limited. Legal certainty depends not only on the quality of harmonised rules or soft law guidance, but on the interaction of entire legal systems shaped by distinct priorities, institutional designs, and policy trade-offs. At the same time, a single regulatory model cannot adequately serve both purely domestic insolvencies and highly integrated cross-border corporate structures. While national insolvency frameworks may remain well suited to local enterprises, they are often not well equipped to address the complexity, scale, and systemic relevance of multinational corporate groups.

Pillar 4 therefore moves beyond incremental adjustment within national frameworks and introduces an additional layer to the regulatory architecture: an optional European insolvency regime, commonly referred to as a 28th regime.<sup>108</sup> In this sense, Pillar 4 completes the strategic shift developed in the previous sections. While targeted harmonisation, regulatory alignment, and transparency measures improve the functioning of insolvency frameworks, the optional regime addresses the cases in which those instruments reach their functional limits.<sup>109</sup> Rather than pursuing uniformity for its own sake, the proposed approach combines convergence with regulatory choice, thereby reconciling the economic need for predictability with the diversity of national insolvency laws. From a regulatory perspective, this approach preserves beneficial regulatory competition between national insolvency systems while offering an alternative mechanism for cross-border cases. Rather than suppressing diversity, the optional regime channels it into a competitive process that allows efficient legal solutions to emerge through voluntary selection.

#### 5.4.1 Main characteristics of the 28<sup>th</sup> regime

This regime would coexist alongside national insolvency laws and apply only where debtors voluntarily opt into it. Its function is not to replace domestic systems, but to offer a unified substantive and procedural framework for cases in which cross-border fragmentation cannot be effectively addressed through coordination alone.<sup>110</sup> The 28th regime is particularly promising for corporate groups or debtors with significant assets and creditor bases in multiple Member States. Participation would be based on an explicit opt-in, either agreed upon ex ante through contractual arrangements or chosen at the opening of insolvency proceedings under clearly defined conditions. This design serves two essential functions. First, it preserves national sovereignty by ensuring that purely domestic insolvencies remain governed by national law. Secondly, it aligns regulatory choice with economic reality: only those actors who stand to benefit from deep harmonisation would invoke the regime. Firms opting into the framework implicitly accept its procedural logic, creditor coordination mechanisms, and enforcement structure, thereby mitigating the risk that formally efficient rules produce dysfunctional outcomes in practice. In this way, the 28th regime avoids the political resistance associated with mandatory harmonisation while still addressing demonstrable internal market failures. Crucially, this model aligns with the Union's traditional approach of negative integration. Instead of imposing positive harmonisation

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<sup>108</sup> See Rasmussen R.K. (1992), *Debtor's Choice: A Menu Approach to Corporate Bankruptcy*, Tex. L. Rev. 71 (1992), pp. 51 et seq.

<sup>109</sup> Mirela N. N. (2017) *The Role of Judiciary for a Greater Convergence of European Insolvency Law*, In: Gant, J. (2017). *Harmonisation of European Insolvency Law*. p. 49.

<sup>110</sup> Letta E. (2024), *Much More Than A Market*, April 2024, available under: <https://www.consilium.europa.eu/media/ny3j24sm/much-more-thana-market-report-by-enrico-letta.pdf>.

obligations on Member States, the Union merely removes structural barriers to cross-border activity by making an alternative legal framework available.<sup>111</sup>

The substantive design of an optional European insolvency regime should be derived from the most effective and well-functioning approaches to creditor coordination, restructuring procedures, and value preservation to support such an exercise. Rather than introducing entirely novel concepts, the regime should selectively consolidate those rules and techniques that have proven efficient in practice across the Member States. By drawing on national best practices, the optional regime would benefit from the most efficient elements of existing insolvency systems, while avoiding rules that generate unnecessary complexity or impede cross-border restructurings. At the same time, the consolidation of these best practices into a single, opt-in framework would significantly reduce legal uncertainty for cross-border investors and corporate groups, supporting integrated capital markets.

#### 5.4.2 A “virtual Delaware” for the Capital Markets Union

The optional 28th regime may also be understood as a European equivalent to the role played by Delaware in the United States<sup>112</sup> - albeit adapted to the legal and political realities of the EU. In the U.S. system, Delaware has emerged as the dominant jurisdiction for corporate law not through federal imposition, but through regulatory competition, legal predictability, and the accumulation of expertise.<sup>113</sup> Firms voluntarily choose Delaware law because it offers a stable, and business-oriented legal framework, while other states retain full competence over their own company and insolvency laws.<sup>114</sup> Although the Delaware model is sometimes criticised for potentially encouraging regulatory arbitrage or a “race to the bottom” in corporate governance standards, the proposed European regime would differ in important respects. It would not seek to attract incorporations or replace national systems, but would operate as a narrowly tailored, optional framework designed primarily for complex cross-border insolvencies. Its objective would be to provide a predictable legal environment for multinational restructurings while preserving regulatory diversity among Member States.

A European 28th regime has a potential to create a similar effect but in a “virtual”, non-territorial form. This mechanism also strengthens freedom of establishment by expanding the range of organisational choices available to market participants. Instead of constraining entrepreneurial activity through uniform regulation, the optional regime enhances autonomy by allowing firms to choose the legal framework that best corresponds to their economic structure and risk profile. Importantly, such a regime would preserve national sovereignty while enabling regulatory competition at the European level. In this sense, the 28th regime promotes efficiency. Legal innovation would no longer depend on slow political negotiations. Over time, ineffective solutions would fall out of use, while successful

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<sup>111</sup> Draghi M. (2024), The future of European competitiveness. Part A | A competitiveness strategy for Europe, available under: [97e481fd-2dc3-412d-be4c-f152a8232961\\_en](https://doi.org/10.2766/cep/2024/97e481fd-2dc3-412d-be4c-f152a8232961_en)

<sup>112</sup> Cary W. L. (1974), Federalism and Corporate Law: Reflections upon Delaware, 83 Yale Law Journal, p. 663.

<sup>113</sup> LoPucki L. M. (2005), *Courting Failure: How Competition for Big Cases Is Corrupting the Bankruptcy Courts*. University of Michigan Press., p. 49.

<sup>114</sup> McCormack G. (2014), Bankruptcy Forum Shopping: The UK and US as Venues of Choice for Foreign Companies, 63 International Comparative Law Quarterly 815, p. 822.

mechanisms would become more widely adopted. Convergence would thus develop through practical experience rather than top-down prescription.

The idea of an optional EU regime is not new. In 2017, the European Commercial Code initiative was launched in 2017 as an attempt to address the structural inconsistencies that characterise European commercial and insolvency law. The crucial function of insolvency law - to allocate losses, redistribute rights, and establish a collective enforcement mechanism - requires it to interpret and coordinate these underlying bodies of law. By integrating insolvency law within a broader commercial code, the initiative aims to harmonise not merely specific procedures, but the legal ecosystem in which insolvency operates. Moreover, codification would allow the introduction of consistent definitions and terminology, particularly with respect to insolvency, restructuring, creditor ranking, and avoidance actions, which would significantly enhance legal predictability and cross-border coordination.

Recently, policy discussions have intensified around the creation of 28th regimes for innovative and high-growth companies, particularly start-ups, digital firms, and scale-ups operating across borders. These initiatives reflect the recognition that traditional national legal forms may not adequately serve the needs of increasingly mobile and innovation-driven businesses. This cepStudy suggests extending that logic further. Rather than limiting an optional regime to a narrow category of innovative firms, all newly established companies should be given the possibility to opt into a European company and insolvency law framework. Allowing new firms to choose an EU-level regime for corporate governance and insolvency would enhance legal certainty *ex ante*, reduce future restructuring costs, and facilitate cross-border financing. Viewed in this light, the 28th regime functions as a “virtual Delaware” for Europe: a voluntary, competitive, and supranational legal framework that strengthens the internal market and offers a way to combine legal diversity with functional unity.

### 5.4.3 Legal constraints

Notwithstanding the functional appeal of the optional regime, concerns relating to subsidiarity, proportionality, and legal competence under the EU Treaties cannot be dismissed.

Article 114 TFEU can be considered as a legal basis for the optional regime, as it would aim to improve the functioning of the internal market by offering an additional, optional layer for multinational cases. The Court of Justice interprets Article 114 broadly, allowing substantive private law measures where they address market fragmentation. However, it would need a clear internal market rationale to avoid exceeding the limits of Article 114. In case Article 114 is considered insufficient, recourse to Article 352 (the flexibility clause) TFEU could be explored. This flexibility clause allows Union action where necessary to attain Treaty objectives, but it requires unanimity in the Council and the consent of the European Parliament. Politically and legally, this makes adoption more challenging. The path is therefore difficult, but not impossible, provided that the economic benefits and internal market necessity are convincingly demonstrated.

Subsidiarity concerns can be mitigated by the voluntary nature of the regime. Member States would retain full autonomy over domestic insolvencies and the choice to opt into the European framework would be exercised by private actors, not imposed by the Union. This limits its intrusiveness and

strengthens its proportionality. Proportionality follows from the limited scope of the instrument. The regime would apply in cross-border cases and upon explicit opt-in. It would therefore avoid the broader spill-over effects typically associated with mandatory harmonisation, particularly in areas such as labour protection, social security, or enforcement structures. National constitutional sensitivities, especially concerning judicial sovereignty and procedural autonomy,<sup>115</sup> could be addressed through decentralised application. Overall, while legally and politically challenging, an optional 28th regime remains feasible if carefully designed and clearly anchored in internal market objectives.

Taken together, these features suggest that an optional 28th regime is constitutionally less intrusive than further steps toward mandatory harmonisation. By offering a choice rather than imposing uniformity, the EU would respect national diversity while still addressing demonstrable internal market failures. In this sense, the 28th regime is better understood as an instrument of market facilitation than as a step towards federalisation. By refraining from mandatory harmonisation, the optional regime avoids restricting entrepreneurial freedom through rigid uniform rules. Instead, it expands the menu of legal options available to firms, thereby preserving innovation, contractual flexibility, and diverse business models across the EU.

## 6 Conclusion

This cepStudy has demonstrated that insolvency fragmentation within the EU is not merely a doctrinal problem, but a structural challenge for the internal market and the CMU. Divergent national insolvency regimes generate legal uncertainty, increase transaction costs, distort capital allocation, and complicate cross-border restructuring. Yet, full harmonisation remains politically contentious and constitutionally constrained by subsidiarity and limited EU competences.

The EU faces a structural choice. It can either continue to manage fragmentation through coordination mechanisms of limited effectiveness, or it can adopt a differentiated integration strategy that acknowledges diversity while creating structured pathways toward coherence. Against this background, this cepStudy proposes a four-pillar strategy to reduce fragmentation:

First, targeted harmonisation (Pillar 1) focuses on specific areas where divergence generates disproportionate cross-border externalities. Rather than pursuing comprehensive codification, the EU should prioritise those elements of insolvency law that directly affect capital markets integration and cross-border restructuring efficiency. This incremental approach enhances legal coherence while remaining consistent with subsidiarity.

Second, financial market regulation (Pillar 2) operates as an indirect but powerful driver of coherent insolvency outcomes. EU prudential rules, supervisory convergence, and resolution frameworks reduce the probability and systemic impact of disorderly insolvencies. By strengthening ex ante resilience and structuring crisis management, financial regulation mitigates fragmentation even where substantive insolvency law remains nationally diverse. This pillar rests on solid Treaty competences and therefore represents the most legally robust instrument for convergence.

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<sup>115</sup> Vallender H. (2013), *The Role of the Judge in the Restructuring of Companies Within Insolvency*, In: *The Role of the Judge in Nomination, Supervision and Removal of the Insolvency Representative: Judicial Wing INSOL Europe*, Nottingham.

Third, transparency and soft law (Pillar 3) address informational fragmentation. Divergence in itself does not necessarily produce inefficiency; unpredictability does. A European Insolvency Portal with standardised, machine-readable data and harmonised performance indicators would substantially reduce due diligence costs and information asymmetries. Complementary soft-law instruments, such as a model SME restructuring framework, can guide national reforms without imposing uniform solutions.

Fourth, the optional “28th regime” (Pillar 4) provides a structural solution for cases where coordination between multiple national systems reaches its limits. Complex multinational corporate groups require procedural unity and predictability that national systems cannot always deliver. An optional European insolvency regime would create a self-contained, coherent framework for cross-border actors while preserving regulatory competition and Member State sovereignty for purely domestic matters.

Insolvency law will likely never be fully unified across the EU. Nor is full uniformity a prerequisite for a functioning internal market. What is required is coherence where it matters most. A four-pillar approach allows the EU to preserve Member State autonomy in socially sensitive areas, strengthen financial stability and capital markets integration, reduce transaction costs and legal uncertainty, and provide a scalable framework for future integration.



**Author:**

Dr. Anastasia Kotowski, LL.M., Head of Department Financial Markets & Information Technologies  
[kotowski@cep.eu](mailto:kotowski@cep.eu)

**Centrum für Europäische Politik** FREIBURG | BERLIN  
Kaiser-Joseph-Straße 266 | D-79098 Freiburg  
Schiffbauerdamm 40 Raum 4205 | D-10117 Berlin  
Phone + 49 761 38693-0

The **Centrum für Europäische Politik** FREIBURG | BERLIN, the **Centre de Politique Européenne** PARIS, and the **Centro Politiche Europee** ROMA form the **Centres for European Policy Network** FREIBURG | BERLIN | PARIS | ROMA.

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