

Collier Monograph: Ancillary and Other Cross-Border Insolvency Cases Under Chapter 15 of the Bankruptcy Code

The following material is excerpted from the Collier Monograph: Ancillary and Other Cross-Border Insolvency Cases Under Chapter 15 of the Bankruptcy Code, written by Hon. Leif M. Clark, United States Bankruptcy Judge for the Western District of Texas and edited by Daniel M. Glosband, Goodwin Procter LLP.

[6] Sections 1504 and 1515. Recognition as a Foreign Main or Foreign Nonmain Proceeding

Sections 1504 and 1515 work together to set the rules for how a foreign representative obtains recognition. However, a number of other provisions in chapter 15 play directly into the determination as well. Section 1517 actually sets the conditions for recognition, invoking the requirement that the court, in the course of recognition, determine whether the foreign proceeding is main or nonmain. That in turn requires consulting section 1502, which defines both of these terms, as well as the subsidiary concept of “establishment,” relevant to whether a proceeding qualifies at least as nonmain.

[a] Why It Matters

Recognition is the essential first step to the foreign representative’s obtaining access to U.S. courts for any purpose. Without recognition, a foreign representative may be affirmatively barred from obtaining comity or cooperation from “courts in the United States.”¹ In addition, without recognition, the foreign representative cannot initiate a full bankruptcy proceeding under U.S. law (voluntary or involuntary).² What is more, absent recognition, the foreign representative cannot participate as a party in interest in a bankruptcy case that is already pending in the U.S.³

By the same token, however, a foreign representative is not necessarily barred from *any* appearance at all. For example, a foreign representative might initiate state court litigation under state law, so long as the laws of that state would *independently* permit the representative to initiate and pursue such litigation.⁴ There are risks, of course. A foreign representative is unlikely to wish to be generally subject to the jurisdiction of U.S. courts for any purpose beyond the duties associated with being a foreign representative. If recognition is granted, the foreign representative is deemed under section 1510 not have generally subjected himself or herself to the jurisdiction of

¹ 11 U.S.C. § 1509(d). The use of the preposition “in” indicates that the order of prevention would apply to efforts to seek such relief not only in federal courts but also state courts. Were the statute intended for the prevention order to apply only to such relief sought in the federal courts, the statute would have used the preposition “of” instead. “Courts of the United States” is an accepted statutory phrase used to refer only to the federal court system.

² See 11 U.S.C. § 1511(a). There is an ostensible inconsistency between § 1511, which requires recognition for a foreign representative to file a petition under another chapter and § 303(b)(4), which appears to permit a foreign representative to file an involuntary petition without reference to recognition. See *In re Bear Stearns High Grade Structured Credit Strategies Master Fund, Ltd.*, 374 B.R. 122, 128 (Bankr. S.D.N.Y. 2007), *aff’d* 389 B.R. 325 (S.D.N.Y. 2008).

³ See 11 U.S.C. § 1512.

⁴ The foreign representative would need to consult the laws of the state where such litigation is proposed to be initiated. There are 50 states. Litigation sought to be commenced in the District of Columbia is by definition litigation in a federal court, and that court would likely insist that the foreign representative first obtain recognition, as federal courts are courts of limited jurisdiction, and standing to sue is deemed jurisdictional. See *United States v. J.A. Jones Construction Co.*, 333 B.R. 637, 639 (Bankr. E.D.N.Y. 2005) (absent recognition, federal district court ruled it had no authority to consider a request for stay).

courts in the United States.⁵ Without recognition, the foreign representative is not protected by this provision. A foreign representative also does not need formal recognition in order to perform tasks that do not require court assistance. Thus, for example, a foreign representative may be able to exercise the debtor's powers as a shareholder to replace board members of a corporation, or to vote the stock for one purpose or another. So long as the foreign representative is duly authorized to act for the debtor, in accordance with state law, the foreign representative may so act without first obtaining recognition under chapter 15.⁶ In most cases, however, prudence suggests that recognition be obtained to minimize questions regarding authority to act that might be raised later.

Of course, recognition especially matters when the foreign representative is in immediate need of relief. Facing imminent creditor collection action or imminent improper transfers of property of the debtor, the foreign representative will want the tools that chapter 15 has to offer. Immediately upon filing for recognition, the foreign representative can request interim relief, including injunctive relief, if it is urgently needed. That relief evaporates if the petition for recognition is later denied.⁷

[b] How Chapter 15 Eligibility Is Established

Chapter 15 follows the approach counseled by the Model Law. Recognition has been simplified and made more objective, compared to the imprecise comity standard used under former section 304. The process of recognition is also supposed to be relatively easy, consistent with the purpose of affording the foreign representative prompt relief to protect assets and preserve the interests of the creditor body. To that end, the statute employs a number of devices to expedite the recognition process. The documentation furnished to the court is relatively easy to obtain and does not require any sort of domestication of the foreign proceeding as a prerequisite. It is enough that the materials demonstrate that the requirements of section 1517 are met. And although section 1517 conditions the entry of an order of recognition on "notice and a hearing," that phrase itself invokes section 102(1) of the Code, which permits relief with minimal or no notice and no hearing if the exigencies so require.⁸ In addition, section 1517(c) specifically directs that the decision on recognition be made "at the earliest possible time."⁹

To make the recognition process even easier, section 1516(a) and (b) of the statute also provides that, if the materials referenced in section 1515(b), attached to the petition, say that the proceeding is a foreign proceeding and that the foreign representative is indeed the duly appointed and authorized foreign representative, then the court is "entitled to so presume." The court is further entitled to presume authenticity of the documents, regardless of whether they

⁵ See 11 U.S.C. § 1510.

⁶ See *In re Iida*, 377 B.R. 243, 256-57 (B.A.P. 9th Cir. 2007).

⁷ It also terminates if recognition is granted, but will be supplanted by the more permanent relief set out in sections 1520 and 1521 if the proceeding is a main proceeding. In addition, a court is permitted to extend the relief granted under section 1519 in a main proceeding. In the case of a nonmain proceeding, the statute itself is silent, though many bankruptcy courts in the U.S. would likely be persuaded in a given case that relief should be extended in that situation as well, through the court's exercise of its powers under section 105.

⁸ See 11 U.S.C. § 102(1); see, e.g., *Law Offices of David A. Boon v. Derham-Burk (In re Eliapo)*, 468 F.3d 592, 603 (9th Cir. 2006) (interpreting "hearing" flexibly so that an actual hearing may not be required so long as the applicant is given "a reasonable opportunity to present legal argument and/or evidence to clarify or supplement his Application.") (quoting *Nelson v. Mickelson (In re Pflighaar)*, 215 B.R. 394, 397 (B.A.P. 8th Cir. 1997)); see also *In re Busy Beaver Bldg. Ctrs., Inc.*, 19 F.3d 833, 845-46 (3d Cir. 1994).

⁹ 11 U.S.C. § 1517(c).

have been “legalized.”¹⁰ Finally, the court is entitled to presume that the country of the debtor’s registered office is also the center of main interest for the debtor.¹¹ The statute’s use of the term “presumption” has been interpreted as a reference to Federal Rule of Evidence 301.¹² Thus, the existence of the documents, and the recitations within the documents form the “base facts” that entitle the court to then presume, as set out in the statute. By the same token, the court is not *required* to make the presumption, but may instead insist on additional facts to support the contentions in the petition. Court decisions now generally confirm the proposition that the court has an independent duty to make the requisite determinations in advance of recognition, and that the court is not *bound* by the presumptions set out in section 1516.¹³

To obtain recognition, a foreign representative must establish the existence and legitimacy of the foreign proceeding in question. The foreign representative must also establish his or her right to act on behalf of the foreign proceeding. In addition, however, the foreign representative must also establish by competent evidence that the foreign proceeding is either a foreign main proceeding or a foreign nonmain proceeding. Moreover, the evidence must establish that the foreign proceeding is one or the other. If it is neither, then recognition will not be granted.¹⁴

10 This is the terminology used in the Model Law, designed to generically reference the various kinds of authentication requirements that might otherwise be required by a given jurisdiction to establish the genuineness of a document issued by a foreign court.

11 11 U.S.C. § 1516(c). The presumption mirrors a similar provision in the EC Regulation. *See* EC Regulation, *reprinted in* Collier International Business Insolvency Guide, App. B (Matthew Bender).

12 *See In re Basis Yield Alpha Fund (Master)*, 381 B.R. 37, 53 (Bankr. S.D.N.Y. 2008) (citing Fed. R. Evid. 301); *see also In re Tri-Continental Exchange Ltd.*, 349 B.R. 627, 635 (Bankr. E.D. Cal. 2006) (“Congress chose to substitute “evidence” for “proof” and otherwise to adopt the Model Law provision word-for-word. The explanation was that the substitution conformed to United States terminology and made clear that the burden of proof of ‘center of main interests’ is on the foreign representative who is applying for recognition of a foreign proceeding as a main proceeding. (footnote omitted) This comports with the concept of a rebuttable presumption for purposes of Federal Rule of Evidence 301.”).

13 *See In re Bear Stearns High Grade Structured Credit Strategies Master Fund, Ltd.*, 389 B.R. 325, 331 (Bankr. S.D.N.Y. 2008).

14 Initially, there was some debate on this point. It was thought by some that a foreign proceeding must be one or the other—main or nonmain. *See, e.g., In re SPhinX, Ltd.*, 351 B.R. 103, 122 (Bankr. S.D.N.Y. 2006) (recognizing the foreign proceeding as a nonmain proceeding because “nothing in chapter 15 provides that there cannot be a ‘nonmain’ proceeding unless there is a ‘main’ proceeding” and because “it would run contrary to logic as well as the statute’s plain language and purpose to force the court to recognize a foreign proceeding as a ‘main’ proceeding simply because it was the only proceeding currently pending”), *aff’d In re SPhinX, Ltd.*, 371 B.R. 10 (S.D.N.Y. 2007). On that theory, recognition itself would require only a showing that the foreign proceeding qualified as such under chapter 15 and the foreign representative was authorized to act on behalf of that proceeding. *See In re SPhinX, Ltd.*, 351 B.R. at 122. The foreign representative would, under that theory, only need to establish that the foreign proceeding was a main proceeding, and if he or she wanted or needed that finding and the special relief that comes with it. *See* discussion *infra*. Otherwise, the “default” finding for an otherwise qualified foreign proceeding would be “nonmain.”

This approach was rejected by the bankruptcy and district courts in *Bear Stearns*. The correct approach, according to Judge Lifland, is that a proceeding must be proven to be either a main or a nonmain proceeding as a prerequisite to recognition. If the proceeding does not qualify as either kind of proceeding, as defined in chapter 15, then recognition should be denied. *See generally In re Bear Stearns High Grade Structured Credit Strategies Master Fund, Ltd.*, 374 B.R. 122, 126-32 (Bankr. S.D.N.Y. 2007), *aff’d* 389 B.R. 325 (S.D.N.Y. 2008). While the circuit courts have not yet spoken on the matter, it seems likely this view will prevail, as the same court to affirm the SPhinX decision more recently affirmed the seemingly-contradictory Bear Stearns decision as well. *See In re Bear Stearns High Grade Structured Credit Strategies Master Fund, Ltd.*, 389 B.R. 325 (Bankr. S.D.N.Y. 2008) (Sweet, J.). This approach also has the advantage of being consistent with the UNCITRAL Legislative Guide to Enactment as well as the legislative history to chapter 15.

While the presumptions are not determinative, they are helpful and will, in most cases, obviate the need for an evidentiary hearing to obtain recognition. However, the foreign representative must always be cognizant that, regardless of the presumption, the ultimate burden of proof is on the foreign representative.¹⁵

With regard to the first requirement for recognition, the petition must demonstrate that the proceeding in question is a “foreign proceeding” within the meaning of section 101 of the Bankruptcy Code.¹⁶ That section tracks the Model Law’s definition. While it is intentionally broad, it is also designed to exclude proceedings that are more in the nature of corporate or partnership dissolutions—though some such proceedings do qualify under this definition.¹⁷ The certified copy of the documentation establishing that such a proceeding has commenced on at least an interim basis will usually be sufficient to satisfy the court that the proceeding in question qualifies under this definition. In addition, including an affidavit describing the essential nature of the proceeding can be helpful, as the order opening the proceeding will itself not address this issue. Such an affidavit can usually be executed by the foreign representative, who is presumably familiar with the legal regime under which he or she was appointed.

Section 1501(c) further provides that, with one exception, an entity that would not qualify as a debtor to file a voluntary petition under the U.S. Bankruptcy Code is also not qualified as a foreign proceeding under chapter 15.¹⁸ Thus, a railroad or a U.S.-regulated bank with a proceeding pending in another country (main or nonmain), is not eligible for relief under chapter 15.¹⁹ The exception to these exclusions is a foreign insurance company. Although such a company cannot be a debtor in a domestic bankruptcy case in the U.S., it is not disabled from seeking relief under chapter 15.²⁰ In addition, stockbrokers, commodity brokers and entities subject to a proceeding under the Securities Investor Protection Act of 1970 are also disqualified from seeking relief under chapter 15.²¹

The second requirement, that the foreign representative is authorized to act on behalf of the proceeding, is also easily satisfied in most situations. The order or other provision appointing the representative and authorizing him or her to act is usually sufficient. If the order is unclear, it may be supplemented with an affidavit from the foreign representative that sets out the role and

15 See *In re Tri-Continental Exchange, Ltd.*, 349 B.R. 627, 635 (Bankr. E.D. Cal. 2006) (substitution of term “evidence” for term “proof” as used in Model Law designed, *inter alia*, to emphasize placement of burden of proof on the foreign representative); see also *Lavie v. Ran*, 384 B.R. 469, 471 (Bankr. S.D. Tex. 2008) (court presented with evidence could not simply rely on presumption to determine whether burden had been sustained).

16 The definition reads as follows: “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).

17 See, e.g., *In re SPhinX, Ltd.*, 351 B.R. 103, 122 (Bankr. S.D.N.Y. 2006) (discussing Cayman proceedings); *Bank of New York v. Treco (In re Treco)*, 240 F.3d 148, 158-59 (2d Cir. 2001) (discussing Bahamian proceedings); see also *Matter of Culmer*, 25 B.R. 621 (Bankr. S.D.N.Y. 1982).

18 11 U.S.C. § 1501(c)(1); see also 11 U.S.C. § 109(b).

19 See 11 U.S.C. § 109(b). Section 109 defines who is eligible to be a debtor in a U.S. proceeding. To mirror the prohibition in section 1502(c), foreign banks are also not eligible to be a debtor in a U.S. proceeding—even though they might have assets or creditors or significant operations in the U.S. 11 U.S.C. § 109(b)(3)(b).

20 See 11 U.S.C. §§ 109(b)(3)(A), 1501(c)(1).

21 11 U.S.C. § 1501(c)(3). There is one other exclusion, unique to U.S. practice. An individual who would otherwise be eligible for relief under chapter 13 of the U.S. Code and who is either a U.S. citizen or resident alien may not obtain relief under chapter 15. Such a person should simply file a chapter 13 petition in the U.S.

duties of the foreign representative under the law under which he or she was appointed. The definition of who is a foreign representative is found in section 101(24).²²

The third requirement²³ is that the foreign representative prove that the proceeding qualifies as either a main or a nonmain proceeding. Another way to state the issue is that a foreign proceeding must at least qualify as a foreign nonmain proceeding, as defined in section 1502, in order to qualify for recognition. Of course, the foreign representative has incentives to qualify as a foreign main proceeding, including most significantly the immediate imposition of a stay on all collection action and litigation, upon recognition.²⁴ In that event, the petition should demonstrate that the proceeding qualifies as a foreign main proceeding. The petition should thus have attached to it an affidavit that with specificity demonstrates subsidiary facts that establish that the proceeding is main or nonmain. If it is a main proceeding, then the affidavit should contain subsidiary facts that show that the locus of the proceeding is the debtor's center of main interests.²⁵ In all events, the affidavit should at least set out facts demonstrating that the locus of the proceeding is at least one in which the debtor has an establishment.²⁶ The case law is still developing regarding the subsidiary facts for each of these options.²⁷ The statute itself does not define the concept "center of main interests," the essential issue for determining whether a proceeding is "main." The statute does define "establishment," but with language that itself begs for judicial construction.²⁸

If the proceeding is pending in a country that is the center of the debtor's main interests, then it is a "main proceeding." There have been only a few court decisions that have discussed the concept of center of main interests, but already there is beginning to develop a consensus on the kinds of factors that might make the case.²⁹

22 The definition reads as follows: "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).

23 There is the possibility that a circuit court might disagree with the district court decision in *Bear Stearns*, reinstating the rule set out in the bankruptcy decision in *SPhinX*. As of this writing, there has been no such decision, and the better analysis supports the rule that proving a foreign proceeding is at least a nonmain proceeding is a prerequisite to recognition.

24 See 11 U.S.C. § 1521.

25 See 11 U.S.C. § 1502(4).

26 See 11 U.S.C. § 1502(5).

27 See *Lavie v. Ran*, 384 B.R. 469, 471 (Bankr. S.D. Tex. 2008). The district court remanded the case to the bankruptcy court, with instructions that it "determine what factors are appropriate when considering the COMI of an individual debtor, and make findings of fact in accord with the aforementioned factors." *Id.* at 472. The bankruptcy court had denied recognition to the foreign representative of an Israeli insolvency proceeding, on grounds that, *inter alia*, Israel could not be the debtor's COMI because the debtor's habitual residence was in Houston, Texas. The district court ruled that the bankruptcy court was obligated to review evidence that might rebut the presumption that the debtor's residence was in fact the debtor's COMI. The court adverted to other cases that have tried to lay out factors. See *In re SPhinX, Ltd.*, 351 B.R. 103 (Bankr. S.D.N.Y. 2006), *aff'd* 371 B.R. 10 (S.D.N.Y. 2007); *In re Loy*, 380 B.R. 154 (Bankr. E.D. Va. 2007); see also *In re Basis Yield Alpha Fund (Master)*, 381 B.R. 37, 47 (Bankr. S.D.N.Y. 2008); *In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd.*, 374 B.R. 122, 128 (Bankr. S.D.N.Y. 2007), *aff'd* 398 B.R. 325 (S.D.N.Y. 2008).

28 See 11 U.S.C. § 1502(2). The statute defines "establishment" as "any place where the debtor carries out a non-transitory economic activity."

29 See *In re SPhinX, Ltd.*, 351 B.R. 103 (Bankr. S.D.N.Y. 2006), *aff'd* 371 B.R. 10 (S.D.N.Y. 2007); *In re Loy*, 380 B.R. 154 (Bankr. E.D. Va. 2007); see also *In re Basis Yield Alpha Fund (Master)*, 381 B.R. 37, 47 (Bankr. S.D.N.Y. 2008); *In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd.*, 374 B.R. 122, 128 (Bankr. S.D.N.Y. 2007), *aff'd* 389 B.R. 325 (S.D.N.Y. 2008).

To start, in the unremarkable case, the presumption in section 1516 will be sufficient to satisfy the showing. However, the decisions in *Bear Stearns* and in *Basis Alpha* demonstrate that taking shelter in the presumption is not a safe course of action.³⁰ The foreign representative thus has a strategic issue to consider at the outset. The representative could present an affidavit disclosing only the country of the debtor's registration, relying solely on the presumption to prove that the country is the center of main interests for the debtor. The court might then require a hearing simply because it is uncomfortable with accepting the presumption at face value. Alternatively, the representative could submit a more complete affidavit, detailing facts that show center of main interests, but again risk the possibility of a hearing to test those facts. The court could even conceivably find that the country where the proceeding is pending is not the center of main interests of the debtor, based solely on the facts set out in the affidavit. Given the tenor of decisions that have been rendered on this issue to date, the wiser course appears to be the latter, unless the facts on the ground are unlikely to support a finding of center of main interest.

If the presumption is insufficient to make the case, then the court will examine the factors surrounding the debtor's operations in the country where the proceeding is pending. In general, courts in the U.S. are likely to interpret the center of main interest concept as similar to the notion of "principal place of business."³¹ Examples of factors that have been found persuasive include the location of the debtor's headquarters operations, the location of books and records, the locus of business accounts and the location of employees.³² An additional factor, whether creditors have come to rely on the location by the way the debtor has operated, is likely to be persuasive. The U.S. courts that have ruled on the question have also noted to the decision of the European Court of Justice in *Eurofoods*, which also dealt with the a center of main interest question.³³

The legislative history to section 1517, as well as the UNCITRAL Legislative Guide, both note a reluctance to spell out any one set of factors making up the COMI concept. The concept is in a clear state of flux as well, as UNCITRAL Working Group V struggles with the problem of corporate groups. Identifying the center of main interest for a corporate group is especially

30 See *Bear Stearns*, 374 B.R., at 130.

31 Here is a listing furnished in a recent case, including a number unpublished decisions: See *In re Daewoo Corp.*, 06-12242(REG) (Korean insolvency proceeding for the flagship company of the Daewoo Group, one of the largest industrial conglomerates in Korea, recognized as foreign main proceeding); *In re AXA Insurance UK PLC*, 07-07-12110(REG); *In re Ecclesiastical Insurance Office PLC*, 07-12111(REG); *In re Global General and Reinsurance Co. Ltd.*, 07-12112(REG); *In re MMA IARDD Assurance Mutuelles*, 07-12113(REG) (in jointly administered case, English insolvency proceeding for three UK companies and one non-UK company, all writing reinsurance business in the London market, recognized as main proceeding for the UK companies, and nonmain proceeding for the non-UK company, where alleged, with respect to the UK companies, that "their principal place of business is the UK," and alleged, for the nonmain proceeding recognition for the non-UK company, that it transacted insurance business in England and maintained an establishment there); *In re Europäische Rückversicherungs-Gesellschaft in Zurich* (European Reinsurance Co. of Zurich), 06-13061(REG) (English insolvency proceeding for Swiss reinsurance company doing business in the London market recognized as nonmain proceeding)." *In re Basis Yield Alpha Fund (Master)*, 381 BR. 37, 54 n. 67 (Bankr. S.D.N.Y. 2008).

32 See *In re Bear Stearns High Grade Structured Credit Strategies Master Fund, Ltd.*, 374 B.R. 122, 128 (Bankr. S.D.N.Y. 2007), aff'd 389 B.R. 325 (S.D.N.Y. 2008) (factors include the location of the debtor's headquarters, location of those who actually manage debtor, the location of the debtor's primary assets, the location of the majority of the debtor's creditors, or of the majority of creditors who would be affected by case, and the jurisdiction whose law would apply to most disputes); *In re Basis Yield Alpha Fund*, 381 B.R. 37 (Bankr. S.D.N.Y. 2008) (same); see also *Petition of Ernst & Young, Inc., as Receiver of Klytie's Developments, Inc.*, 383 B.R. 773 (Bankr. D. Colo. 2008) (debtor entities used to defraud investors were placed into a receivership in Canada; Canadian court then authorized the receiver to seek aid and recognition in the U.S.; court granted recognition as a foreign main proceeding, after examining the factors set out in *Bear Stearns*).

33 See *Bondi v. Bank of America, N.A. (In re Eurofood IFSC Ltd.)*, Case 341/04 (para 33), 2006 ECR I-3813 (construing the term as used in the EC Insolvency Regulation).

troublesome.³⁴ One court ruled that the fact that a parent company had its center of main interest in the country of the foreign proceeding did not necessarily establish that the country was the COMI for the filing subsidiary.³⁵ Another concluded that Canada was the COMI for a U.S. and a Canadian debtor that were both subject to a Canadian receivership.³⁶ As currently drafted, chapter 15 operates on the assumption that each proceeding stands on its own.³⁷ The clear danger is the possibility of multiple proceedings in more than one country involving multiple but related companies, with more than one of such proceedings qualifying as pending in the COMI of each of two or more related companies. In that event, chapter 15 offers the possibility of coordination among the proceedings, utilizing the principles of cooperation and coordination set out in sections 1525 through 1527.³⁸

In the event that COMI cannot be proven, then the foreign representative must be able to prove that the proceeding is pending in a country in which the debtor has an establishment. The statute defines establishment as a place where the debtor “carries out a non-transitory economic activity.” There is no presumption to aid the determination of establishment, as there is for COMI. The case law is only just now developing with regard to this concept, so clear guidance is not yet possible. Early cases have concluded that merely maintaining an office, maintaining a bank account or being registered is insufficient to prove a non-transitory economic activity. Two recent cases, both discussing Cayman Islands proceedings, are worthy of note. In *Bear Stearns*, the court concluded that the foreign representative had failed to sustain its burden of proof on the presence of an establishment. The evidence showed only “[a]uditing activities and preparation of incorporation papers performed by a third party,” and that, said the court, did not fall within the ordinary meaning of “operations” or “economic activity.”³⁹ In addition, there were no assets of the debtor entity in the Caymans as of the filing date.

The court added that it would not permit the representatives to supplement the record on appeal, declining to craft a special rule for appellate review of these kinds of decisions.⁴⁰ In the other notable case, the *Basis Yield Alpha Fund* court declined to use a section 1516 presumption

34 See generally Aaron M. Kaufman, Comment, *The European Union Goes COMI-tose: Hazards of Harmonizing Corporate Insolvency Laws in the Global Economy*, 29 Houst. J. Int'l L. 625 (2007) (discussing the tendencies of some insolvency courts to favor their own home countries as the debtor's COMI); Ralph R. Mabey & Susan Power Johnson, “Coordination Among Insolvency Courts in the Rescue of Multi-National Enterprises,” 34th Lawrence P. King & Charles Seligson Workshop on Bankruptcy and Business Reorganization, New York University School of Law (September 2008).

35 See *In re Aerovias Nacionales de Colombia S.A. Avianca*, 303 B.R. 1, 17-18 (Bankr. S.D.N.Y. 2003) (declining to dismiss or abstain from exercising jurisdiction over a U.S. subsidiary's chapter 11 case where the parent had filed its own case in its home country of Colombia; “although courts will generally defer to the ‘center of gravity’ of multiple proceedings if one can be ascertained, a court may also choose to proceed jointly with a foreign court or to ‘exercise its power to the full extent of its jurisdiction in an appropriate case.’”) (citing *Hong Kong and Shanghai Banking Corp. v. Simon (In re Simon)*, 153 F.3d 991, 999 (9th Cir. 1998)).

36 *Petition of Ernst & Young, Inc., Receiver for Klyties Development, Inc.*, 383 B.R. 773 (Bankr. D. Colo. 2008). The court walked through the factors laid out by Judge Lifland in the *Bear Stearns* decision. See *In re Bear Stearns High Grade Structured Credit Strategies Master Fund, Ltd.*, 374 B.R. 122, 128 (Bankr. S.D.N.Y. 2007), *aff'd* 389 B.R. 325 (S.D.N.Y. 2008). It found that both debtors' managers ran the enterprises from Canada at the time of the conduct that eventually led to the receivership. It noted that there was no real business anywhere, given that the entities were created as part of a fraudulent scheme. The principal assets of the debtors consisted of the funds tendered by investors, and those funds were property of the Canadian company, KDI. The court found applicable law and jurisdictional issues not to be relevant.

37 This concept is consistent with the principle that corporate governance rules should be honored.

38 See 11 U.S.C. § 1529; see Section 12[2][a] *infra*.

39 See *id.* *Bear Stearns High Grade Structured Credit Strategies Master Fund, Ltd.*, 389 B.R. 325 (Bankr. S.D.N.Y. 2008).

40 See *id.* at 331.

as a substitute for the foreign representative's need to submit actual evidence of the debtor's COMI or establishment.⁴¹

[c] Neither Main Nor Nonmain

As noted, the case law so far requires that a foreign proceeding qualify as either main or nonmain as a condition to recognition. If the proceeding does not qualify as either, such that recognition is no longer an option, the remaining options are limited. For example, the foreign representative who fails to obtain recognition also loses the ability to initiate a full bankruptcy proceeding under U.S. law. Section 1511 states that the foreign representative can initiate either an involuntary bankruptcy proceeding under section 303 or a voluntary proceeding under section 301—but only upon recognition. Section 1511(b) explicitly states that, to file such a petition, the representative must attach a certified copy of the recognition order. The argument has been made by one court that in fact a foreign representative *could* initiate a full bankruptcy case even absent recognition, notwithstanding section 1511. In *Bear Stearns*, Bankruptcy Judge Lifland opined that the foreign representatives there, to whom he had just denied recognition, could still initiate at least an involuntary case under U.S. law because section 303(b)(4), unlike section 1511, does *not* make recognition a precondition to initiating an involuntary bankruptcy case. In this regard, Judge Lifland could have adverted as well to the UNCITRAL Legislative Guide, which suggests this very option in its discussion of article 11 of the Model Law.⁴² However, chapter 15 altered the text of article 11 substantially, expressly adding the qualifying phrase “upon recognition.” Section 1511 also added a subsection expressly directing that a certified copy of the order of recognition be attached to any petition filed by a foreign representative under either section 301 or 303. As Judge Lifland candidly acknowledged in *Bear Stearns*, the lack of a specific reference in section 303(b)(4) either to recognition in particular or to chapter 15 generally is more likely an oversight on the part of Congress than a statement of legislative intent.⁴³

The consequences of non-recognition under chapter 15 for a foreign representative are thus quite severe. The foreign representative for the most part will be barred from appearing in state or federal court as a party litigant.⁴⁴ There is a limited exception to this general bar in section 1509(f) that permits a foreign representative to initiate lawsuits in state or federal court for the limited purpose of collecting or recovering on a claim which is property of the debtor.⁴⁵ In addition, there are

41 See *In re Basis Yield*, 381 B.R. 37, 48 (Bankr. S.D.N.Y. 2008) (“But the Court cannot endorse that approach [of using section 1516(c) as a proxy for submission of evidence], and find that there is a section 1517 qualification as a matter of law, for two separate reasons. Here there is evidence to the contrary. And the Court’s power to examine the facts underlying a request for recognition under section 1517, and to inquire under Fed. R. Evid. 614, cannot be sidestepped or eliminated by elections to not plead or introduce the relevant facts.”).

42 See Legislative Guide, ¶¶ 98-99. The Guide explains that Article 11 gives the foreign representative standing to initiate a chapter 7 or chapter 11 case in the Enacting State (i.e., the country that enacted the Model Law), and that the representative need not have obtained recognition in order to initiate such a proceeding.

43 See also *United States v. J.A. Jones Construction Co.*, 333 B.R. 637, 639 (Bankr. E.D.N.Y. 2005) (“In the absence of recognition under chapter 15, this Court has no authority to consider [the movant’s] request for a stay. Such a request may not be necessary should a bankruptcy court grant a petition for recognition. In most cases, commencement of an ancillary proceeding before a bankruptcy court may be unnecessary, since, as a practical matter, a plaintiff or other creditor with little prospect of recovery has little incentive to pursue a defunct defendant foreign corporation.”).

44 See 11 U.S.C. § 1509(d). The statute implies this conclusion by negative inference because the access described in section 1509(b) is conditioned on granting recognition. However, subsection (d) specifically empowers the bankruptcy court to issue “any order necessary to prevent the foreign representative from obtaining comity or cooperation” in the event recognition has been denied, expressly granting to the court the power to prevent abuse.

45 See 11 U.S.C. § 1509(f).

numerous actions that do not require resort to courts, for which recognition is not therefore a prerequisite. For example, a foreign representative was held justified in having exercised voting rights to appoint a new officer and new directors to a non-debtor corporation owned by the debtor, there being no prohibition on a duly appointed foreign representative to take such action under the law of the state in question.⁴⁶

⁴⁶ See *Iida v. Kitahara (In re Iida)*, 377 B.R. 243, 258 (B.A.P. 9th Cir. 2007) (“In this instance, the Foreign Representative’s actions in exercising shareholder rights to change the directors and officers of the Hawaii Corporations, in circumstances in which the corporations and the Iidas acquiesced without questioning the Foreign Representative’s authority, did not impel a need for judicial assistance. Thus, even if chapter 15 had been in effect when the Foreign Representative removed and replaced the officers and directors of the Hawaii Corporations, there would have been no impediment imposed by chapter 15.”)

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JUDGE LEIF M. CLARK has served as a bankruptcy judge for the Western District of Texas since 1987. Prior to his appointment, he was a partner with the firm of Cox & Smith, in San Antonio, Texas. He is the author of well over 200 opinions, many of them seminal decisions on emerging issues in consumer and business bankruptcy. In addition, he has published scholarly articles in law reviews and treatises, including a series of articles on the Fifth Circuit's bankruptcy jurisprudence from 1995 through 2002 in the Texas Tech University Law Review. For many years, Judge Clark authored the monthly column *Dicta* in the *ABI Journal*. He was invited to testify before the National Bankruptcy Review Commission regarding Article III issues. He is a frequent lecturer on bankruptcy issues at seminars nationwide. He served as an officer and director of the American Bankruptcy Institute for many years and participated in the formation of that organization's Endowment Committee to fund bankruptcy research. He currently serves as a member of the Endowment Board for the National Conference of Bankruptcy Judges. He was inducted as a Fellow of the American College of Bankruptcy in 1994, and is a conferee in the National Bankruptcy Conference, serving on its International Committee. He is also an active member of the International Insolvency Institute.

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