The Workings of and Current Trends in Chapter 15

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The ushering in of Chapter 15 by the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA") on October 17, 2005 could not have been more timely. Little did the enactors of BAPCPA know that a financial typhoon was already brewing that would envelop the world economy and immediately start putting Chapter 15 to the test. This article briefly reviews the landscape of cross-border cases prior to Chapter 15, the foundations of Chapter 15, the basic purpose, scope and application of Chapter 15, a review of the recent 15 hedge fund line of cases, an analysis of the surprisingly limited use of Chapter 15, and finally a brief review of recent cases under Chapter 15.

I. Before Chapter 15

Prior to BAPCPA's implementation of Chapter 15, cross-border insolvencies had been governed by § 304 of the Bankruptcy Code. In summary, § 304 provided recognition of some foreign proceedings by U.S. courts and generally set forth certain principles to guide those courts in administration of such proceedings.[1] Unfortunately, § 304 contained several significant limitations necessary to create a comprehensive statutory framework when dealing with recognition of foreign proceedings.[2]

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[1] *See* Aaron L. Hammer & Matthew E. McClintock, "*Understanding Chapter 15 of the United States Bankruptcy Code: Everything You Need to Know About Cross-Border Insolvency Legislation in the United States*," 14-SPG L. & Bus. Rev. Am. 257, 262 (Spring 2008) (hereinafter "Hammer & McClintock").

[2] *See id.,* n.16 (noting that under § 304 foreign representatives were only able to commence limited purpose bankruptcy cases and they were not authorized to operate a debtor's business or sell its assets); *see also*

The underlying bases for what would become Chapter 15 were borne not out of the current set of worldwide financial calamities, but rather the dramatic rise in cross-border insolvencies since the early 1990s. Efforts to deal with and intelligently manage cross-border insolvencies compelled multiple efforts by "insolvency organizations and the international community to devise better legal frameworks" for effectively handling this new set of bankruptcy and restructuring challenges.[3] Efforts by the international insolvency community, particularly in Europe, led to the first steps of a comprehensive international insolvency structure upon which Chapter 15 would be based.

II. A Brief Look at the Foundations and Formation of Chapter 15

The structure of Chapter 15 is modeled on the UNCITRAL Model Law (the "Model Law") from 1997 and the European Union Regulation on Insolvency Proceedings from 2000 (the "EU Regulation"). While this article does not attempt to review any substantial historical underpinnings of Chapter 15, it is important to recognize that the intended purpose of the Model Law was to "harmonize existing cross-border insolvency regimes (which was to presumably result in increased legal certainty for trade and investment, an express objective of the Model Law) and designed to enhance international cooperation and efficiency with respect to the administration of cross-border insolvencies."[4]

The Model Law was drafted in such a way as to make it easier for individual countries to both adopt the Model Law and at the same time not require substantial

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Griffiths & Smith, *Transatlantic Insolvency Jurisdiction – The Interplay Between Chapter 15 of U.S. Bankruptcy Code and the EU Insolvency Regulation*, 21(8) J. Int'l Banking L. & Reg. 435, 435-36 (2006).

[3] Hammer & McClintock at 259.

[4] *Id.* at 260.

changes to their existing domestic insolvency laws.[5] This flexible drafting led to the widespread acceptance and adoption of the Model Law by many countries, including the United States.[6]

"Although the Model Law came into force prior to the EU Regulation (in 1997 as opposed to 2000), the EU Regulation was drafted first, and the Model Law copied many of the EU Regulation's most important concepts."[7] Among these is the mandate, now captured in Chapter 15 in § 1508, that "U.S. courts look to case law interpreting identical provisions under both the Model Law and EU Regulation."[8] As a result of this provision, bankruptcy courts may now consider foreign case law in the context of Chapter 15 decision-making.

III. The Purpose, Scope and Application of Chapter 15

The general and overriding purpose of Chapter 15 is to create an efficient and effective means to administer cross-border insolvencies.[9] Section 1501(a) codifies this objective.[10] Likewise, § 1501(b) clearly lays out the scope of Chapter 15.[11] Section 1501(c) further lists when Chapter 15 will not apply.[12]

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[5] *Id.*

[6] *Id.*

[7] *Id.* at 262.

[8] *Id.*

[9] *Id.* 263.

[10] Section 1501(a) states,

> **(a)** The purpose of this chapter is to incorporate the Model Law on Cross-Border Insolvency so as to provide effective mechanisms for dealing with cases of cross-border insolvency with the objectives of--
> **(1)** cooperation between--
> **(A)** courts of the United States, United States trustees, trustees, examiners, debtors, and debtors in possession; and

Despite these clearly laid out purposes and applications, to understand Chapter 15 with any clarity, an understanding of certain terms peculiar to Chapter 15 must first be undertaken. Among these are "foreign proceeding" and "foreign representative." These terms are specifically defined in § 101.

> **(B)** the courts and other competent authorities of foreign countries involved in cross-border insolvency cases;
> **(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 interested entities, including the debtor;
> **(4)** protection and maximization of the value of the debtor's assets; and
> **(5)** facilitation of the rescue of financially troubled businesses, thereby protecting investment and preserving employment.

11 U.S.C. § 1501(a).

[11] Section 1501(b) states,

> **(b)** This chapter applies where--
> **(1)** assistance is sought in the United States by a foreign court or a foreign representative in connection with a foreign proceeding;
> **(2)** assistance is sought in a foreign country in connection with a case under this title;
> **(3)** a foreign proceeding and a case under this title with respect to the same debtor are pending concurrently; or
> **(4)** creditors or other interested persons in a foreign country have an interest in requesting the commencement of, or participating in, a case or proceeding under this title.

11 U.S.C. § 1501(b).

[12] Section 1501(c) states,

> **(c)** This chapter does not apply to--
> **(1)** a proceeding concerning an entity, other than a foreign insurance company, identified by exclusion in section 109(b);
> **(2)** an individual, or to an individual and such individual's spouse, who have debts within the limits specified in section 109(e) and who are citizens of the United States or aliens lawfully admitted for permanent residence in the United States; or
> **(3)** an entity subject to a proceeding under the Securities Investor Protection Act of 1970, a stockbroker subject to subchapter III of chapter 7 of this title, or a commodity broker subject to subchapter IV of chapter 7 of this title.

11 U.S.C. § 1501(c).

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."[13] A "foreign representative means 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."[14]

IV. Recognition and Implications Thereof

For the insolvent entity seeking relief in the U.S., the most important consideration is whether or not the bankruptcy court will recognize its foreign proceeding.[15] This is a vital step because without recognition the debtor is excluded from Chapter 15. Leaving aside for this article the procedural steps and required pleadings to gain this recognition, it is sufficient to note that the recognition process itself is made significantly easier by § 1516(b) which grants a presumption that all documentation submitted in connection with the Chapter 15 petition is deemed authentic, in the absence of evidence to the contrary.[16] If the Chapter 15 petition is granted then the proceeding

[13] 11 U.S.C. § 101(a)(23).

[14] 11 U.S.C. § 101(a)(24).

[15] This article does not attempt to provide guidance on the procedural hurdles and requirements for obtaining this recognition; however, Hammer and McClintock provides valuable guidance on this topic.

[16] Section 1516(b) states, "The court is entitled to presume that documents submitted in support of the petition for recognition are authentic, whether or not they have been legalized." Additionally, § 1517 provides that a hearing on the petition should be held quickly. While this presumption seems straight forward, many courts have rejected it as was the case in the *Bear Sterns* decision discussed *infra*.

will either be recognized as a "foreign main proceeding"[17] or a "foreign nonmain proceeding,"[18] the differences and consequences of which can be extremely important to the debtor.[19]

Upon recognition, the foreign representative of the debtor becomes eligible to "(i) sue and be sued in the United States; (ii) to apply directly to a court in the United States for relief from that court and (iii) can seek comity or cooperation from the United States court."[20] While recognition provides the above rights, the distinction between the court

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[17] *See* 11 U.S.C. § 1502(4) (defining "foreign main proceedings" as a "foreign proceeding pending in the country where the debtor has the center of its main interests").

[18] *See* 11 U.S.C. § 1502(5) (defining "foreign nonmain proceeding" as "other than a foreign main proceeding, pending in a country where the debtor has an establishment").

[19] In the interim period from the filing of the petition and corresponding supporting documents and pleadings and the decision on recognition 11 U.S.C. § 1519 grants the court discretion of whether to grant interim relief. This can be especially important to "protect the assets of the debtor or the interests of the creditors." *See also* Hammer & McClintock at 268. However, note that certain limits on the scope of protections that the court can offer are contained in § 1519(c) and (d).

[20] *See* section 1521(stating the relief that may be granted upon recognition):

> **(a)** Upon 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 the creditors, the court may, at the request of the foreign representative, grant any appropriate relief, including--
> **(1)** staying the commencement or continuation of an individual action or proceeding concerning the debtor's assets, rights, obligations or liabilities to the extent they have not been stayed under section 1520(a);
> **(2)** staying execution against the debtor's assets to the extent it has not been stayed under section 1520(a);
> **(3)** suspending the right to transfer, encumber or otherwise dispose of any assets of the debtor to the extent this right has not been suspended under section 1520(a);
> **(4)** providing for the examination of witnesses, the taking of evidence or the delivery of information concerning the debtor's assets, affairs, rights, obligations or liabilities;
> **(5)** entrusting the administration or realization of all or part of the debtor's assets within the territorial jurisdiction of the United States to the foreign representative or another person, including an examiner, authorized by the court;
> **(6)** extending relief granted under section 1519(a); and
> **(7)** granting any additional relief that may be available to a trustee, except for relief available under sections 522, 544, 545, 547, 548, 550, and 724(a).

recognizing the debtor as a foreign main proceeding or foreign nonmain proceeding is especially important.

If recognized as a foreign main proceeding, the debtor is given a series of delineated statutory rights under § 1520.[21] Most importantly among these is the use of

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> **(b)** Upon recognition of a foreign proceeding, whether main or nonmain, the court may, at the request of the foreign representative, entrust the distribution of all or part of the debtor's assets located in the United States to the foreign representative or another person, including an examiner, authorized by the court, provided that the court is satisfied that the interests of creditors in the United States are sufficiently protected.
> **(c)** In granting relief under this section to a representative of a foreign nonmain proceeding, the court must be satisfied that the relief relates to assets that, under the law of the United States, should be administered in the foreign nonmain proceeding or concerns information required in that proceeding.
> **(d)** The court may not enjoin a police or regulatory act of a governmental unit, including a criminal action or proceeding, under this section.
> **(e)** The standards, procedures, and limitations applicable to an injunction shall apply to relief under paragraphs (1), (2), (3), and (6) of subsection (a).
> **(f)** The exercise of rights not subject to the stay arising under section 362(a) pursuant to paragraph (6), (7), (17), or (27) of section 362(b) or pursuant to section 362(n) shall not be stayed by any order of a court or administrative agency in any proceeding under this chapter.

11 U.S.C. § 1521; *see also* Hammer & McClintock at 268.

[21] Section 1520 provides,

> **(a)** Upon recognition of a foreign proceeding that is a foreign main proceeding--
> **(1)** sections 361 and 362 apply with respect to the debtor and the property of the debtor that is within the territorial jurisdiction of the United States;
> **(2)** sections 363, 549, and 552 apply to a transfer of an interest of the debtor in property that is within the territorial jurisdiction of the United States to the same extent that the sections would apply to property of an estate;
> **(3)** unless the court orders otherwise, the foreign representative may operate the debtor's business and may exercise the rights and powers of a trustee under and to the extent provided by sections 363 and 552; and
> **(4)** section 552 applies to property of the debtor that is within the territorial jurisdiction of the United States.
> **(b)** Subsection (a) does not affect the right to commence an individual action or proceeding in a foreign country to the extent necessary to preserve a claim against the debtor.
> **(c)** Subsection (a) does not affect the right of a foreign representative or

the automatic stay provisions under § 362 and the automatic application of the other statutory rights under § 1520 without need to obtain further court order granting those rights. Additionally, "if a foreign proceeding is recognized as a foreign main proceeding the foreign representative is authorized to commence a voluntary bankruptcy case for the debtor under another chapter of the Bankruptcy Code."[22]

If the proceeding is instead recognized as a foreign nonmain proceeding then relief is not automatic and instead is wholly discretionary with the court. Additionally, the foreign representative in the nonmain proceeding is not allowed to file a bankruptcy case under another title. While the granting of relief is discretionary, those discretionary powers are extremely broad, with the Bankruptcy Code authorizing the court in a nonmain proceeding to grant any necessary or appropriate relief.[23]

With all that is at stake in obtaining recognition as a main proceeding and with all foreign debtors wanting their cases to be a main proceeding, United States courts have decided this issue by determining where the debtor has its "center of main interests" (hereinafter "COMI"). Chapter 15 does not define COMI, and because the enactment of Chapter 15 is both recent, and has a dearth of explanatory case law, courts are left to either consider the limited jurisprudence in the U.S. or to look internationally as

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> an entity to file a petition commencing a case under this title or the right of any party to file claims or take other proper actions in such a case.

11 U.S.C. § 1520.

[22] Hammer & McClintock at 269(noting further that while the filing of a Chapter 11 in the United States by the foreign debtor is somewhat limited, only assets within the territorial jurisdiction of the United States would be included in the case. However, the authors further note that through the use of a Chapter 11 it would confer upon the foreign representative the rights and powers to pursue preference and fraudulent transfer actions).

[23] Relief available to the debtor in a foreign nonmain proceedings includes, but is not limited to those provisions in 11 U.S.C. § 1521(a).

instructed by § 1508.[24] Courts considering the issue have deferred to the location of the debtor's registered office[25] and have considered the type and amount of contacts between the debtor and foreign nation where the insolvency proceedings were initiated.[26] Compounding this lack of precedent, the exacerbating factor of a worldwide financial crisis has emerged making certainty with and access to Chapter 15 even more pressing. As the world financial crisis has continued to deepen, three important decisions regarding recognition, each involving hedge funds located in the Cayman Islands, is beginning to shape the landscape of Chapter 15 recognition jurisprudence.

IV. The Hedge Fund Triad

The continuing collapse and strain on hedge funds certainly appears to be one of the harbingers of a prolonged global financial crisis. At the end of 2008, hedge funds, as broadly defined, held over $2.5 trillion dollars in assets and were located primarily outside of the United States.[27] With the souring worldwide economy further restricting credit and causing large downturns in nearly all sectors of economies worldwide, some hedge funds have been severely impacted and have sought the protection of both their origin or haven country, while seeking Chapter 15 protection as well. Since 2007, three important Chapter 15 recognition decisions, involving Cayman Island hedge funds, have

[24] Section 1508 states that "[i]n interpreting this chapter, the court shall consider its international origin, and the need to promote an application of this chapter that is consistent with the application of similar statutes adopted by foreign jurisdictions." 11 U.S.C. § 1508.

[25] *See In re Tri-Continental Exchange, Ltd.*, 349 B.R. 627 (Bankr. E.D. Cal. 2006).

[26] *See In re SPhinX, Ltd.*, 351 B.R. at 122 (Bankr. S.D.N.Y. 2006).

[27] *See* www.aima.com. While the funds themselves are primarily located off-shore from the United States, the most popular offshore location was the Cayman Islands (57% of number of offshore funds), followed by British Virgin Islands (16%) and Bermuda (11%). Other offshore centers are the Isle of Man and the Republic of Mauritius. An important distinction also worth noting is that while the hedge funds themselves are located off-shore, they have no employees and only investors. The actual human component of the hedge funds is found in the hedge fund manager, normally located in the United States.

been rendered. Each provides further guidance on how Chapter 15 recognition will be decided by U.S. courts.

A. *In re SPhinX, Ltd.*[28]

The debtor hedge funds in *SPhinX* were established under and regulated by Cayman Islands law. Besides complying with some minimal Cayman Islands legal requirements, namely keeping certain books and records, the hedge funds basically had no contacts with or connection to the Cayman Islands. Specifically, they had no employees, offices, directors or assets in the Cayman Islands. Most of the funds assets were located in United States accounts and the hedge fund manager was a Delaware corporation located in New York.

In July of 2006, the debtor hedge funds filed voluntary petitions in the Cayman Islands and petitioned for Chapter 15 relief in the U.S. The U.S. bankruptcy court recognized the Cayman Islands proceeding as a "foreign proceeding," but struggled with whether it should be recognized as a foreign main or nonmain proceeding. In reaching its determination, the court considered "the location of the debtor's headquarters," "the location of those who actually manage the debtor," "the location of the debtor's primary asset," "the location of the majority of the debtor's creditors or of a majority of the creditors who would be affected by the case" and "the jurisdiction whose law would apply to most disputes."

In weighing these factors the court noted that flexibility was important and that any decision should be made with due consideration of Chapter 15's focus on protection of interested parties, the use of fair procedures and maximization of the value of the debtor for the benefit of creditors. The court focused heavily on whether the creditors

[28] *In re SPhinX, Ltd.*, 371 B.R. 10 (S.D.N.Y. 2007).

opposed, supported or provided no position on the issue of whether the debtor should be considered a foreign main proceeding.

After careful review the court decided that recognition of the Cayman Islands proceedings as a foreign main proceeding would not be granted. The court declined to recognize the foreign proceeding due to what the court found was the primary purpose of the bankruptcy filing, namely evidence of forum shopping and the frustration of an existing judgment. While there could have been other proper purposes for the filing, at the time of the adjudication of the recognition decision those were the only purposes supported by the evidence before the court.

The court reasoned that "[s]uch circumstances as [these] support denial of recognition as a foreign main proceedings on that the ground that the recognition is being sought for an improper purpose."[29] The debtor appealed and the district court affirmed the decision, but noted that despite the many factors against recognition of a foreign main proceeding, the bankruptcy could still grant the recognition if there was no objection by creditors.

B. *In re Basis Yield Alpha Fund*[30]

The debtors, Cayman Islands' hedge funds, filed for liquidation due to the global economic downturn and loss of value in fund assets. The debtors then sought Chapter 15 protection and recognition as a foreign main proceeding. No creditors objected and the debtors filed no evidentiary support for this recognition request, instead relying solely on

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[29] *Id.*

[30] *In re Basis Yield Alpha Fund*, 381 B.R. 37 (Bankr. S.D.N.Y. 2008)

the presumptions contained in § 1516 which provides that "[i]n the absence of evidence to the contrary, the debtor's registered office…is presumed to be the [debtor's COMI]."[31]

The court rejected the statutory presumption, concluding instead that it had the power to require evidentiary support for the recognition, even in the absence of creditor objections. Instead, the court held that like the debtor in *SPhinX*, the debtors in *Alpha Fund* had little or no contact with the Cayman Islands and therefore would need to present evidence to support its assertion that it should be granted foreign main proceeding status.

C. *In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd.* [32]

The debtors, open-ended investment companies with registered offices in the Cayman Islands, filed insolvency proceedings in the Cayman Islands after a massive devaluation of their asset portfolios due to the worldwide economic turmoil. Except for two directors, the funds had no employees, assets or operations in the Cayman Islands. After filing insolvency proceedings in the Cayman Islands, the debtors sought Chapter 15 protection in the U.S., seeking recognition as a foreign main, or alternatively, nonmain proceeding.

The bankruptcy court undertook the same analysis as was performed by the *SPhinX* court, but gave no weight to whether or not creditors objected to recognition as requested by the debtors. Instead, the court found that there is generally a presumption under § 1508 that if the registered office of the debtor is located in the jurisdiction where

[31] 11 U.S.C. § 1516.

[32] *In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd.*, 374 B.R. 122 (Bankr. S.D.N.Y. 2007)

the proceeding is filed then the proceeding will be recognized as a foreign main proceeding. However, the court ruled that this presumption is for administrative efficiency and does not relieve a court of its duty to make a determination that the presumption is justified. The court then went on to hold that if there is evidence that an entity's COMI is located somewhere other than the haven state, then the foreign representative has the burden of proving the COMI in order to gain main or even nonmain recognition.

Due to what the bankruptcy court deemed only tangential contacts of the funds with the registered office jurisdiction of the Cayman Islands, the court refused to recognize the Cayman Islands proceedings as a foreign main proceeding. Additionally, the court refused to grant the debtor foreign nonmain recognition. The court held that to be considered a foreign nonmain proceeding non-transitory economic activity must be conducted in that foreign jurisdiction. The court determined that the only economic activities that were performed in the Cayman Islands were done to support the U.S. based business, therefore falling short of establishing the non-transitory burden.

The debtors appealed the bankruptcy court's decision to the district court.[33] The debtors argued that there were in fact substantial connections between the funds and the Cayman Islands. Specifically, the debtors stated that most of the funds remaining liquid assets were in bank accounts in the Cayman Islands. The district court rejected this assertion, instead finding that prior to the Chapter 15 all of the hedge funds' funds were in the United States and that only after the Chapter 15 filing did the funds direct some-millions of dollars in cash to accounts in the Cayman Islands.

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[33] *In re Bear Sterns High-Grade Structured Credit Strategies Master Fund, Ltd.*, 389 B.R. 325 (S.D.N.Y. 2008).

The debtors further stated that two directors lived in the Cayman Islands. The district court rejected this assertion as well, finding instead that the directors living in the Cayman Islands were not shown to have had any substantial involvement in the business of the funds. The debtors additionally argued that the funds investors and creditors knew or should have known that the funds were incorporated in the Cayman Islands. The court rejected this argument due to no evidence being offered to even suggest that any creditor or investor of the funds knew, or had reason to know of the funds Cayman Islands incorporation or of any location of the funds other than at the New York offices of Bear Stearns.

The funds next asserted that the funds had substantial connections to the Cayman Islands due to the fact that the funds were subject to Cayman Island tax laws and were required to be wound up in the Cayman Islands. The court brushed aside these facts, finding instead, even if true, neither constituted substantive economic activity in the Cayman Islands. Finally, the funds asserted that substantial connections were demonstrated by Cayman Islands based attorneys and accountants performing the pre-filing insolvency work. The district rejected this assertion, holding instead that even if accurate, this fact was outweighed by the overall full set of objective facts determining there were not substantial connections between the fund and the Cayman Islands.

The district court then affirmed the bankruptcy court decision stating that "[t]he lack of objection to the petition may result from any number of considerations, unknown to the courts but subject to any assumption. That absence does not relieve the bankruptcy court of its duty to apply the statute as written."[34]

[34] *Id.* at 338 (quoting 11 U.S.C. § 1502(2)).

Additionally, the district court affirmed the bankruptcy court's decision to not grant recognition of the debtors as a foreign nonmain proceeding. The debtors argued that at minimum, the funds connections to the Cayman Islands constituted an "establishment," defined by § 1502(2) as "any place of operations where the debtor carries out nontransitory economic activity."[35] The district court disagreed, holding instead that the "existence of an establishment is essentially a factual question, with no presumption in its favor."[36] Therefore, the bankruptcy court's finding that there was insufficient nontransitory economic activity prior to the bankruptcy filing, coupled with the fact that the funds had no assets in the Cayman Islands at the time of filing was sufficient to support the conclusion that nonmain recognition would be inappropriate.[37]

V. Recent Chapter 15 Trends and Filings

Despite the global economic downturn, and overall increase in bankruptcy filings, Chapter 15 has not really followed this trend.[38] Instead, as of the writing of this article, Chapter 15 filings appear to have no relationship volume-wise to the current economic crisis.[39] Due to this disconnect between the number of Chapter 15 filings and economic health of the world as a whole, Chapter 15 filings do not appear to be a good indicator of the state of the world's financial systems. Instead, analysis of Chapter 15 filings

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[35] *Id.*

[36] *Id.*

[37] *Id.* at 339.

[38] *See* Ben Rooney, Bankruptcy filings rise 30% this year (December 15, 2008), http://money.cnn.com/2008/12/15/news/economy/bankruptcy_3Q/index.htm (stating that overall bankruptcies have continued to rise from the lows after the enactment of BAPCPA to current).

[39] The Administrative Office (the "AO") provides data of Chapter 15 bankruptcy filings that runs two quarters behind. In 2005 the AO reported 6 Chapter 15 filings, in 2006 75 filings, in 2007 42 filings and through the second quarter of 2008, 19 filings. A review of the most likely places historically for a Chapter 15 to file, namely the Southern and Western Districts of New York and Delaware show that just in those courts during the third and fourth quarters of 2008 there have been 39 filings.

collectively or individually seems better suited to understand the weaknesses in select business, whether micro or macro, and potentially may allow a deeper understanding of the condition of certain industries.

Hedge fund debtors are noticeably absent from the most recent wave of Chapter 15 filings. Instead, the entities that have recently sought bankruptcy protection under Chapter 15 represent a sampling of companies from throughout the world facing a mixture of internal and external financial pressures and challenges.

Recent filings[40] fall into four general categories; (i) fraudulent activities by the entity itself or the principal of the entity;[41] (ii) bad business decisions and/or poor overall market conditions;[42] (iii) impact from the global financial crisis;[43] and (iv) use of Chapter

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[40] Recent filings for purpose of this article are cases filed in the third or fourth quarter of 2008.

[41] Recent filings involving fraudulent activities, or alleged fraudulent actions include *In re Super Save Superannuation Fund (In Liquidation)*, Case No. 08-14982 (Bankr. S.D.N.Y. 2008) (Australian ponzi scheme); *In re Integrity Plus Unit Trust (In Liquidation)*, Case No. 08-14959 (Bankr. S.D.N.Y. 2008) (Australian ponzi scheme); *In re Capacity Clothing, Inc.*, Case No. ___ (Bankr. S.D.N.Y. 2008) (Canadian company alleging misappropriation by principal).

[42] Recent filings involving bad business decisions or the impact of poor market conditions include: *In re Britannia Bulk PLC*, Case No. ___ (Bankr. S.D.N.Y. 2008) (British service provider to cargo interests purchased additional storage capacity immediately prior to capacity demand steeply dropping); *In re Pope & Talbot, Inc., et al*, Case No. ___ (Bankr. D. Del. 2008) (Canadian paper pulp and lumber mill company. Encountered low prices for products, higher business costs and a strengthening Canadian dollar that also impacted sales negatively); *In re Tembec Indus., Inc.*, Case No. ____ (Bankr. S.D.N.Y. 2008) (Canadian lumber companies filing due to decreased demand in their product); *In re Quebecor World, Inc.*, Case No. ____ (Bankr. S.D.N.Y. 2008) (Canadian commercial printer filed due to decrease in sales and increased competition).

[43] Recent filings resulting from the impact of the global financial crisis include *In re Glitnir Banki HF*, Case No. ____ (Bankr. S.D.N.Y. 2008) (Icelandic bank adversely affected by global financial crisis); *In re Landsbanki Islands HF.*, Case No. 08-________ (Bankr. S.D.N.Y. 2008) (Icelandic bank adversely affected by global financial crisis); *In re Destinator Technologies, Inc., et al.*, Case No. 08-11003 (Bankr. D. Del. 2008)(Canadian technology company forced to file due to lack of financing, compounded by operational and cost inefficiencies); *In re Bluepoint RE Ltd.*, Case No. 08-____ (Bankr. S.D.N.Y. 2008) (Bermudian re-insurer adversely affected by the "credit crunch"); *In re Corporacion Durango, S.A.B. de C.V.*, Case NO. 08-______ (Bankr. S.D.N.Y. 2008) (Mexican container company affected by the "severe liquidity crisis").

15 to complete the orderly winding down of companies.[44] The only commonality is the diverse use of Chapter 15 and the ever broadening jurisprudence being created.

VI. Conclusion

Clearly, the statutory interpretation and jurisprudence regarding Chapter 15 is still being developed. Due to the unprecedented and unforeseen financial crisis, quick, clear and consistent interpretations of this new statutory framework for international insolvencies by U.S. courts have becoming vitally important. As the hedge fund cases clearly show, consistent and strict adherence to the statutory language of Chapter 15 has not yet been achieved.

It is additionally unclear whether the hedge fund triad cases represent a trend in Chapter 15 jurisprudence, or whether those decisions are specific to hedge funds alone. It is an easier proposition to determine COMI when the foreign entity has actual business operations in the haven state. However, courts have struggled to find the same clarity with hedge funds set up in the Cayman Islands to allow investors to reap the resulting tax benefits. This lack of clarity jeopardizes the efforts of hedge fund managers, creditors and investors seeking the protections that Chapter 15 affords.

In normal economic times this lack of consistency would be frustrating, but in perilous economic times it can become extremely damaging to both investment funds in need of Chapter 15 protection, as well as creditors looking to salvage the remaining value of their investments. This real need for Chapter 15 is made even more urgent due to the hedge funds significant loses as a result of the recent credit catastrophe. With these

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[44] Recent filings involving the completion of the orderly wind-down of business include: *In re Global General and Reinsurance Co. Ltd.*, Case No. 08-_____ (Bankr. S.D.N.Y. 2008) (English insurance-reinsurance company completing orderly wind down); *In re Sphere Drake Ins. Ltd.*, Case No. 08-_____ (Bankr. S.D.N.Y. 2008) (English insurance-reinsurance company completing orderly wind down).

depletions of what were once large pools of liquid assets from which to provide funding, companies in financial crisis will find it much more difficult to obtain financing. Until this crisis passes it is unlikely that any of the recent Chapter 15 debtors will be able to look to this source of capital in order to finance operations in Chapter 15, or to finance a timely exit from the bankruptcy process. Only with clear and consistent bankruptcy court decisions will this new chapter become a dependable link in synchronizing the world's statutory insolvency schemes.

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SAUCE FOR THE GOOSE?
DUAL STANDARD EMERGING IN CROSS BORDER INSOLVENCIES:
DOMICILE NOT ENOUGH TO RECOGNIZE FOREIGN PROCEEDING

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SAUCE FOR THE GOOSE?
DUAL STANDARD EMERGING IN CROSS BORDER INSOLVENCIES:
DOMICILE NOT ENOUGH TO RECOGNIZE FOREIGN PROCEEDING

I. Introduction

Recent cases interpreting Chapter 15 of the United States Bankruptcy Code have created two different standards for recognizing whether domestic entities and foreign entities have filed insolvency proceedings in the proper venue. The issue of the double standard arises not in the actual venue of the Chapter 15 case, but in the refusal of some courts to recognize a foreign proceeding despite the fact that the foreign corporation filed in its country of registration, what would be its domicile and proper for venue under the United States venue statute, without the further showing that the foreign entity has an establishment in that country of registration. Thus some United States courts have refused to recognize a foreign proceeding notwithstanding that the foreign proceeding is itself filed in a proper venue.

The United States venue laws allow a debtor to commence a case in the district court for the district in which the debtor has its domicile, residence, principal place of business in the United States, or principal assets in the United States. A corporation's domicile is its state of incorporation. Thus, in the corporate context, domicile is sufficient to establish proper venue. A domestic corporation can file a petition in its state of incorporation even if the debtor has no contact with the state other than filing the pieces of paper and payment of the fees associated with maintaining its corporate status. In such a case, although venue may be challenged as being inconvenient, venue cannot be challenged as being improper.

In contrast, some United States courts have held that a foreign entity's country of registration is not sufficient to recognize a foreign insolvency proceeding. Chapter 15 provides a procedure for United States courts to recognize insolvency proceedings not filed in the United States. Under Chapter 15, United States courts require a foreign entity to have filed its insolvency proceeding where it has a "center of main interest" (COMI) to recognize a foreign proceeding as a main proceeding and an "establishment" to recognize a foreign proceeding as a foreign nonmain proceeding.

Some United States courts have indicated, contrary to some foreign courts, that the United States' concept of domicile, place of incorporation, is not sufficient for the recognition of a foreign proceeding. Some United States courts will not recognize a foreign proceeding pending in the country of the foreign entity's registration without further evidence of COMI such as a principal place of business or an "establishment" in that country. In these cases, to have an establishment means more than just to have a domicile.

The Bankruptcy Code specifically provides that when interpreting Chapter 15, "the court shall consider its international origin, and the need to promote an application of this chapter that is consistent with the application of similar statutes adopted by foreign jurisdictions." 11 U.S.C. § 1508. Despite this mandate in the statute, some recent United States decisions have refused to recognize foreign proceedings filed in the country of the foreign entity's organization, thus

holding foreign debtors to a higher standard than would be applied to a domestic corporate debtor filing in its domicile, its place of incorporation.

According to one commentator, the cases reflect a United States "legislative policy to provide the assistance of its bankruptcy courts only to those foreign bankruptcy proceedings that are premised on a tangible presence of the debtor in the foreign jurisdiction. If the debtor is really a U.S. business with only its technical domicile off shore, then the debtors' bankruptcy should be a U.S. affair."[1] Another commentator, discussing European laws, has suggested that the better approach would be to "preserve companies' flexibility to opt into a particular nation's corporate laws by domiciling in that nation, but would apply this choice to both corporate law and insolvency regulation. . . . Linking corporate and insolvency law to domicile would sharply reduce any risk that a company would choose an insolvency regime at the last minute to the benefit of insiders and the detriment of everyone else. The location and source of regulation would be clear because it would be determined by the company's domicile."[2]

This *sub rosa* policy of directing financially troubled multinational companies into the United States bankruptcy system seems to contradict the purpose of Chapter 15 in the first place and creates a double standard for foreign over domestic debtors.

II. Background of Chapter 15

The Bankruptcy Abuse, Prevention and Consumer Protection Act of 2005, which was signed into law in the United States on April 20, 2005, and became effective, for the most part, on October 17, 2005, created a new chapter of the United States Bankruptcy Code (11 U.S.C. § 101, *et seq.*, as amended) (the "Bankruptcy Code")[3] – Chapter 15. Chapter 15 is entitled "Ancillary and Other Cross Border Cases," and replaced Bankruptcy Code Section 304 in dealing with cross border cases.

Chapter 15 is based on the Model Law on Cross Border Insolvency which had been prepared by the United Nations Commission on International Trade Law (UNCITRAL), with significant input from insolvency practitioners all over the world. *U.S. v. J.A. Jones Constr. Group, LLC*, 333 B.R. 637, 638 (E.D.N.Y. 2005). It was designed to create procedures for cooperation among foreign courts where insolvency proceedings are pending in more than one country and establish guidelines for the protection of assets internationally, while being sensitive to the political issues and differing legal systems of the countries involved. Any determination of a request for assistance under Chapter 15 must be "consistent with the principles of comity." [4] 11 U.S.C. § 1507; *see J.A. Jones*, 333 B.R. at 638.

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[1] Glosband, Daniel M., *Bankruptcy Court Rejects Cayman Proceedings of Bear Stearns Hedge Funds*, AM. BANKR. INST. J. Vol. XXVI, No. 8 (Oct. 2007), available at www.abiworld.org.

[2] Skeel, David A., *European Implications of Bankruptcy Venue Shopping in the U.S.*, 54 BUFF. L. REV. 439, 463 (JULY 2006).

[3] Unless otherwise indicated, all citations to Sections of the Bankruptcy Code contained herein are to those Sections as they exist after October 17, 2005.

[4] "Comity," in the legal sense, is neither a matter of absolute obligation, on the one hand, nor of mere courtesy and good will, upon the other. But it is the recognition which one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and

Chapter 15 establishes more detailed procedures and, in certain instances, expands the rights of the foreign representative from those previously provided under Section 304. Chapter 15 follows the UNCITRAL model law by expressly encouraging cooperation and communication between courts handling cross border cases. 11 U.S.C. § 1525. While most courts in the United States and other countries have effectively utilized cross border protocols and cooperation agreements, some have been reluctant to do so without express statutory authority. Chapter 15 further establishes procedures and recommendations for communication and cooperation between U.S. case trustees and examiners, their foreign counterparts and foreign courts. 11 U.S.C. §§ 1526 and 1527.

A Chapter 15 case is commenced by the filing of a petition seeking recognition of a foreign proceeding by a foreign representative. 11 U.S.C. § 1504. Chapter 15 is designed so that the recognition procedure is the gateway to a foreign representative's access to state and federal courts in the United States on behalf of a foreign debtor.

III. General Provisions

Both foreign and domestic creditors have the same rights regarding commencement and participation in a Chapter 15 case. However, Chapter 15 does contain special notification procedures for foreign creditors and enables the court to provide additional time for foreign creditors to file proofs of claim. 11 U.S.C. § 1514. With the exception of foreign insurance companies, the limitations on who may be a debtor, as set forth in 11 U.S.C. § 109, still apply. 11 U.S.C. § 1501(c).

Who May Be a Debtor

Section 109 of the Bankruptcy Code defines who may be a debtor under the various chapters of the Bankruptcy Code. Section 109(a) provides that a person may be a debtor under the Bankruptcy Code if the person "resides or has a domicile, a place of business, or property in the United States . . . ." 11 U.S.C. § 109(a). Although a "person" is defined, generally, as an individual, partnership, or corporation, 11 U.S.C. § 101(41), other legal entities have also been found to be a "person" and thus an eligible debtor. *See e.g.*, *In re Midpoint Dev., LLC*, 313 B.R. 486 (Bankr. W.D. Okla. 2004) (concluding that a state limited liability company is a "person" and thus an eligible debtor). Foreign corporations are, therefore, generally eligible for relief under the Bankruptcy Code.

Chapter 15 expressly incorporates the limitations of Section 109(b) as to who may seek relief under Chapter 15. 11 U.S.C. § 1501(c). Under Section 109(b), any person is eligible for relief under Chapter 7 (liquidation) except for railroads, insurance companies, and certain banking

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convenience, and to the rights of its own citizens or of other persons who are under the protection of its laws. *Hilton v. Guyot*, 159 U.S. 113, 163-64, 16 S.Ct. 139, 143 (1895). A comity analysis is appropriate only when (1) there is no legislative direction prohibiting a comity analysis; and (2) a true conflict exists between U.S. law and the law of a foreign jurisdiction. *Maxwell Communication Corp. v. Societe Generale (In re Maxwell Communication Corp.)*, 93 F.3d 1036, 1047 (2nd Cir. 1996) (citations omitted).

institutions. 11 U.S.C. § 109(b). Any person eligible for relief under Chapter 7, except for stockbrokers or commodity brokers, may file for relief under Chapter 11. 11 U.S.C. § 109(d). *See In re Agency for Deposit Ins., Rehabilitation, Bankr. and Liquidation of Banks,* No. 03 Civ. 9320(JSR), 03 Civ 9321(JSR), 2004 WL 414831 (S.D.N.Y. Mar. 4, 2004) (noting that Yugoslavian bank was not eligible to be a debtor under Section 109). Chapter 15 expands the category of eligible debtors, specifically stating that foreign insurance companies are now eligible for relief under Chapter 15. 11 U.S.C. § 1501(c).

In summary, a foreign corporation that is not a railroad or a banking institution, and that has a residence, domicile, place of business, or property in the United States, can obtain relief under Chapter 15. Additionally, notwithstanding the proscription of Section 109, foreign insurance companies may also be debtors under Chapter 15.

Who May File a Chapter 15 Petition

Any "foreign representative" appointed in a "foreign proceeding" who is authorized to either administer the financial restructuring, liquidation or reorganization of a debtor's assets, or is authorized to act as a representative in a foreign proceeding, is authorized to file a petition seeking recognition of the foreign proceeding in the United States. *See U.S. v. J.A. Jones Constr. Group, LLC*, 333 B.R. 637, 638 (E.D.N.Y. 2005). The minimal requirements for recognition of a foreign proceeding are some type of documentation or certification from the foreign court confirming the existence of the foreign insolvency proceeding and the authority of the foreign representative to act. *See In re Artimm*, *S.R.L.*, 335 B.R. 149, 158 (Bankr. C.D. Cal. 2005). A petition for recognition 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 establishing the existence of the foreign proceeding and the appointment of the representative; or (3) other acceptable evidence of the existence of the foreign proceeding and the appointment of the foreign representative. *Id.* This is a less exacting standard than that which existed under prior Section 304, which required some investigation into the nature and purpose of the foreign proceeding. While the definition of "foreign representative" has been modified in Chapter 15, the prior statute was interpreted broadly, and it is unlikely that the definitional changes will have much practical impact on who is a foreign representative.

IV. The Double Standard: United States Venue Statutes and Recognition of Foreign Proceedings

The Venue Statutes and Rules

Sections 1408, 1409, and 1410 of the United States Code set forth proper venue for cases under title 11, proceedings arising under, arising in, or related to cases under title 11, and venue of cases ancillary to foreign proceedings.

Except for Chapter 15 cases, cases under title 11 may be commenced in the district court for the district—"(1) in which the domicile, residence, principal place of business in the United States, or principal assets in the United States, of the person or entity that is the subject of such case

have been located" for a specified period of time; or "(2) in which there is pending a case under title 11 concerning such persons' affiliate, general partner or partnership." 28 U.S.C. § 1408.[5]

Section 1408(1) provides four alternative tests for determining whether venue is sufficient: the debtor's domicile, residence, location of principal place of business in the United States, or location of principal assets in the United States. 11 U.S.C. § 1408(1); 1 COLLIER ON BANKRUPTCY ¶ 4.01[2][a] (Lawrence P. King ed., 15th ed. revised 2008). Any one of the four possible venue locations is sufficient. *Id.* "The statute allows many possible locations where an entity or individual may file for bankruptcy protections." *Broady v. Harvey (In re Broady)*, 247 B.R. 470, 472 (B.A.P. 8th Cir. 2000).

Under Section 1408(1), the prospective debtor selects the venue for its Chapter 11 reorganization. *In re Enron Corp.*, 274 B.R. 327, 341 (Bankr. S.D.N.Y. 2002). "Venue in the district in which the debtor files its bankruptcy petition is presumed to be proper, and the party challenging venue bears the burden of establishing by a preponderance of the evidence that [the] case was incorrectly venued." *In re Broady*, 247 B.R. at 472-73.

The ability to file in many possible locations allows debtors to select the most favorable forum. That fact has been noted by a leading bankruptcy treatise: "Section 1408(1) has been used to permit the most blatant form of forum shopping." 1 COLLIER ON BANKRUPTCY ¶ 4.01[2][b] (Lawrence P. King ed., 15th ed. revised 2008). But, "forum shopping is permitted by the literal language of the statute." *Id.* at ¶ 4.01[3].

The ability to file in different forums may lead to a filing in a forum that, though proper, is somehow unfair or inconvenient for certain other parties in the case. In those cases the Bankruptcy Code provides for a change in venue: "A district court may transfer a case or proceeding under title 11 to a district court for another district, in the interest of justice or for the convenience of the parties." 28 U.S.C § 1412. "This standard is "broad and flexible." *In re Innovative Communication Co., LLC,* 358 B.R. 120 (Bankr. D. Del. 2006), *on motion for reconsideration*, 2007 Bankr. D. Del. Feb. 13, 2007) (quoting *Gulf States Exploration Co. v. Manville Forest Prods. Corp. (In re Manville Forest Prods. Corp.)*, 896 F.2d 1384, 1391 (2d Cir. 1990)).

In considering the convenience of the parties, the Court weighs the proximity of the debtor, the creditors and the witnesses to the court, the location of the debtor's assets, the economic administration of the estate, and the necessity of ancillary administration in the event of liquidation. *In re Enron Corp.*, 274 B.R. at 343. "The factor to be given the most weight is the promotion of the economic and efficient administration of the estate." *Id.* When considering the

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[5] Chapter 15 cases may be commenced in the district court of the United States for the district—"(1) in which the debtor has its principal place of business or principal assets in the United States; (2) if the debtor does not have a place of business or assets in the United States, in which there is pending against the debtor an action or proceeding in a Federal or State court; or (3) in a case other than those specified in paragraph (1) or (2), in which venue will be consistent with the interests of justice and the convenience of the parties, having regard to the relief sought by the foreign representative. 28 U.S.C. § 1410.

"interest of justice," the court considers "whether transfer of venue will promote the efficient administration of the estate, judicial economy, timeliness, and fairness. *Id.*[6]

Enron was one of the ultimate venue forum shopping cases. Enron had one minor subsidiary incorporated in New York with very few employees. Enron's principal place of business was in Houston, as were all its major officers and many of its employees. Houston was the major hub of its operations. Enron's assets were global, with few, if any, being located in the Southern District of New York. On a motion to transfer venue, the Court concluded that notwithstanding these facts, Enron's major creditors (money center and international financial institutions) as well as its counsel, were in New York. The Court did not mention that most of these financial institutions, as well as its counsel, also had offices in Houston. The unstated gloss of the opinion was simply that the Southern District of New York was simply a better place to be because the court, and the local bar and creditors were more sophisticated in the handling of mega chapter 11 cases.

Although the Bankruptcy Code and Rule 1014 provide for the transfer of venue, bankruptcy courts have noted that "[t]ransferring venue of a bankruptcy case is not to be taken lightly." *In re Enron Corp.*, 274 B.R. at 342. "A debtor's choice of forum is entitled to great weight if venue is proper." *In re Enron Corp.*, 274 B.R. at 342. The burden of proof is on the party moving for change of venue, and that party must carry that burden by a preponderance of the evidence. *In re Dunmore Homes, Inc.*, 380 B.R. 663 (Bankr. S.D.N.Y. 2008). As discussed further below, less weight is given to a foreign entity's choice of forum.

In addition, the ability to file in many possible locations may also lead to a situation in which petitions involving the same or related debtors are filed in different locations. The debtor may file in one location that it perceives to be favorable, while the creditors may file an involuntary petition against the debtor in a forum that they perceive to be more favorable. *See e.g., In re Innovative Communication Co., LLC,* 358 B.R. at 120.[7] The European Courts are also starting

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[6] Federal Rule of Bankruptcy Procedure 1014 ("Rule 1014") provides the procedure to transfer the case:

> If a petition is filed in the proper district, the court, on the timely motion of a party in interest or on its own motion, and after hearing on notice to the petitioners, the United States trustee, and other entities as directed by the court, may transfer the case to any other district if the court determines that the transfer is in the interest of justice or for the convenience of the parties.

Fed. R. Bankr. P. 1014(a)(1).

[7] This situation also is addressed by Rule 1014:

> (b) Procedure When Petitions Involving the Same Debtor or Related Debtors are Filed in Different Courts. If petitions commencing cases under the Code are filed in different districts by or against (1) the same debtor, or (2) a partnership and one or more of its general partners, or (3) tow or more general partners, or (4) a debtor and an affiliate, on motion filed in the district in which the petitions filed first is pending and after hearing on notice to the petitioners, the United states trustee, and other entities as directed by the court, the court may determine, in the interest of justice or for the convenience of the parties, the district or districts in which the case or cases should proceed. Except as otherwise ordered by the court in the district in which the petition filed first is pending, the proceedings on the other petitions shall be stayed by the courts in which they have been filed until the determination is made.

to wrestle with this issue in the context of subsidiaries of a multinational parent filing in different countries. See discussion of *In re Eurofood IFSC Ltd., supra,* at p. 18.

Domicile

A domestic corporation may file a bankruptcy case in its state of incorporation, even if it has no other ties to that district. Venue of a case under title 11 is proper in the district in which a person has a domicile. 28 U.S.C. § 1408. "Domicile" is defined by federal law, among other reasons, because Congress intended the federal bankruptcy statutes to have uniform application. *Donald v. Curry (In re Curry)*, 328 B.R. 192, 200 (B.A.P. 9th Cir. 2005). "[N]on-uniform state-law definitions of domicile could produce nonsensical results in frustrations of the purpose of the statute." *Id.* (citing *Miss. Band of Choctaw Indians v. Holyfield*, 490 U.S. 30, 45-46 (1943)).

Under federal law, a corporation's domicile is its state of incorporation. *In re Innovative Communication Co.*, 358 B.R. at 125; *In re Segno Communications, Inc.*, 264 B.R. 501 (Bankr. N.D. Ill. 2001); *Underwood v. Hilliard* (*In re Rimsat, Ltd.*), 98 F.3d 956, 960 (7th Cir. 1996) (citing *Bank of Augusta v. Earle*, 38 U.S. (13 Pet.) 519, 588, 10 L.Ed. 274 (1839)); Restatement (Third) of the Foreign Relations Law of the United States § 213 (1987)).

Applying the venue statute in the corporate context, domicile is sufficient to establish proper venue. In such a case, although venue may be challenged as being inconvenient, venue is rarely challenged as, and would not be considered, improper. For example, in *In re Dunmore Homes, Inc.*, the debtor, Dunmore New York, filed its voluntary petition under Chapter 11 in the Southern District of New York. *In re Dunmore Homes, Inc.*, 380 B.R. at 669. Creditors filed a motion for change of venue arguing that the debtor's only contact with New York was the fact that it was incorporated in that state. The creditors did not argue that domicile was an improper forum, but that venue should be transferred to California in the interest of justice and for the convenience of the parties. The court agreed and transferred the case. *Id.* at 677. Before doing so, however, the court noted that Dunmore New York was incorporated in New York and would be considered domiciled there. *Id.* at 670. Therefore, the venue selected by the debtor was proper under Section 1408. *Id.*

Similarly, *In re B.L. of Miami*, 294 B.R. 325, 328 (Bankr. D. Nev. 2003), the Nevada court found that "[s]ince the Debtor is incorporated here in Nevada, the District of Nevada may be considered Debtor's domicile and venue is thus proper under § 1408(1)." Although venue was technically proper in Nevada, the debtor's business activities and trade creditors were in Miami, Florida. *Id.* at 334. In the interest of justice, the court transferred the case to the United States Bankruptcy Court for the Southern District of Florida. *Id.*

In *In re Segno*, however, the debtor challenged venue in its domicile and moved to dismiss an involuntary Chapter 7 that creditors had filed against it in Illinois. *In re Segno Communications, Inc.*, 264 B.R. 501, 504 (Bankr. N.D. Ill. 2001). The debtor, a dissolved Illinois corporation, argued that venue was improper in Illinois because Segno's principal place of business was in Indiana. *Id.* The evidence showed, and the creditors' counsel conceded, that Segno's principal place of business was in Indiana. The court analyzed Section 1408(1) and noted that Section 1408(1) provided four alternative bases for venue: domicile, residence, principal place of

business and the location of the debtor's principal assets in the United States. *Id.* at 505. "Given that those four tests are stated in the alternative, any of the four is jurisdictionally sufficient." *Id.* The court further stated that Section 1408(1) treats individual and non-individual debtors the same for determining proper venue. *Id.* Thus, the "domicile" of a corporate debtor may be a proper venue for a bankruptcy case. *Id.* "To determine the domicile of a corporation we look to the state of its incorporation." *Id.* (citing *In re FRG Inc.*, 107 B.R. 461, 471 (Bankr. S.D.N.Y. 1989). The court found that Segno's domicile was the state of Illinois and, pursuant to 28 U.S.C. § 1408(1) the Northern District of Illinois was the proper venue for the creditors' involuntary Chapter 7 petition. *Id.* at 511. The court denied the motion to dismiss. *Id.*

Similarly, in a case of dueling venues, the court transferred venue not because the debtor's filing in its domicile was improper, but because the forum in which the debtors' had their principal places of business best satisfied the interest of justice. *In re Innovative Communication Co.*, 358 B.R. at 125. In *In re Innovative Communication Company, LLC,* involuntary cases were filed against three debtors, Innovative Communications Company, LLC ("ICC-LLC"), Emerging Communications, Inc., ("Emerging"), and Jeffrey Prosser ("Prosser"), an individual, in the United States Bankruptcy Court for the District of Delaware. ICC-LLC was a Delaware limited liability company with its principal place of business in the U.S. Virgin Islands ("USVI"). *Id.* at 122. Emerging was a Delaware corporation with its principal place of business in USVI. *Id.* Prosser was an "affiliate"[8] of ICC-LLC and Emerging. *Id.* Citing Section 1408(1), the court found that venue was appropriate in the state of incorporation, so venue was "proper in Delaware with respect to the corporate Debtors." *Id.* at 125. Acknowledging that the venue of Prosser's case was less clear, as he did not reside nor was he domiciled in Delaware, the court found that venue of his case still could lie in Delaware because of Prosser's "affiliate" status. *Id.*

The court then found that the corporate debtors had operations in USVI and that Prosser had a residence in the USVI. ICC-LLC's principal place of business, employees and assets were in the USVI. Its principal asset was Emerging stock, and Emerging was the parent of a USVI corporation that controlled the USVI telephone company. There were no books, records or witnesses in Delaware. The public interest pointed to USVI. *Id.* at 127. There was nothing in the record to indicate that Delaware would be the best venue with respect to Prosser. *Id.* at 129. Based on these facts, the court found that, for all three debtors, the USVI venue was proper and best satisfied the interests of justice. *Id.*

These cases illustrate that, in the corporate context, a filing in the state of the entity's domicile, although not necessarily the most convenient venue, is still a proper venue. This provision of the bankruptcy venue statute, however, has not been without controversy. The unfairness to employees and often, even creditors, when a corporation chooses to file in its state of incorporation, notwithstanding its lack of any assets, operations or employees in that state, have

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[8] The Bankruptcy Code defines "affiliate" in part as and (A) entity that directly or indirectly owns, controls, or holds with power to vote, 20 percent or more of the outstanding voting securities of the debtor. . ." *In re Innovative Communication Co.*, 358 B.R. at 125 (citing 11 U.S.C. § 101(2)(A)). Prosser wholly owned ICC-LLC. *Id.* at 122.

been discussed in numerous articles, cases and by Congress.[9] One commentator has written at length about the history of the Delaware bankruptcy cottage industry and the perceived corruption of a system where major cases are funneled to a few bankruptcy courts such as Delaware and the Southern District of New York. *See* LoPucki, Lynn M., *Courting Failure: How Competition for Big Cases is Corrupting the Bankruptcy Courts*, The University of Michigan Press 2005. Many speculate as to the future of this venue provision now that Senator Joseph Biden (D-Delaware) is no longer chair of the Senate Judiciary Committee which, for years, managed to table any attempts to change the bankruptcy venue provisions as to corporate domicile.

Definition of Foreign Proceeding

A different standard has been applied to foreign proceedings. A "foreign proceeding" is 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 purposes of reorganization or liquidation." 11 U.S.C. § 101(23); *see J.A. Jones*, 333 B.R. at 638 n.2. Most notable changes in this definition from Section 304 is that some type of court supervision of the foreign proceeding is expressly required, the reference to insolvency laws is broader than prior references to liquidation and debt adjustment, and the venue requirements of domicile, residence or principal place of business for the foreign proceeding are expanded to require only that the proceeding be filed in a foreign country (presumably to accommodate possible concurrent main and nonmain proceedings). A "foreign court" is defined as "judicial or other authority competent to control or supervise a foreign proceeding." 11 U.S.C. § 1502(3).

Main and Nonmain Foreign Proceedings

One of the most significant provisions of Chapter 15 adopted from the European Insolvency Regulation promulgated by the European Union ("EU") is the concept of determining whether a foreign proceeding is a "main" or "nonmain" proceeding, that is, whether the proceeding is one with primary control over the debtor and its estate. United States bankruptcy courts have used a test very similar to the "center of main interest" or "establishment" tests used in the EU in determining whether a foreign proceeding is main or nonmain.[10] While the definitions of main and nonmain contained in Chapter 15 may not have been intended to be venue concepts, the interpretation of the definitions have led to disputes in which United States courts have used the definitions to apply a higher standard for evaluating the proper venue of a foreign proceeding by refusing to recognize and otherwise properly filed foreign proceeding.

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[9] On February 8, 2005, Sen. John Cornyn (R-Texas) introduced legislation to amend 28 U.S.C. §1408 "to combat forum shopping" that the senator in his remarks on the Senate Floor asserted hurts "consumers, creditors, workers, pensioners, shareholders and small businesses." The bill amended §1408 by inserting a new subsection (b)(1) that defines a corporation's domicile and residence as "where the debtor's principal place of business is located." Jeffrey Morris, S.314-Fairness in Bankruptcy Litigation Act of 2005, Restricting Venue Choices for Corporate Debtors, ABI (web posted March 1, 2005 available at http://www.abiworld.org. The bill did not pass.

[10] For more information on cases analyzing the "center of main interest" ("COMI") or "establishment" tests visit www.eir-database.com.

The relief available to a foreign representative under Chapter 15 upon recognition of a foreign main proceeding by the United States bankruptcy court is significantly greater than that which had been available under former Section 304 in that, with certain exceptions, the panoply of rights available under Chapter 11 become immediately available to the foreign representative. Additionally, the foreign representative of a foreign main proceeding has the option of filing a full voluntary Chapter 11 case, while the foreign representative of a foreign nonmain proceeding is limited to filing an involuntary Chapter 11 case. Thus recognition is a critical first step for a foreign representative seeking the protections of United States Bankruptcy Code.

Center of Main Interest

Section 1502(4) provides that a "foreign main proceeding" is a foreign proceeding "pending in the country where the debtor has the center of its main interests." The use of the single criterion, center of main interests, for qualifying a foreign proceeding as a main proceeding is intended to avoid the risk of various foreign proceedings competing for recognition as the main proceeding. *In re Ran*, 390 B.R. 257, 263 (Bankr. S.D. Tex. 2008) (illustrating the process of developing the "center of main interests").[11]

COMI is not defined in the Bankruptcy Code. Section 1516 provides that, "In the 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. *In re Artimm*, 335 B.R. at 159. Thus, section 1516 provides a rebuttable presumption that the location of the debtor's registered office is the center of its main interests or COMI. *See In re Artimm*, 335 B.R. at 159; *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) (Pursuant to the introductory clause to [Section] 1516(c), however, that presumption may be rebutted.")

In *In re Artimm*, Artimm, S.r.l was an Italian corporation with its registered office in Rome. *Id.* at 155, 159. The court, applying the statute, stated that the debtor's center of main interests was presumed to be where its registered office is located. Noting that the issue had not been contested, the court assumed that, "under chapter 15, it would find that Artimm's center of main interests is located in Rome."

Section 1502(5) defines a "foreign nonmain proceeding" as a foreign proceeding "pending in a country where the debtor has an establishment." "Establishment" is defined in Section 1502(2) as "any place of operations where the debtor carries out nontransitory economic activity."[12]

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[11] In *Ran*, the court noted that both "domicile or habitual residence of the debtors" and "[principal place of business] [centre of debtor's main interests]" had been considered as sole bases for recognition. *In re Ran*, 390 B.R. at 263 n.2 (citing the Report of the Working Group on Insolvency Law on the Work of its Nineteenth Session, United Nations General Assembly A/CN. 9/44 (25 April 1996)). The Working Group was concerned about giving rise to the recognition of more than one foreign proceeding as "main" and agreed that the paragraph should be modified to refer to one fact as the test for foreign main proceeding. *Id.* It was agreed that the factor should be "centre of the debtor's main interests." *Id.*

[12] How these definitions will be applied in cases where a parent holding corporation is registered in one country, but its operating subsidiaries are registered in different countries and have operations in several others,

The Bankruptcy Code does not set forth the types of evidence that will be required to rebut the presumption that a debtor's COMI is its place of registration of incorporation. But two relatively recent cases in the Southern District of New York have discussed the factors that may be relevant to such a determination: *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) and *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).

Those factors that could be relevant to such a determination include: the location of the debtor's headquarters, the location of those who actually manage the debtor, the location of the debtor's primary assets, the location of the majority of the debtor's creditors or of the majority of the creditors who would be affected by the case; and/or the jurisdiction whose law would apply to most disputes. *In re Bear Stearns*, 374 B.R. at 128 (citing *In re Sphinx*, 351 B.R. at 117).

Applying the factors in *In re SPhinX*, the bankruptcy court determined that the presumption that a Chapter 15 debtor's registered office, the Cayman Islands, was its COMI had been sufficiently rebutted. *Id.* at 106. In *SPhinX*, the debtor had been incorporated and registered under the laws of the Cayman Island, the debtor kept some business records in the Cayman Islands, the company's auditors had an address in the Cayman Islands, certain investor subscriptions were received in the Cayman Islands, and one member of the Liquidation Committee was based in the Cayman Islands. *Id.* at 119.

Although the evidence of incorporation and registration alone would have been sufficient to establish domicile and thus proper (though not necessarily the most convenient) venue had the debtor been a domestic corporation filing in the district of its state of incorporation, the evidence was not sufficient to establish the Cayman Islands as the debtor's COMI. Instead, the court found that the evidence in the case strongly supported the conclusion that the Cayman Islands was not the debtor's COMI. *Id.* The debtor did not conduct business in the Cayman Islands, the debtor had no employees in the Cayman Islands, the debtor had no assets in the Cayman Islands, and almost all of the debtor's $500 million of assets were located in the United States. *Id.* at 107-08. Additionally, multiple lawsuits were pending against various debtor entities in the United States, various debtor entities had filed proofs of claims in United States bankruptcy cases, and all of the debtor's corporate administration was handled in the United States *Id.* The *SPhinX* court also considered the fact that the Cayman court would have to seek assistance from other courts, primarily the U.S. court, to realize on the assets and ensure the proceeds of the assets were used to pay creditors. *Id.* at 119. Further, most of the creditors and investors were

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remains to be seen. UNCITRAL's Legislative Guide had focused on the insolvency of a single debtor, as opposed to the insolvency of a corporate or enterprise group composed of a number of affiliated debtors, whether in a single state or across multiple jurisdictions. Working Group V of UNCITRAL has met specifically to address the issue of corporate groups in insolvency. The concept of "corporate groups" encompasses both horizontal and vertical affiliated companies, be they brother or sister entities or parent/subsidiary entities. *See UNCITRAL Refining Guidance on Multinational Corporate Insolvency*, February 20, 2008 available at http://www.allenovery.com/AOWEB/AreasOfExpertise/PrintEditorial.aspx. *See also*, U.N. Comm'n Int'l Trade Law, Report of Working Group V (Insolvency Law) on the Work of its Thirty-fifth Session, Vienna, 17-21 November 2008, December 2, 2008, ¶23-111 (discussing treatment of enterprise groups in insolvency).

not located in the Cayman Islands, and the Cayman courts would have to rely on other courts to bind those parties. *Id.* The culmination of these factors was sufficient to rebut the presumption that the Cayman Islands was the debtor's COMI. Therefore, the *SPhinX* court refused to recognize the foreign proceeding as a foreign main proceeding, but instead recognized the foreign proceeding as a foreign nonmain proceeding.

Another case decided under Chapter 15, *In re Tri-Continental Exchange, Ltd.*, 349 B.R. 627 (Bankr. E.D. Cal. 2006), set forth a straightforward application of the COMI presumption. The court stated that the registered office or place of incorporation was evidence that was "probative of, and that may in the absence of other evidence be accepted as a proxy for, 'center of main interests'" but does not otherwise carry special evidentiary weight. *Id.* at 635. If the foreign proceeding is not in the country of the registered office, then the foreign representative has the burden of proof on the COMI. If the foreign proceeding is in the country of the registered office, but there is evidence that the COMI is elsewhere, then the foreign representative must prove that the center of main interests is in the same country as the registered office. *Id.*

In this case, several insurance companies operating under the laws of the nation of St. Vincent and the Grenadines ("SVG") filed to wind up their operations in the SVG courts. The SVG proceeding appointed liquidators to the case. The Debtors were run by a United States citizen ("Brown") who had left the United States after being indicted by two different states. Brown was later convicted in absentia in Canada for fraud, and the United States government filed a criminal complaint against him. Brown was later arrested in Canada. Acting together, United States and SVG authorities shut down the Debtors' offices in Kingstown, St. Vincent. Brown died while in U.S. custody.

The liquidators in the SVG case identified millions of dollars worth of assets located all over the world. The liquidators then sought recognition under Chapter 15 as a foreign proceeding. A creditor at the hearing argued that the Debtors' COMI should be the United States because most of the allegedly defrauded creditors were located in the United States. The court discussed the enactment of Chapter 15 at length and held that the SVG case was a "foreign proceeding." The court also held that the fact that the Debtors were insurance companies and ineligible to be a debtor under the Bankruptcy Code does not affect the availability of Chapter 15 relief. *Id.* at 632. The creditors argued that the SVG case was not a foreign main proceeding, and that therefore, the Debtors were not entitled to relief under Section 1520 such as the imposition of the automatic stay and the authorization to operate the Debtors' business and exercise trustee rights. The court noted that whether the Debtors' case was a foreign main proceeding turned on the location of the Debtors' COMI. The court noted that Chapter 15 does not provide a definition for this term. The court then analyzed the legislative history and intent of UNCITRAL to determine the proper application of a debtor's COMI. *Id.* at 633-35. The court held that because the Debtors conducted regular business out of their registered offices in SVG, that was the Debtors' "principal place of business" and therefore the SVG proceedings were the foreign main proceedings.

A court's refusal to recognize a country of registration as a COMI may lead to a situation where, even though a foreign proceeding is pending, the United States court could refuse to recognize that foreign proceeding as either a foreign main or a foreign non-main proceeding, arguably

defeating the purpose of Chapter 15. In *In re Bear Stearns*, Burton R. Lifland, Honorable Bankruptcy Judge for the Southern District of New York, took up the issue of whether the provisional liquidators of Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd. and Bear Stearns High-Grade Structured Credit Strategies Enhanced Leverage Master Fund, Ltd. (together, the "Funds") could seek relief under Chapter 15 of the Bankruptcy Code as either a recognized "foreign main proceeding" under Section 1517 of the Bankruptcy Code or, in the alternative, as a recognized "foreign nonmain proceedings." 374 B.R. at 127. The Court determined that the Funds' Cayman Island proceedings were not entitled to recognition as either "main" or "nonmain" proceedings, but that the Funds could still seek protection by filing an involuntary petition pursuant to Section 303(b)(4) of the Bankruptcy Code. *Id.* at 132-33.

In addition to reciting the factors set forth in *SPhinX*, the *Bear Stearns* court explained that Chapter 15 directs courts to obtain guidance from the application of similar statutes by foreign jurisdictions. *Id.* at 128 (citing 11 U.S.C. § 1505). Although not binding on the court, one of the sources for persuasive guidance is the Guide to Enactment of the UNCITRAL Model Law on Cross-Border Insolvency ("Guide") that was promulgated in connection with the approval of the Model Law.[13] *Id.* The Guide explains that the use of the COMI concept to determine whether a foreign proceeding was a "main" proceeding "was modeled on the use of that concept in the European Union Convention on Insolvency Proceedings ("EU Convention") that was already in the process of being adopted when the UNCITRAL drafted the Model Law." In the regulation adopting the EU Convention, the COMI concept is described as "the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties." *Id.* at 129 (citing Council Reg. (EC) No. 1346/2000, ¶ 13; Case 341/04, *Bondi v. Bank of Am., N.A. (In re Eurofood IFSC Ltd.)*, 2006 E.D.R. I-3813, p. 18-19 ¶ 32, 2006 WL 1142304 (E.C.J. May 2, 2006). "This generally equates with the concept of a 'principal place of business' in United States law." *Id.* (citing *In re Tri-Continental Exchange Ltd.*, 349 B.R. at 633-34).

In this case, on July 31, 2007, the board of directors of the Funds had authorized the winding up of the Funds by filing petitions under the Companies Law of the Cayman Islands (the "Foreign Proceedings") and joint provisional liquidators ("JPLs") were appointed. *Id.* at 125. Once appointed, the JPLs filed petitions for recognition under Section 1515 seeking recognition of the Foreign Proceedings as "foreign main proceedings" as defined by Section 1502(4). *Id.* Section 1502(4) provides that a "foreign main proceeding" means "a foreign proceeding pending in the country whether the debtor has the center of its main interests." 11 U.S.C. § 1502(4). *Id.* at 127.

The JPLs argued that the Foreign Proceedings are pending in the country where the Funds have the "center of their main interests" because the Funds are Cayman Islands limited liability companies with registered offices in the Cayman Islands. *Id.* at 129. No other party had

[13] *See* Guide to Enactment of the UNCITRAL Model Law on Cross-Border Insolvency, U.N. Gen. Ass., UNCITRAL 30th Sess., U.N. Doc. A/CN.9/442 (1997); *see RSM Richter v. Aguliar (In re Ephedra Products Liability Litigation)*, 349 B.R. 333, 226 (S.D.,N.Y. 2006) ("the House Judiciary Committee, in enacting Chapter 15, specifically indicated that the Guide 'should be consulted for guidance as to the meaning and purpose of Chapter 15's provisions.'")

objected to the JPL's petition. *Id.* The court, again citing the Guide, stated that the COMI presumption does "not prevent, in accordance with applicable procedural law, calling for or assessing other evidence if the conclusion suggested by the presumption is called into *question by the court* or an interested party." *Id.* (citing Guide § 122) (emphasis in original). Then, despite the absence of objections, the Court took up the analysis of whether the Foreign Proceedings should be recognized as either a "foreign main proceeding" or "foreign nonmain proceeding." *Id.*

The court found that the Petitioners' own pleadings provided sufficient evidence to establish that the funds' COMI was the United States, not the Cayman Islands. *Id.* at 129. As stated by the court, "Section 1516(c) presumes that the COMI is the place of the debtor's registered office but only '[i]n the absence of evidence to the contrary.'" *Id.* at 129-30 (citing 11 U.S.C. § 1516(c)). From the verified petition, the court determined that the debtors' only connection with the Cayman Islands was that fact that the funds had registered there.

The verified petitions also showed that:

- The debtors had no employees or managers in the Cayman Islands.
- The investment manager for the Funds was in New York
- The administrator of the Funds was a Massachusetts corporation.
- The books and records of the Funds were kept in the United States.
- The Funds' investor registers were located in the Republic of Ireland.

Id. at 129.

The Court concluded that the only connection to the Cayman Islands was their registration in the Cayman Islands. Accordingly, the Funds did not have their center of main interest in the Cayman Islands. *Id.* at 130. Instead, the court determined that the Funds' real seat, and therefore, their COMI, was the United States, the place where the Funds conducted the administration of their interests on a regular basis and was "therefore ascertainable by third parties." *Id.* Thus, the Foreign Proceedings could not be recognized as "foreign main proceedings." *Id.* at 132.

The JPLs also petitioned for recognition of the Foreign Proceedings as "foreign nonmain proceedings." A "foreign nonmain proceeding" means a "foreign proceeding, other than a foreign main proceeding, pending in a country where the debtor has an establishment." 11 U.S.C. § 1502(5). The JPLs could not establish that the Funds had an "establishment" in the Cayman Islands (*i.e.*, "a local place of business"), and the Court concluded that the Foreign Proceedings were not "foreign nonmain proceedings." The Court commented that, "Chapter 15 . . . imposes a rigid procedural structure for recognition of foreign proceedings as either main or nonmain and thus the jurisprudence developed under Section 304 is of no assistance in determining the issues relating to the presumption for recognition under chapter 15." *Bear Stearns*, 374 B.R. at 17. In short, Judge Lifland's recognition of a Chapter 15 petition as foreign main or nonmain was a threshold prerequisite to receiving any relief from the Bankruptcy Court. In so holding, Judge Lifland parted with dicta in the *SPhinX* decision, discussed above regarding

COMI, "opining that if the parties in interest had not objected to the Cayman Islands proceeding being recognized as main, recognition would have been granted under the sole grounds that no party objected and no other proceeding had been initiated anywhere else." *Id*. at 130 (citing *In re SPhinX Ltd.*, 351 B.R. at 117).

The Court explained that the alternative when no foreign main or nonmain proceeding exists is to file for relief under Chapter 7 or Chapter 11 of the Bankruptcy Code. *Id*. at 132. Interestingly, the Court went on to state that the JPLs could find relief by filing an involuntary petition under Section 303(b)(4) of the Bankruptcy Code. *Id*. Section 303(b)(4) provides that an involuntary petition may be commenced "by a foreign representative of the estate in a foreign proceeding concerning such person." 11 U.S.C. § 303(b)(4). The Court determined that Section 303 does not require that the foreign proceeding be recognized as either main or nonmain, allowing the JPLs relief despite the lack of recognition of the Foreign Proceedings. *Bear Stearns*, 374 B.R. at 132-33. This reading is at odds with Section 1511, which governs commencement of a case under Section 301 or 303 by a foreign representative, and expressly requires that an involuntary case may be commenced by a foreign representative "upon recognition." 11 U.S.C. § 1511(a)(1).

On appeal, the district court affirmed Judge Lifland's decision holding that the foreign proceeding was neither a main nor a nonmain proceeding. *In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd.*, 389 B.R. 325, 327 (S.D.N.Y. 2008). In that opinion, Judge Sweet explained:

> The objective criteria for recognition reflect the legislative decision by UNCITRAL and Congress that a foreign proceeding should not be entitled direct access to or assistance from the host country courts unless the debtor had a sufficient pre-petition economic presence in the country of the foreign proceeding. *See* House Report at 110; § 1509(b)(3). If the debtor does not have its center of main interests or at least an establishment in the country of the foreign proceedings, the bankruptcy court should not grant recognition and is not authorized to use its power to effectuate the purposes of the foreign proceeding. *See* House Report at 113; Guide paras. 73, 75, 128. Implicitly, in such instance the debtor's liquidation or reorganization should be taking place in a country other than the one in which the foreign proceeding was filed to be entitled to assistance from the United States.

Id. at 333-34. The district court also held that the bankruptcy court had correctly interpreted the COMI presumption stating that "Judge Lifland was right to reject Appellants' position that 'this Court should accept the proposition that the Foreign Proceedings are main proceedings because the Petitioners say so and because no [one] else says they aren't.'" *Id.* at 335. It was the bankruptcy judge's duty to see that the law was properly administered. *Id.*

Turning to the standard for the COMI determination, the district court stated that COMI means "the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties." *Id.* at 336 (citing Council Reg. (EC) No. 13462000 ¶ 13). The court further stated that COMI is properly equated to the United States' concept of

"principal place of business." *Id.* (citing *Tri-Continental*, 349 B.R. at 129). The court agreed that the facts found supported the denial of main recognition. *Id.* at 338.

The court next held that the appellants had failed to allege facts establishing nonmain recognition. The appellants had argued that the Funds' connection to the Cayman Islands were sufficient to constitute an "establishment" under Section 1502. *Id.* Most of the Funds' remaining liquid assets were in Cayman Island bank accounts. Two of the directors of the funds resided in the Cayman Islands. The Funds' investors and creditors knew or should have known they were dealing with Cayman Island incorporated entities. Additionally, appellants argued that as Cayman Island incorporated companies, the Funds were subject to Cayman Island tax laws and were "required" to be wound up in the Cayman Islands. The Funds' pre-filing attorneys were in the Cayman Islands and the Funds' pre-filing auditors performed some auditing work in the Cayman Islands. *Id.* at 338. The court found that these facts were not sufficient to show "establishment" as they did not establish that the Funds had a "place of operations" that carried out "nontransitory economic activity" in the Cayman Islands. *Id.* "Auditing activities and preparation of incorporation papers performed by a third party do not in plain language terms constitute 'operations' or 'economic activity' by the Funds. Nor does the alleged review of insider transactions fall within the ordinary meaning of 'economic activity.'" *Id.* at 339.

Judge Robert D. Drain's *In re SPhinX* decision has been criticized for its failure to reach the same conclusion as the *In re Bear Stearns* decision. *See* Glosband, Daniel M. et al., *SPhinX Chapter 15 Opinion Misses the Mark*, AM. BANKR. INST. J. Vol. XXVI, No. 10, at 44 (Dec./Jan. 2007), available at www.abiworld.org. In *In re SPhinX, Ltd.*, the court held that a foreign proceeding was not a foreign main proceeding despite the presumption of COMI in the foreign locality where the company was registered. However, the *SPhinX* court proceeded to recognize the foreign proceeding as a foreign nonmain proceeding without any analysis of whether an "establishment" existed at all in the foreign locality. 351 B.R. at 117.

Critics suggest that *SPhinX* wrongfully makes recognition a separate step from the determination of whether a foreign main or nonmain proceeding exists. Glosband, *supra*, at 46. Supporters of the *Bear Stearns* approach explain that "[s]evering recognition from the application of the definitional requirements of foreign main proceedings and foreign non-main proceedings results in the court ignoring whether [the funds] are foreign proceedings eligible for chapter 15 recognition." *Id*. at 46. At the heart of this argument is that the *SPhinX* court determined that the debtor's COMI was in the United States. *SPhinX*, 351 B.R. at 119. The court did not then determine that an establishment existed in the Cayman Islands, and arguably, the facts did not support such a determination. *Id*. Therefore, the debtor could not establish that its foreign proceeding in the Cayman Islands was a foreign main OR a foreign nonmain proceeding by definition. A commentator explains that "[t]his should have ended the matter. The Cayman Islands proceeding, while a foreign proceeding, is not eligible for chapter 15 recognition at all." Glosband, *supra*, at 46.

Much like in *Bear Stearns*, shareholders authorized the liquidation of the Basis Yield fund under the laws of the Cayman Island and appointed JPLs. *In re Basis Yield Alpha Fund (Master)*, No. 07-12762 (REG), at *3 (Bankr. S.D.N.Y. Jan. 16, 2008) (slip op.), errata order (January 22, 2008). Further, just as the JPLs did in *Bear Stearns*, the Basis JPLs argued that "because Basis

Yield's registered office is in the Cayman Islands, the Cayman Islands is presumed to be the COMI, under Section 1516 of the Code . . . and that with no objections having been filed, there is no evidence to the contrary." *Id.* at *6. The court rejected the JPLs' arguments. Instead, the court explained that the JPLs had failed to put on any evidence that the Cayman Islands was the COMI of the Fund. *Id.* at *14. Although there was a presumption that the Cayman Islands was the COMI of the Fund, because the Fund's registered office was located in the Cayman Islands, the court determined that evidence existed that was contrary to the presumption, *id.* at *15-17, and, more importantly, that the court has the power to inquire into the facts surrounding a Chapter 15 debtor's COMI. *Id.* at *17. The court explained that courts are entitled to rely on the presumption in Section 1516 of the Bankruptcy Code, but are not required or bound to rely upon that presumption. *Id.* at *18-19. Finally, the court rejected any argument that failure to object by other parties-in-interest binds the court to the debtor's claim of entitlement to recognition. *Id.* at *19-22. In making its determination, the court also considered that as an "exempted limited liability company" under Cayman Island law, the debtor operated exclusively outside of the Cayman Islands; in this case, it operated in the United States.

One court recently has applied the *Bear Stearns* factors and recognized a foreign main proceeding over the objection of creditors. *In re Ernst & Young, Inc.*, 383 B.R. 773 (Bankr. D. Colo. 2008). In *Ernst & Young*, the Canadian court appointed Ernst & Young as the receiver of KDI and KD/CO and Ernst & Young filed a petition for recognition of foreign main proceeding in bankruptcy court in Colorado. The Securities Commissioner for the State of Colorado (the "Commissioner") argued that KD/CO perpetrated multi-national cross-border securities fraud, that the debtors' COMI was where the fraud occurred and because the investor money flowed through banks in the United States, the COMI was Colorado. *Id.* at 777-78. The court found that the persons who were the "driving force" behind KDI and KD/CO formed those companies in Canada, directed their operations of KDI and KD/CO from Canada and that the majority of the assets involved were in the name of or ultimately controlled by KDI in Canada. The court further found that the public policy exception in Chapter 15 was to be applied narrowly. *Id.* at 781. The court recognized the receivership proceeding as a foreign main proceeding. *Id.* at 782.[14]

Judge Lifland's analysis in *Bear Stearns* is consistent with the wording of the UNCITRAL Model Law, and the definitions of "foreign main" and "foreign non-main" proceedings in Chapter 15 track the Model Law. The question becomes whether that language creates a greater need for a debtor's connection to its place of filing than that which is imposed on domestic debtors.[15] In contrast to the venue decision in *Enron* (which is consistent with venue decisions

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[14] For more information on the cases discussed in this Section or to track new cases dealing with Chapter 15, visit www.chapter15.com/bin/chapter15_cases.

[15] It is interesting to note that the newly passed (but not yet in effect) Canadian amendments to the Bankruptcy and Insolvency Act and the Companies' Creditors Arrangement Act dealing with international insolvencies do not contain the "establishment" test for determining whether a foreign proceeding is a non-main proceeding. The Canadian statute tracks the definitions of the Model Law (and thus Chapter 15) as to the debtor's COMI being determinative of whether a foreign proceeding is a foreign main proceeding, but eliminates the establishment requirement from the foreign non-main proceeding definition. This may create different kinds of foreign non-main proceedings in Canada than anticipated by the Model Law or Chapter 15. Sarra, Janis, *Crossing the Finish Line: the Potential Impact on Business Rescue of Adoption of the new Cross-Border Insolvency*

in many other cases), where the Southern District of New York stated that the "debtor's choice of forum is entitled to great weight if proper," 274 B.R. 342, in both *SPhinX* and *Bear Stearns*, the Southern District of New York gave little weight to the debtor's choice of forum or the fact that the forum was proper for its own filing. While arguably the "establishment" requirement only limits the type of access the foreign representative gets to the courts of the United States, it does place a burden on Chapter 15 policy.

<u>European Courts and COMI</u>

It is academically interesting, in considering whether the *Bear Stearns* analysis makes sense in analyzing US venue and whether Congress should abandon domicile as a venue provision for domestic debtors in the United States, to look at the how the European Courts treat the registration presumption for determining a company's COMI. European Council Regulation No. 1346/2000 of 29 May 2000 (the "EU Regulation") is the regulation applicable to member states of the European Union governing recognition of insolvency proceedings opened in an EU member state. *In re Ran*, 390 B.R. 264. The EU Regulation provides, "The 'centre of main interests' should correspond to the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties.'" *Id.* at 265. The issue of what qualifies as an entity's COMI has been a contentious issue for European courts.[16] Primarily, courts have struggled with the question of how much weight they should give the presumption that a debtor's COMI is the location of the debtor's registered office.

Some courts have considered the location of the debtor's registered office important, despite evidence that could rebut the presumption. For example, in *In re Eurofood IFSC Ltd.*, the Irish High Court determined that Eurofoods, a subsidiary of the Parmalat Group, had its COMI in Ireland, notwithstanding the fact that the parent entity clearly had its COMI in Italy. [2004] BCC 383 (High Court (Ireland)), *aff'd by* [2005] I.L. Pr. 2 (Supreme Court (Ireland)). The court based its decision on the fact that the company was registered in Ireland, conducted the administration of its business interests in Ireland, and third-party creditors were under the belief that they were doing business with an Irish company. Parmalat argued that Eurofoods' COMI was in Italy, because Eurofoods was a wholly-owned subsidiary of Parmalat formed for the sole purpose of financing other members of the corporate family, company policy was determined in Italy, and the company had no employees in Ireland. The Irish courts rejected Parmalat's arguments; however, an Italian court disagreed with the findings of the Irish courts and determined that the debtor's COMI was in Italy. Tribunale Parma (February 30, 2004).

This jurisdictional dispute between the Italian and Irish courts was referred to the European Court of Justice (ECJ), and on September 27, 2005, an advocate-general of the ECJ agreed with the Irish courts, determining that where the subsidiary is located is the critical question, not where its parent company is located. Opinion of Advocate General Jacobs, Case C-341/04*,*

Provisions, Report to the Office of the Superintendent of Bankruptcy, 2007, available at <u>http://corporationscanada.ic.gc.ca/eic/site/bsf-osb.nsf/eng/h_br01667.html</u>.

[16] *See* Aaron M. Kaufman, *The European Union Goes Comi-tose: Hazards of Harmonizing Corporate Insolvency Laws in the Global Economy*, Houston. J. Int'l Law (Spring 2007) available at <u>http://www.entrepreneur.com/tradejournals/article/print/168283784.html.</u>

Eurofood IFSC Ltd. (September 27, 2005). The advocate general reasoned that "the fact of the parent company's control is not sufficient to rebut the presumption . . . that the centre of main interest of a subsidiary company is situated in the [location] where its registered office is to be found." *Id*. at ¶ 110.

In a May 2, 2006 ruling that has far-reaching implications for pan-European insolvencies, the ECJ agreed with the Irish courts and determined that the liquidation of Eurofood should be carried out under Irish law. According to the ECJ, when a debtor company carries out its business in the country where its registered office is located—as opposed to merely keeping a "letterbox" or post-office address for the company there—the fact that a parent company can or may control the debtor company from another country does not rebut the presumption that COMI lies where the debtor company's registered office is located. Judgment of the Court (Grand Chamber), Case C-341/04*, Eurofood IFSC Ltd.* (May 2, 2006).

Other courts have determined that the presumption that a debtor's COMI is the place of its registered office is not a particularly strong presumption. For example, in *Re Parkside Flexibes SA* (Ch.) (Combined Court, Quayside, Newcastle-upon Tyne), No. 75 (February 9, 2005), the court wrote that "there seems to be no reason to suppose that this presumption is a particularly strong one. It is rather, just one of the factors to be taken into account with the rest of the evidence which is before the court." *Id*. at ¶ 9. The court then proceeded to set forth what has been referred to as the "balance of probabilities test" to see if the presumption has been rebutted. The court asked itself "is [the company's COMI] more probably Poland or more probably England?" *Id*. at ¶ 32. After determining that the debtor's interests in both countries weighed equally, the court considered whether third parties would consider the debtor's COMI to be in England or Poland. *Id*. at ¶ 36. The court determined that while the evidence of where the debtor's interests were located weighed equally between Poland and England, the presumption was rebutted because third party creditors were likely to believe the debtor was centered in England. This approach seems to offer little, if any, weight to location of the registered office of the debtor. *Id*. Even the court expressed that this decision was reached "by the narrowest of margins." *Id*. at ¶ 37.

In *In Re BRAC Rent-A-Car Int'l*, High Court of Justice Chancery Division Companies Court, EWHC (Ch.) 128--0042/2003 (February 7, 2003), the court determined that the location of the registered office of the debtor was of little importance. The Court determined that although the company was registered in the United States, the COMI was in the United Kingdom. *Id*. at ¶ 31. The court based its decision on the fact that the company had been registered as a foreign company in the United Kingdom for many years and that the company's operations were almost completely run in the United Kingdom and almost all of its employees worked in the United Kingdom. *Id*. at ¶ 4.

In determining whether the presumption was rebutted, some courts have considered the effect the presumption would have on the interests of third parties. *In Re Daisytek-ISA Ltd*., [2003] BCC 562 (Chancery Division). In *Daisytek-ISA Ltd.*, a company was trading in the country in which it was registered but was, to a greater degree, controlled from a head office elsewhere. The court determined that the French and German subsidiaries of a United Kingdom company had their COMI in the United Kingdom. *Id*. at ¶ 14-18. The court reasoned that the majority of the

subsidiaries' creditors knew that the registered office of the parent company was the location of the most important functions for the subsidiaries. *Id.* The court wrote that "the most important 'third parties'. . . are the potential creditors." *Id.* at ¶ 16.

In *Skjevesland v. Geveran Trading Co. Ltd.*, [2003] BCC 209 (Chancery Division (Bankruptcy Ct)), [2003] BCC 391 (Chancery Division), the English courts emphasized that the most important considerations when determining a COMI were where the debtor conducted the administration of its business on a regular basis and where third-party creditors believed the debtor's COMI was located. The courts explained that the ability of creditors to ascertain where the debtor is located should be of primary importance to courts in determining the locations of a COMI.

An important difference between the EU Regulation applied by these European courts and Chapter 15 is that if the court of a EU member state determines that it has jurisdiction under the EU Regulation to open main insolvency proceedings at the debtor's COMI, that decision is not subject to reconsideration by the courts of any other EU member state and must be accepted as final. In contrast, Chapter 15 does not provide for recognition of an insolvency proceeding based on a foreign court's determination that it has jurisdiction based on the debtor's COMI. Instead, Chapter 15 requires the US court to make an independent evaluation of the location of the debtor's center of main interests at the time a petition for recognition is presented. *In re Ran*, 390 B.R. 267.

V. Conclusion

A domestic corporation in the United States can file a bankruptcy case in the district court in its domicile – its state of incorporation. This is a very low threshold to establish proper venue. In contrast, the recognition of a foreign main proceeding requires that the foreign representative demonstrate that the foreign debtor's insolvency proceedings were filed in a forum in which the debtor had its center of main interests. Although the statute specifically provides that there is a presumption that the country of registration of the foreign entity is its center of main interests, the presumption can be rebutted, and the Southern District of New York has determined that, even in the absence of objection, it should make an inquiry into further evidence of COMI, beyond evidence of registration, and that the evidence should demonstrate an establishment or a principal place of business.

This has created a double standard of sorts. While nothing requires that the recognition standards provisions of Chapter 15 be consistent with the Bankruptcy Code's general venue provisions, state of incorporation and country of registration are identical concepts. What's sauce for the goose, the United States domestic corporation, is not sauce for the gander, the foreign corporation. However, if the goal is to force a debtor that is really a United States business, despite its foreign domicile, to reorganize in the United States, the *Bear Stearns* line of cases is consistent with that goal. A US business with its domicile in the United States can establish proper venue based on the domicile. A US businesses with a foreign domicile will have to file bankruptcy in the United States or risk not having its foreign proceeding recognized in the US.