

# Chapter 15: Navigating Cross-Border Insolvency Proceedings

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## Introduction

This memorandum will discuss the law governing cross-border insolvency proceedings from its origins in the UNCITRAL Model Laws to its application in the U.S. bankruptcy court in the form of Chapter 15. As an overview, this memorandum will focus on Chapter 15 with sections that discuss (1) cross-border insolvency in general; (2) the purpose and scope of Chapter 15; (3) the procedure; (4) the provisional relief; (5) contesting recognition; (6) “main” and “nonmain” recognition; (7) automatic and discretionary relief; and (8) cooperation and coordination.

## Cross Border Insolvency

Insolvency occurs when a person or entity is unable to pay debts as they are due. The legal meaning of an insolvency proceeding varies both substantively and procedurally depending on the national jurisdiction. When insolvent debtors operate businesses, own assets, or owe money to creditors in foreign countries, problems arise because the interested parties cannot be reasonably assured that the outcome of the foreign insolvency proceeding will conform to their expectations based on the laws of their jurisdiction. Mark G. Douglas, Global Focus: Foreign Insolvency Proceedings Recognized Under New Chapter 15 of the Bankruptcy Code, 38 UCC L. J. 1, 6 (2006).

In 1997, the United Nations Commission on International Trade Law (“UNCITRAL”) created the Model Laws on Cross-Border Insolvency to remedy the disconnect that occurs in cross-border insolvency proceedings. The Model Laws focus on four elements of cross-border insolvency: (1) foreign representatives and creditors access to insolvency proceedings in foreign courts; (2) recognition of foreign insolvency proceedings and relief in local courts;

(3) relief to debtors and creditors; and (4) cooperation among courts with concurrent insolvency proceedings. United National Commission on International Trade Law, 1997 WL 651489, 96 (1997). The Model Laws do not provide a universal insolvency code but rather a system to coordinate diverging insolvency laws of different jurisdictions.

### **Purpose and Scope of Chapter 15**

In 2005, the U.S. Congress used the Bankruptcy Abuse Prevention and Consumer Protection Act to adopt most of the Model Laws on Cross-Border Insolvency into its domestic Bankruptcy Code as Chapter 15. Alesia Ranney-Marinelli, Overview of Chapter 15 Ancillary and Other Cross-Border Cases, 82 Am. Bankr. L.J. 269, 269 (2008). Chapter 15 explicitly advances the same objectives as the UNCITRAL Model Law: (1) cooperation between U.S. bankruptcy courts and foreign insolvency courts and authorities, (2) greater legal certainty for trade and investment, (3) fair and efficient administration of cross-border insolvencies that protects the interests of all creditors and other interests, (4) protection and maximization of the debtor's assets, and (5) facilitation of the rescue of financially troubled businesses. 11 U.S.C § 1501(a).

In general, Chapter 15 treats cross-border insolvency proceedings as a single process wherein a court in one country administers the primary proceeding, and a court in another country assists that proceeding by conducting an ancillary proceeding. Most Chapter 15 cases are inbound requests for the U.S. bankruptcy court to assist a primary insolvency proceeding in a foreign country. 11 U.S.C § 1501 (b)(1). Alternatively, Chapter 15 cases can be an outbound request for a foreign court to provide assistance in a Title 11 U.S. bankruptcy proceeding. 11 U.S.C § 1501 (b)(2). Chapter 15 can also be used to coordinate information when a single debtor has a foreign proceeding and a Title 11 proceeding pending concurrently. 11 U.S.C § 1501 (b)(3). Lastly, foreign interested parties can use Chapter 15 to

initiate or participate in a Title 11 bankruptcy proceeding if they are eligible to do so. 11 U.S.C § 1501 (b)(4).

### **Procedure**

A party seeking to initiate an ancillary Chapter 15 case must file a petition for recognition of the “foreign proceeding” and the “foreign representative” to the U.S. bankruptcy court. 11 U.S.C § 1509. The petition must include documents showing the existence of all known foreign proceedings and the legitimate appointment of the foreign representative. 11 U.S.C § 1515. Foreign creditors are entitled to notice of the Chapter 15 petition with deadlines to file their unsecured and secured claims against the debtor. 11 U.S.C § 1514(a), (b), (c). Chapter 15 also dictates that foreign creditors have the same rights as domestic creditors with respect to commencing or participating in a bankruptcy proceeding. 11 U.S.C § 1513(a). Moreover, insolvency proceedings from countries that have not adopted the Model Laws are still eligible for recognition under Chapter 15. Alesia Ranney-Marinelli, Overview of Chapter 15 Ancillary and Other Cross-Border Cases, 82 Am. Bankr. L.J. 269, 330 (2008).

### **Provisional Relief**

Unlike Chapter 7 or 11, Chapter 15 does not afford the petitioner with automatic relief upon filing their petition. While the bankruptcy court evaluates recognition of the foreign proceeding, it may choose to grant provisional relief when the relief is urgently needed to protect debtor’s assets or creditors interests. 11 U.S.C. § 1519(a). Provisional relief may include executing a stay against the debtor’s assets, entrusting the assets to a foreign representative, suspending the right to transfer the debtor’s assets, or gathering evidence concerning the debtor’s assets. 11 U.S.C. § 1519(a). For example, the court granted the debtor provisional stay relief in In re Pro-Fit Holdings Ltd., 391 B.R. 850, 858 (Bankr. C.D. Cal. 2008), pending the recognition of the United Kingdom insolvency proceeding. However,

provisional relief can only be granted if the bankruptcy court is certain that the interests of both creditors and debtors are “sufficiently protected.” 11 U.S.C. § 1522(a). Moreover, any provisional relief terminates when the court makes its final determination on recognition. 11 U.S.C. § 1519(b).

### **Contesting Recognition**

Contesting recognition of a foreign proceeding is an important tool for interested parties that fail to benefit from Chapter 15. Contestants can argue that the foreign proceeding or the foreign representative do not qualify for recognition. FRBP Rule 1011(a). Contestants can also argue that the goals of Chapter 15 would be better served by denying recognition. For instance, recognition could be denied if the foreign proceeding did not permit reorganization of the debtor’s assets even when doing so would maximize the value of the estate. Finally, contestants can argue that a Chapter 15 recognition would be “manifestly contrary” to public policy. 11 U.S.C. § 1506. For example, if foreign laws allow for discriminatory treatment based on nationality, then the court will likely decide that disparate treatment of creditors based on nationality goes against American public policy. See In re Toft, 453 B.R. 186, 198 (Bankr. S.D. N.Y. 2011) (denying recognition of a foreign insolvency proceeding because the foreign representative’s motion for the U.S. based internet service provider to turn over the debtor’s private emails is “manifestly contrary to U.S. public policy.”).

### **“Main” and “Nonmain” Recognition**

If the bankruptcy court grants recognition, it must categorize the foreign proceeding as either “nonmain” or “main” because the debtor may have multiple insolvency proceedings in different countries. 11 U.S.C. § 1502(4), (5). A “nonmain” proceeding occurs if the debtor merely has an “establishment” of “non-transitory economic activity” in that country. 11 U.S.C. § 1502(2), (5). See In re Brit. Am. Ins. Co. Ltd., 425 B.R. 884, 916 (Bankr. S.D. Fla.

2010); In re SPhinX, Ltd., 351 B.R. 103, 122 (Bankr. S.D. N.Y. 2006), aff'd, 371 B.R. 10 (S.D. N.Y. 2007). A “main” proceeding occurs if the proceeding is pending in the country where the debtor has its “center of main interests” (COMI). 11 U.S.C. § 1502(4). See In re Betcorp Ltd., 400 B.R. 266, 292 (Bankr. D. Nev. 2009). Although a Chapter 15 petitioner designates a COMI in their petition, the United States Trustee<sup>1</sup> or interested party may challenge the designation with a motion for determination. 11 U.S.C. § 1516(a) (b); FRBP Rule 1004.2. Chapter 15 does not define COMI, but it does provide the rebuttable presumption that the debtor’s COMI is in the country of its registered office. 11 U.S.C. § 1516(c). Chapter 15 allows the bankruptcy court to consult the UNCITRAL Model Law or similar European regulations on cross-border insolvency for guidance on interpreting the meaning of COMI. 11 U.S.C. § 1508. For example, the California bankruptcy court in In re Tri-Continental Exchange Ltd., 349 B.R. 627, 633-34 (Bankr. E.D. Calif. 2006) consulted EU regulations that defined COMI as “the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties.”

### **Automatic and Discretionary Relief**

Recognition as a “main” proceeding triggers automatic stay relief for the debtor but only for property located in U.S. jurisdictions. 11 U.S.C. § 1520. Recognition also automatically triggers “adequate protection” of creditor’s interests in the debtor’s property and prevents the debtor from alienating real or personal property outside the ordinary course of business. Id. Moreover, the bankruptcy court may use its discretion to provide “additional assistance” if doing so would reasonably assure (1) just treatment of creditors, (2) protection of U.S. creditors against prejudice and inconvenience in the processing of claims in foreign proceedings, (3) prevention of preferential or fraudulent dispositions of property of the

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<sup>1</sup> The United States Trustee is charged with oversight of various aspects of bankruptcy filings in the United States.

debtor, (4) distribution of proceeds of the debtor's property substantially in accordance with the order of the Bankruptcy Code, and (5) if appropriate, the provisions of an opportunity for a fresh start for debtors. 11 U.S.C. § 1507(a), (b). The bankruptcy court may only exercise discretionary relief "if the interests of the creditors and other interested entities, including the debtor, are sufficiently protected." 11 U.S.C. § 1522(a).

In contrast, recognition as a "nonmain" proceeding does not automatically trigger any relief under Chapter 15. Alesia Ranney-Marinelli, Overview of Chapter 15 Ancillary and Other Cross-Border Cases, 82 Am. Bankr. L.J. 269, 307 (2008). Instead, the foreign representative must specifically request relief from the bankruptcy court. Id. The bankruptcy court will only use discretion to grant relief if it is necessary to fulfill a Chapter 15 purpose, such as protecting assets of the estate or interests of the creditors. 11 U.S.C. § 1521.

Recognition of a foreign "main" proceeding is proof that the debtor is generally not paying its debts unless there is evidence to the contrary. 11 U.S.C. § 1531. After the bankruptcy court recognizes the foreign "main" proceeding, the foreign representative is authorized to operate the domestic business of the foreign debtor with the power of a trustee. 11 U.S.C. § 1520(a)(3). The foreign representative can request discovery of the debtor's estate and distribution of debtor's assets to foreign creditors. 11 U.S.C. § 1521. In addition, the foreign representatives can initiate bankruptcy cases under other chapters of the Bankruptcy Code if the foreign debtor is eligible to be a U.S. debtor under 11 U.S.C. § 109. 11 U.S.C. §§ 1511, 1520(c), 1528.

### **Cooperation and Coordination**

Chapter 15 authorizes U.S. bankruptcy courts and trustees to communicate and coordinate directly with foreign courts or foreign representatives to advance cross-border cooperation. 11 U.S.C. §§ 1525, 1526. If a foreign debtor has multiple bankruptcy proceedings in the U.S., Chapter 15 dictates that the bankruptcy court harmonize the relief

decided in the Chapter 15 case with the relief in the other case. 11 U.S.C. § 1529(1), (2). The bankruptcy court must also coordinate the relief granted in “nonmain” foreign proceedings with foreign “main” proceedings. 11 U.S.C. § 1530. Furthermore, Chapter 15 asserts that creditors of a foreign debtor that have full or partial payment on their claims cannot seek compensation for the same claim under any chapter of the Bankruptcy Code. 11 U.S.C. §1532.

### **Conclusion**

The demand for international cooperation to adjudicate cross-border insolvency is self-evident in today’s globalized world economy. Chapter 15 is just one example of the fruit borne from international cooperation through various legal systems. Yet, U.S. bankruptcy courts are still in the early stages of developing the Chapter 15 case law, and there are many differences of opinion. In 2021, a Florida bankruptcy court refused to apply the section 109 requirement to Chapter 15 cases – meaning that a debtor does not need to reside or have a place of business domiciled in the U.S. to be eligible under Chapter 15. See In re Zawawi, 634 B.R. 11, 14 (Bankr. S.D. Fla 2021). This decision directly contradicts the decision made by the Second Circuit in In re Barnet, 737 F. 3d 238, 247 (2d Cir. 2013); the Barnet decision has been universally criticized. The future case law surrounding Chapter 15 may be uncertain, but its prominence in America and the global economy is unwavering.