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Introduction to Recognition under Chapter 15

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Given the globalization of our economy, cross-border insolvencies and debt restructurings are becoming more commonplace. The Bankruptcy Code provides a mechanism to assist in the administration of such cross-border cases. Indeed, one of the key components of the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA) was the addition of chapter 15 to the Bankruptcy Code.¹ Chapter 15, which is based on the United Nations Commission for International Trade Law (UNCITRAL) Model Law on Cross Border Insolvency (Model Law), was enacted to address certain objectives set forth in §1501 of the Bankruptcy Code, including:

- cooperation between U.S. and foreign courts;
- greater legal certainty for trade and investment;
- fair and efficient administration of cross-border insolvencies that protects the interests of all creditors and other interested parties;
- protection and maximization of the value of the debtor's assets; and
- facilitation of the rescue of financially troubled businesses.

Several countries, including Mexico, Canada, Great Britain and Japan, have enacted legislation based on the Model Law.

According to the legislative history, chapter 15 was designed to be the "exclusive door to ancillary assistance to foreign proceedings" in the U.S. H.R.

¹ Prior to Oct. 17, 2005, requests for assistance in connection with a cross-border case were governed by former §304 of the Bankruptcy Code.

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Rep. 109-031, 110 (2005). Although ancillary assistance can come in a variety of forms, the culmination of a chapter 15 case is generally "recognition." Indeed, chapter 15 functions through recognition of a foreign proceeding. See *In re Condor Insurance Limited*, 2010 WL 961613, *4 (5th Cir. March 17, 2010). Given that U.S. courts are frequently called upon to assist in the administration of many foreign proceedings, it is crucial that new and younger lawyers are aware of chapter 15 and understand the basics of the recognition process.

as "the entry of an order granting recognition of a foreign main proceeding or foreign nonmain proceeding." 11 U.S.C. §1502. Nevertheless, a court may grant provisional relief upon the filing of a chapter 15 petition and before recognition if it is "urgently needed to protect the assets of the debtor or the interests of creditors." 11 U.S.C. §1519. Substantive relief is usually reserved, however, until recognition of the foreign proceeding. See *In re Condor*, 2010 WL 961613, at *2; 11 U.S.C. §§1521.

Requirements for Recognition

Recognition of a foreign proceeding is relatively straightforward and indeed has been characterized as "formulaic." *In re Bear Stearns High Grade Structured Credit Strategies Master Fund Ltd.*, 374 B.R. 122, 126 (Bankr. S.D.N.Y. 2007) (*Bear Stearns I*), *aff'd.*, 389 B.R. 325

Building Blocks

The Chapter 15 Petition



Douglas E. Deutsch

A case under chapter 15 is commenced, like other bankruptcy cases, by the filing of a petition. See 11 U.S.C. §1504. Although a chapter 15 petition may look like any other bankruptcy petition, it has a much more limited effect than a chapter 7, 11 or 13 petition. For example, a chapter 15 petition is not an "order for relief" and does not result in the imposition of the automatic stay. Moreover, the filing of a chapter 15 petition does not create a bankruptcy estate under §541 of the Bankruptcy Code. A chapter 15 petition can be described as a request for "recognition," which is defined

(S.D.N.Y. 2008). The requirements for recognition are set forth in §1517 of the Bankruptcy Code. In particular, a foreign proceeding shall be recognized if (1) the foreign proceeding is a foreign main or foreign nonmain proceeding, (2) the petition for recognition was filed by a foreign representative and (3) the petition satisfies all of the requirements under §1515. 11 U.S.C. §1517. "By establishing a simple, objective eligibility requirement for recognition, Chapter 15 promotes predictability and reliability." *In re Bear Stearns High Grade Structured Credit Strategies Master Fund Ltd.*, 389 B.R. 325, 333 (S.D.N.Y. 2008) (*Bear Stearns II*). Assuming all three criteria are satisfied, recognition should only be denied if recognition would be "manifestly contrary to the public policy of the United States." *In re Ephedra Products*

Definition of a Foreign Proceeding

A prerequisite for commencing a chapter 15 case is a “foreign proceeding.” Under chapter 15, a foreign proceeding is defined as “a collective judicial or administrative proceeding in a foreign country, including an interim proceeding, under a law relating to insolvency or adjustment of debt in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation.” 11 U.S.C. §101(23). The definition includes both solvent and insolvent debtors. *See 2 Collier on Bankruptcy*, ¶ 101.24 (15th ed. rev. 2009) (phrase “adjustment of debt” was added to definition to ensure that solvent debtor could be subject of foreign proceeding).

The definition of foreign proceeding consists of the following key components: (i) a collective judicial proceeding, (ii) in which the assets and affairs of the debtor are subject to control or supervision by a foreign court, (iii) for the purpose of reorganization or liquidation and (iv) under a law relating to insolvency or adjustment of debt. *See In re Betcorp Ltd.*, 400 B.R. 266, 277 (Bankr. D. Nev. 2009). Courts have recognized foreign liquidations, administrations, bankruptcies, schemes of arrangement and company voluntary arrangements as foreign proceedings under chapter 15. A receivership, which is typically instituted at the request and for the benefit of a single secured creditor, however, would likely not qualify as a foreign proceeding given that it is not collective (*i.e.*, does not consider the rights and obligations of creditors generally).

First Requirement: The Foreign Proceeding

In order to be eligible for recognition under chapter 15, a foreign proceeding must qualify as either a foreign “main” proceeding or a foreign “nonmain” proceeding. If the foreign proceeding is not foreign main or foreign nonmain, “a court should not grant recognition and is not authorized to use its power to effectuate the purposes of the foreign proceeding.” *Bear Stearns II*, 389 B.R. at 334.

Foreign Main Proceeding

A foreign main proceeding is defined as “a foreign proceeding pending in the country where the debtor has the center of its main interests.” 11 U.S.C. §1502(4). Chapter 15 does not define what constitutes a debtor’s “center of main interests” (also known as “COMI”).² Chapter 15, however, provides that “in absence of evidence to the contrary, the debtor’s registered office, or habitual residence in the case of an individual, is presumed to be the center of the debtor’s main interests.” 11 U.S.C. §1516(c). This presumption may be rebutted. *See Bear Stearns II*, 389 B.R. at 335-336. The Bankruptcy Code, however, does not provide any guidance as to what evidence would be sufficient to rebut the presumption. *See In re Basis Yield Alpha Fund (Master)*, 381 B.R. 37, 47 (Bankr. S.D.N.Y. 2008).

U.S. Courts are required to consider chapter 15’s international origins when called upon to interpret its provisions. *See* 11 U.S.C. §1508. Therefore, in analyzing COMI, U.S. courts have looked to the *Guide to Enactment of the UNCITRAL Model Law on Cross-Border Insolvency*, which explains that the COMI concept is derived from the European Convention on Insolvency Proceedings (EU Convention). Courts have noted that the regulation that adopted the EU Convention defines COMI as “the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties.” *See, e.g., In re Tri-Continental Exchange Ltd.*, 349 B.R. 627, 634 (Bankr. E.D. Cal. 2006). This concept has been equated with “principal place of business” in the U.S. *See In re Tri-Continental Exchange Ltd.*, 349 B.R. 627, 634 (Bankr. E.D. Cal. 2006). In determining a corporate debtor’s COMI, U.S. courts may consider a long list of factors, including:³

- the location of the debtor’s headquarters;
- the location of those who actually manage the debtor (which conceivably could be the headquarters of a holding company);
- the location of the debtor’s primary assets;

² COMI and the decisions analyzing COMI have been the subject of significant discussion and debate. For purposes of this introductory article, we limit our discussion to a brief overview on the subject.

³ “Factors that are useful in instances where the debtor is an individual include: the location of a debtor’s primary assets; the location of the majority of the debtor’s creditors or a majority of creditors [that] would be affected by the case; and the jurisdiction whose law would apply to most disputes.” *In re Loy*, 380 B.R. 154, 162 (Bankr. E.D. Va. 2007) (citations omitted).

- the location of the majority of the debtor’s creditors or of the majority of the creditors who would be affected by the case;
- the jurisdiction whose law would apply in most disputes; and
- the jurisdiction in which the debtor is organized and/or registered, and as what kind of business entity (*e.g.*, corporation, limited liability company, general or limited partnership, business trust, etc.).

See, e.g., Bear Stearns II, 389 B.R. at 336; *In re Basis Yield*, 381 B.R. at 56-57; *In re SPhinX Ltd.*, 351 B.R. 103, 117 (Bankr. S.D.N.Y. 2006), *aff’d.*, 371 B.R. 10 (S.D.N.Y. 2007).

Upon considering these factors, several courts have refused to grant recognition to Cayman Islands’ liquidations of hedge funds registered as exempted companies in the Cayman Islands on the basis that such hedge funds did not have their COMI in the Cayman Islands.⁴ Nevertheless, the U.S. Bankruptcy Court for the District of Delaware recently granted recognition to the liquidation of such a hedge fund as foreign main after considering evidence supporting the allegation that the debtor’s COMI was the Cayman Islands. Transcript of Proceedings at 19, *In re Saad Investments Finance Co. (No. 5)*, Case No. 09-13985 (Bankr. D. Del. Dec. 4, 2009).

Foreign Nonmain Proceeding

A foreign nonmain proceeding refers to a foreign proceeding pending in a country where the debtor has an “establishment.” 11 U.S.C. §1502(5). An establishment is defined as “any place of operations where the debtor carries out a non-transitory economic activity.” 11 U.S.C. §1502(2). There are very few decisions analyzing the Bankruptcy Code’s definition of a foreign nonmain proceeding. The few courts that have addressed the issue have interpreted it to mean a “local place of business.” *See, e.g., Bear Stearns I*, 374 B.R. at 131. A foreign proceeding premised only on the presence of assets in the foreign country, however, will not qualify as a foreign nonmain proceeding and therefore will not be eligible for recognition.

⁴ Under Cayman Islands law, an exempted company is prohibited from engaging in business in the Cayman Islands except in furtherance of its business conducted outside of the Cayman Islands. *See Bear Stearns I*, 374 B.R. at 131. Therefore, courts have questioned how a hedge fund registered as exempted company in the Cayman Islands could have its COMI there. *In re Basis Yield*, 381 B.R. at 49.

Second Requirement: The Foreign Representative

Under §1517, a foreign proceeding may only be recognized if the “foreign representative” applying for recognition is a person or body. A foreign representative is defined as:

a person or body, including a person or body appointed on an interim basis, authorized in a foreign proceeding to administer the reorganization or the liquidation of the debtor’s assets or affairs or to act as a representative of such foreign proceeding.

11 U.S.C. §101(24).

The definition is extremely broad and may include a company’s board of directors, so long as the board has the authority to administer the reorganization or liquidation of the company’s assets or affairs. *See In re Board of Directors of Hopewell Int’l. Ins. Ltd.*, 238 B.R. 25, 53 (Bankr. S.D.N.Y. 1999) (board of directors qualifies as foreign representative under former §304 of the Bankruptcy Code), *aff’d.*, 275 B.R. 699 (S.D.N.Y. 2002). This requirement is typically relatively easy to address.

Third Requirement: The Petition Must Satisfy §1515 Procedural Hurdles

Pursuant to §1515 of the Bankruptcy Code, a chapter 15 petition must be accompanied by (1) a certified copy of the decision commencing the foreign proceeding and appointing the foreign representative, (2) a certificate from the foreign court affirming the existence of the foreign proceeding and appointment of the foreign representative or (3) in the absence of either of these, any other evidence acceptable to the court of the existence of the foreign proceeding and appointment of the foreign representative. In addition, a petition must be accompanied by a statement identifying all foreign proceedings with respect to the debtors that are known to the foreign representative.⁵ In most instances, there is likely to be little, if any, dispute regarding this requirement.

⁵ Although not a requirement for recognition, Rule 1007(a)(4) of the Federal Rules of Bankruptcy Procedure requires that a chapter 15 petition be accompanied by (1) a corporate ownership statement and (2) “a list containing the names and addresses of all persons or bodies authorized to administer foreign proceedings of the debtor, all parties to litigation pending in the United States in which the debtor is a party at the time of the filing of the petition, and all entities against whom provisional relief is being sought under §1519 of the Code.”

Relief Available Upon Recognition

Assuming that the three requirements for recognition are satisfied, §1517(a) of the Bankruptcy Code provides that “after notice and a hearing, an order recognizing a foreign proceeding shall be entered.” Section 1517(c) provides that “[a] petition for recognition of a foreign proceeding shall be decided upon at the earliest possible time.” Given the notice requirements set forth in Bankruptcy Rule 2002(q), it is possible that a court could issue an order granting recognition within 21 days after the filing of the chapter 15 petition.⁶

Pursuant to §1509(b) of the Bankruptcy Code, upon recognition (1) “the foreign representative has the capacity to sue and be sued in a court in the United States,” (2) “the foreign representative may apply directly to a court in the United States for appropriate relief in that court” and (3) “a court in the United States shall grant comity or cooperation to the foreign representative.” Prior to recognition, a foreign representative will not be able to avail himself of the U.S. courts with one exception: under §1509(f) of the Bankruptcy Code, a foreign representative may bring an action in a court in the U.S. to collect or recover a claim which is the property of the debtor, such as an account receivable. *See* 11 U.S.C. §1509(f). In addition, a foreign representative may take actions that do not require judicial assistance (*e.g.*, exercising shareholder voting rights) before recognition. *See, e.g., In re Iida*, 377 B.R. 243, 258 (B.A.P. 9th Cir. 2007); *see also In re Loy*, 380 B.R. 154, 166 (Bankr. E.D. Va. 2007) (holding that recognition was not prerequisite to filing *lis pendens*).

As described above, chapter 15 draws a distinction between a foreign main proceeding and a foreign nonmain proceeding. Upon recognition of a foreign main proceeding, certain protections arise automatically in favor of the foreign debtor under §1520 of the Bankruptcy Code, including the imposition of an automatic stay under

⁶ Pursuant to Bankruptcy Rule 2002(q), “the debtor, all persons or bodies authorized to administer foreign proceedings of the debtor, all entities against whom provisional relief is being sought under §1519 of the Code, all parties to litigation pending in the United States in which the debtor is a party at the time of the filing of the petition, and such other entities as the court may direct” must be given at least 21 days’ notice of the hearing on the petition for recognition. A literal reading of Rule 2002(q) would suggest that notice not be given to all creditors. However, absent notice of the chapter 15 petition, an order granting recognition to a foreign proceeding would likely violate U.S. creditors’ rights. Thus, notice of a chapter 15 petition should be given to all U.S. creditors. Pursuant to Bankruptcy Rule 1011, any “party in interest” to a chapter 15 case may contest the petition.

§362, pursuant to which parties are enjoined from continuing or commencing any actions against the foreign debtor or its assets. Recognition as a foreign main proceeding is advantageous because it eliminates the procedural hurdle of having to seek court approval for a stay or related relief. However, as noted by the U.S. Bankruptcy Court for the Southern District of New York, the main vs. nonmain designation ultimately may have little consequence beyond timing and procedural issues “since the chapter [15] gives the bankruptcy court the ability to grant substantially the same types of relief in assistance of foreign nonmain proceedings as main proceedings.” *In re SPhinx Ltd.*, 351 B.R. at 116.

Section 1521 of the Bankruptcy Code provides, in pertinent part, that “[u]pon recognition of a foreign proceeding, whether main or nonmain, where necessary to effectuate the purpose of this chapter and to protect the assets of the debtor or the interests of creditors, the court may grant any appropriate relief.” 11 U.S.C. §1521. According to the legislative history of §1521, “[t]his section does not expand or reduce the scope of relief currently available in ancillary cases under sections 105 and 304.” H.R. Rep. No. 109-031, 116 (2005). Therefore, whether a foreign proceeding is main or nonmain, §1521 allows a court to grant relief, including injunctive relief, to assist the administration of the foreign proceeding. In determining whether to grant injunctive relief under §1521, a court must consider the traditional standards for injunctive relief.

Public Policy Considerations

It is also important to note that chapter 15 provides that “[n]othing in this chapter prevents the court from refusing to take an action governed by this chapter if the action would be manifestly contrary to the public policy of the United States.” *See* 11 U.S.C. §1506. In general, other than allegations that the petitioner failed to satisfy any of the three requirements of §1517(a) of the Bankruptcy Code, the only ground to object to the recognition of a foreign proceeding would be that such recognition would be manifestly contrary to U.S. public policy. As the legislative history explains and the courts have noted, this public-policy exception should be narrowly construed and only “invoked when the

most fundamental policies of the United States are at risk.” *In re Ernst & Young, Inc.*, 383 B.R. 773, 781 (Bankr. D. Colo. 2008); *see also In re Ephedera Products Liability Litigation*, 349 B.R. 333, 336 (S.D.N.Y. 2006) (holding that denial of constitutional right to jury trial was not manifestly contrary to U.S. public policy where claimants were assured of fair hearing).

Conclusion

Although recognition of a foreign proceeding is designed to be relatively expeditious and straightforward, it is well established that recognition should not be “rubber stamped” by the courts. *Bear Stearns I*, 374 B.R. 126; *In re Basis Yield*, 381 B.R. at 40. Indeed, the mere fact that recognition is unopposed will not preclude a court from analyzing the pleadings to determine whether the petitioner has satisfied its burden. A petitioner should make every effort to demonstrate that it has satisfied its burden of meeting the requirements for recognition set forth in §1517 of the Bankruptcy Code. Once the court is satisfied that the petition and the foreign proceeding meet the requirements of chapter 15, and in particular §§1502 and 1517, recognition should be granted, unless such recognition would be manifestly contrary to United States public policy. ■

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