INTERNATIONAL ASSOCIATION OF YOUNG LAWYERS

THE QUEST FOR COORDINATION OF PROCEEDINGS IN CROSS BORDER INSOLVENCY CASES

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1. **Do you have the notion in your legal system of main insolvency proceedings. Is this notion procedural or substantial? Is this notion purely international or also domestic?**

The notion of "main insolvency proceedings" only exists in the context of the UNICTRAL Model Law on Cross-Border Insolvency — codified as Title 11, United States Code § 1501 *et seq* ("Chapter 15"). Under the uniform structure of Chapter 15, the notion is substantive rather than procedural — as a foreign insolvency can be recognized in the United States as a "foreign main proceeding" or a "foreign *nonmain* proceeding." Whether a foreign proceeding is recognized as "main" or "nonmain" may greatly vary the rights afforded to the bankrupt person or entity ("petitioner").

The notion of "main" versus "nonmain" is linked to the center of main interests ("COMI") analysis. Courts have looked to a variety of factors in determining a debtor's center of main interests. For example, in In re Fairfield Sentry Ltd., 714 F. 3d 127, 137 (2d Cir. 2013), the court looked to the debtor's activities at or around the time the debtor filed for Chapter 15 as well as the debtor's activities between the filing of the foreign insolvency proceeding and the filing of the Chapter 15 to prevent any bad faith manipulation of the debtor's center of main interests. In In re SPhinX, Ltd., 351 BR. 103, 117 (Bankr. S.D.N.Y. 2006), the court considered the debtor's location of its headquarters, managers and officers, assets, creditors, and the jurisdiction whose law would apply to most of the debtor's disputes. The court noted that no single factor can be determinative and the analysis invites flexibility in its application.

A "foreign main proceeding" is one where the insolvency proceeding is pending in the country where the debtor has its "COMI." See § 1517(b)(1). Recognition of a foreign insolvency proceeding as a "foreign main proceeding" entitles the petitioner to automatic relief under § 1520, which includes (a) the benefit of a stay of all actions or execution against the debtor's property within the territorial jurisdiction of the United States; (b) the ability to sell the petitioner's assets under the aegis of the U.S. Federal Bankruptcy Court (including selling property free of any liens or encumbrances); (c) the ability to recover the petitioner's assets to the extent they have been fraudulently transferred pursuant to U.S. law; and (d) the ability to operate the petitioner's business and exercise the powers of a trustee over such business. See § 1520(a).

By contrast, recognition of a foreign insolvency proceeding as a "foreign nonmain proceeding" does not bring with it any automatic relief under § 1520. Notwithstanding, a petitioner may always apply for discretionary relief under § 1521, which includes the option to seek a stay of all actions or execution upon the debtor's property in the United States, and examination of witnesses and the taking of evidence, as well as entrusting the administration of the debtor's assets within the United States to the foreign representative of the foreign insolvency proceeding. See § 1521(a). Such relief may be requested at the initial recognition stage; however, the petitioner has the burden of showing that the relief is necessary to effectuate the purpose of Chapter 15 and to protect the assets of the debtor or the interests of the United states creditors. It should also be noted that recognition of foreign insolvency proceeding, whether "main" or "nonmain," always entitles a petitioner to sue or be sued in any U.S. Court, which are directed to grant the petitioner comity or cooperation. See § 1509.

The notion of "main" versus "nonmain" proceedings does not apply to domestic insolvency proceedings commenced under any Chapter of the U.S. Federal Bankruptcy Code other than Chapter 15. To that extent, the notion is purely international.

2. **Do you know the notion of secondary insolvency proceedings? Is this notion purely international or also domestic?**

Other than "nonmain" proceedings under Chapter 15—described above—there is no notion of "secondary" insolvency proceedings under the U.S. Federal Bankruptcy Code. As such, the notion is purely international.

3. **Are the material effects of the main proceedings halted when secondary proceedings elsewhere are opened? Please specify, if this is not the case, whether or not the law of the State in which main proceedings are opened shall affect certain rights of third parties or have effect in certain contractual relations, e.g. labour contracts.**

No. In the context of "main" and "secondary" insolvency proceedings, the U.S. Federal Bankruptcy Courts are governed by the wholesale or nearly wholesale adoption of the UNCITRAL Model Law on Cross-Border Insolvency. Chapter 15 expressly contemplates that, where foreign insolvency proceedings require the assistance of the U.S. Courts, a "foreign representative" of such insolvency (typically a foreign trustee or a person specially appointed by the foreign court to seek recognition in the U.S.) may apply to a U.S. Federal Bankruptcy Court for recognition.

The process is not intended to halt the foreign proceeding but rather to grant assistance, comity, and cooperation to the foreign representative. See § 1509(b). The foreign representative also gains access to sue or be sued in U.S. Courts. See id. Indeed, the stated purposes of Chapter 15 are to promote (a) cooperation between U.S. Courts, debtors, and trustees on one hand, and foreign courts and competent authorities involved in such insolvency proceedings on the other hand; (b) the fair and efficient administration of cross-border insolvencies; (c) protect the interest of *all* creditors and interested parties; (d) protect and maximize the bankrupt's assets; and (e) facilitate the rescue of financially troubled businesses. See § 1501(a).

Typically, the law of the State in which the foreign insolvency proceeding is pending will greatly affect the proceedings in the U.S. under Chapter 15. Although ultimately a Chapter 15 proceeding is governed by U.S. law, U.S. Courts frequently employ foreign law when determining what is in the best interests of creditors. For example, published decisions under Chapter 15 have included the consideration or application of Canadian, British Virgin Island, Brazilian, German, Mexican, and Japanese law in determining the underlying rights of the parties. Additionally, under §§ 1525—27, the U.S. Federal Bankruptcy Courts, or its appointed trustees or representatives, are empowered to liaise directly with the foreign court or its representatives to promote cooperation and efficient administration.

The application of foreign law is subject to at least two caveats. First, under § 1506, a U.S. Federal Bankruptcy Court *may* refuse to take an action under Chapter 15 that would

be manifestly contrary to the public policy of the United States. However, the provision is invoked only under extraordinary circumstances as the general rule is that comity should be granted. See § 1509(b). Second, to the extent a provision or act under Chapter 15 conflicts with the treaty or international agreement obligations of the U.S. and a foreign country, such treaty or agreement requirements prevail.

4. **Shall the creditors have the right to lodge claims in any of the insolvency proceedings (main and secondary)?**

Chapter 15 does not automatically establish a claims procedure for U.S. or foreign creditors to lodge claims in the *U.S. Chapter 15 proceeding* against the foreign bankruptcy person or entity—although the U.S. Federal Bankruptcy Court may establish a claims procedure under U.S. law. More typically, a proceeding under Chapter 15 is used to recognize procedures or orders that the foreign court establishing as its own claim procedure. That is, the U.S. Federal Bankruptcy Court may order U.S. creditors to file what, in the typical U.S. insolvency parlance, is called a "proof of claim" in compliance with the procedures of the foreign court. Chapter 15 does not prohibit any creditor from lodging a claim against the foreign bankrupt person or entity in any other foreign court. In fact, as a requirement to allow a foreign representative to administer the assets of a foreign debtor, it is required that U.S. creditors be sufficiently protected.

5. **Are the dividends in all proceedings pooled? In other words, are dividends obtained in proceeding X deducted from dividends to be obtained in other proceedings?**

Under Chapter 15, there is no specific procedure for distributing or administering the assets of a bankruptcy estate other than the right to do so without discriminating against U.S. creditors. Given, however, the numerous provisions under Chapter 15 providing for assistance, cooperation, and comity to the foreign insolvency proceeding, it is unlikely that assets would be distributed in a manner that would be inconsistent with the foreign proceeding's procedures.

6. **If by liquidation of assets in any secondary proceedings it is possible to meet all claims, shall the liquidator transfer any remaining assets to the liquidator in the main proceedings?**

The "liquidator," or foreign representative of the foreign insolvency proceeding before the U.S. Federal Bankruptcy Court is frequently the same trustee, liquidator, or administrator of the foreign insolvency proceeding. Accordingly, it is common that the foreign representative will liquidate assets in the U.S. and direct the proceeds to be administered in the foreign proceeding.

There is nothing under Chapter 15 that requires the foreign representative to return the proceeds of the estate's assets to the foreign proceeding. Indeed, a foreign representative could commence a wholly separate and concurrent insolvency proceeding under other provisions of the U.S. Bankruptcy Code and administer the assets of the foreign bankrupt in such proceeding. See § 1523, 1528—32. However, a concurrent proceeding under the U.S. Bankruptcy Code is appropriately limited by the relief sought in a Chapter 15 proceeding. See §§ 1528—32. More commonly, the proceeds would be

transferred to the foreign representative in the foreign proceeding and distribution thereof thereafter would be governed as per local law of the foreign main preceding.

7. **Does the so-called «dominance» of the main proceedings create a leading role for the liquidator, appointed in the main proceedings, to coordinate all insolvency proceedings pending against the same debtor?**

Chapter 15 does not impose any affirmative requirement on the liquidator in the foreign main proceeding. In fact, a Chapter 15 proceeding in the U.S. is commenced by the filing of a petition by the "foreign representative," who is a person or body "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." See 11 U.S.C. § 101(24). Accordingly, the "foreign representative" need not be the liquidator in the foreign main proceeding. That is not to say there are not substantial obligations imposed on the foreign representative to protect the interests of *all* creditors, the bankrupt, and other interested parties. See § 1522(a) (the U.S. Federal Bankruptcy Court may grant relief to the foreign representative "only if the interests of the creditors and other interested entities, including the debtor, are sufficiently protected.").

Moreover, the dominance of a foreign main proceeding is most apparent in the provisions governing conflicting foreign main and nonmain proceedings. For example, pursuant to § 1530, the U.S. Federal Bankruptcy Courts are directed, when recognizing foreign nonmain proceedings, to (a) only grant relief consistent with the *main* proceeding; and (b) grant, modify, or terminate additional relief in the nonmain proceeding so as to be consistent with the recognition of the main proceeding. To that extent, a foreign representative cannot seek relief in support of a foreign nonmain proceeding to a greater extent than it would be available in connection with the "main" insolvency proceeding.

Finally, if a foreign representative is denied recognition of a foreign insolvency proceeding—whether main or nonmain—the U.S. Federal Bankruptcy Court denying recognition may issue an order preventing the foreign representative from obtaining comity or cooperation from any other U.S. court. See § 1509(d). This too can be used by creditors as a tool to ensure that the foreign representative is not seeking recognition and relief of a "nonmain" proceeding in a manner that would be inconsistent with and potentially prejudicial to a "main" insolvency proceeding.

8. **How do you think the above mentioned issues have been tackled by the new EU Regulation on Transnational Insolvency? If yes, in which way defective or useful?**

The UE Regulations on Transnational Insolvency are wholly inapplicable in proceedings in the United States. That said, the United States has developed common law preventing debtors from attempting to manipulate COMI after insolvency has commenced.

9. **How do you think the above mentioned issues have been tackled by the UNCITRAL Model Law on Cross-Border Insolvency? If yes, in which way defective or useful?**

In the United States, the UNCITRAL Model Law on Cross-Border Insolvency—*i.e.*, Chapter 15 of the U.S. Federal Bankruptcy Code—has been useful in dealing with the

above issues. The procedures implemented by Chapter 15 have replaced what was before a very uncertain area of U.S. bankruptcy law under previous 11 U.S.C. § 304.

Since its implementation in 2005, a substantial body of jurisprudence has arisen to aid in the interpretation of Chapter 15. U.S. Courts are also instructed to follow, and are indeed guided by, the decisions of foreign jurisdictions which have adopted similar statutes. See § 1508. In that sense, the Model Law and Chapter 15 provide a good framework for dealing with cross-border insolvency issues and can evolve concomitantly with the jurisprudence of other jurisdictions.

10. Are there other salient aspects of the EU Regulation on Transnational Insolvency or the UNCITRAL Model Law on Cross-Border Insolvency that are key to answer the need and quest for coordination in cross borders insolvency proceedings?

Again, the UE Regulations are inapplicable in the U.S. That said, the provisions of the Model Law dealing with cooperation and direct communication between courts and there representatives are often underused in the resolution of cross-border insolvencies. See §§ 1525—27. A different set of rules in different jurisdictions does not assist in this objective. The cooperation provisions nonetheless are opinion key to answer the need and quest for coordination between the various courts administering cross-border insolvencies. As iIn the UK, where both the model law and the regulations are often analyzed in tandem, similar analyses by other courts in the EU may be of assistance.

11. Are there other devices that the EU Regulation on Transnational Insolvency or the UNCITRAL Model Law on Cross-Border Insolvency should have regulated or adopted to enhance further coordination in cross borders insolvency proceedings?

There may be room to solidify the issues pertinent to the COMI analysis set forth by US courts in other jurisdiction. For example, U.S. courts often look to a variety of factors in making this determination. See In re SPhinX, Ltd., 351 BR. 103, 117 (Bankr. S.D.N.Y. 2006) (the court considered the debtor's location of its headquarters, managers and officers, assets, creditors, and the jurisdiction whose law would apply to most of the debtor's disputes. The court noted that no single factor can be determinative and the analysis invites flexibility in its application). Perhaps these factors can be codified for greater clarity in the laws of the U.S. and other jurisdictions to lend greater certitude in the ultimate result of the application of the Model law.

Also, the issue of whether the debtor's COMI can be manipulated lacks a clear answer. Some courts have addressed the issue. For example, in In re Fairfield Sentry Ltd., 714 F. 3d 127, 137 (2d Cir. 2013), the court looked to the debtor's activities at or around the time the debtor filed for Chapter 15 as well as the debtor's activities between the filing of the foreign insolvency proceeding and the filing of the Chapter 15 to prevent any bad faith manipulation of the debtor's center of main interests. Courts are conflicted on this issue, which should be, and I understand is, addressed in more recent revisions to the Model law.

Additionally, courts can curtail abuse by placing the onus on the foreign representative to affirmatively establish COMI. In In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd., 374 B.R. 122 (Bankr. S.D.N.Y. 2007), the court considered the propriety of granting "foreign main proceeding" status where the debtor gave little or no evidence that its COMI was in the Cayman Islands. Without a showing of the debtor's COMI, or even a showing of an "establishment" in the Cayman Islands to establish "foreign *nonmain* status," the court denied recognition wholesale. Id. at 132. The court reiterated that, even absent a dispute, a debtor must show that it is affirmatively entitled to recognition.

The ability for opportunistic debtors to forum shop and manipulate their ability to administer insolvency proceedings favorably by establishing favorable COMIs should affirmatively be addressed by any regulations or amendments to the Model law as to make such determinations uniform among nations.