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NY Ruling Is A Ch. 15 Reminder For Practitioners Outside US

By **Rick Hyman and Gregory Plotko** (December 19, 2022, 3:23 PM EST)

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Chapter 15 of the U.S. Bankruptcy Code serves an important purpose in a global financial marketplace.

The chapter, enacted in 2005 as the U.S. version of the United Nations Commission on International Trade Law's Model Law on Cross-Border Insolvency, allows bankruptcy courts to cooperate and coordinate with insolvency proceedings located abroad.

Chapter 15 provides foreign debtors and their representatives wide-ranging relief and expansive rights, often greater than those that may be available in their local jurisdictions.

It is not unusual that a foreign debtor may have assets located in the U.S., U.S.-based creditors or other counterparties, and contractual relationships governed by U.S law.

In such instances, the imposition of the automatic stay to protect U.S. assets, access to Section 363 of the Bankruptcy Code to sell assets, and other features of the Bankruptcy Code have proven extremely valuable, providing an efficient mechanism to preserve assets and maximize value in conjunction with insolvency proceedings abroad.

Not all proceedings in foreign jurisdictions are eligible for Chapter 15, however. In order to be eligible, a proceeding must constitute a foreign proceeding under the Bankruptcy Code, among other things. The Bankruptcy Code defines a foreign proceeding as

> a collective judicial or administrative proceeding in a foreign country ... 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.[1]

More recently, foreign debtors have sought Chapter 15, in part, to conduct broad discovery that is often much wider in scope than may be available in the foreign debtors' home jurisdiction, indeed, perhaps reaching persons or entities that may not subject to the jurisdiction of foreign tribunals.

In particular, Bankruptcy Rule 2004 provides for wide-ranging discovery with respect to the debtor's affairs and is available to debtors in Chapter 15.

The joint provisional liquidators, or JPLs, of Global Cord Blood Corporation appointed by the Grand Court of the Cayman Islands seemingly had broad discovery in mind when they filed a Chapter 15 petition in the U.S. Bankruptcy Court for the Southern District of New York in In re: Global Cord Blood Corporation.[2]

The JPLs were appointed following allegations that the company's board and/or officers authorized wrongful expenditures of corporate funds. The order appointing the JPLs was issued in respect of Section 92(e) of the Cayman Islands Companies Act and, very generally directed them, among other things, to:

- Protect and preserve the company's assets;
- Investigate and report on the company's affairs; and
- Collect and retain the company's assets, and further barred proceedings against the company except with leave of court.

The order also authorized them to "commence winding up proceedings and/or any insolvency process in the Cayman Islands or any other country."[3] Section 92(a), however, does not require that a company be insolvent, and does not address the classification, adjustment or resolution of debts.

Bankruptcy courts have identified a number of elements that must be satisfied in order to be deemed a foreign proceeding eligible for Chapter 15. Three stand out:

- The proceeding must be collective in nature;
- The proceeding must be conducted under a law that relates to insolvency or debt adjustment; and
- The proceeding must be for the purpose of reorganization or liquidation.

A purported shareholder of Global Cord challenged the JPLs' request for recognition, arguing that the Cayman proceeding did not satisfy the criteria to be a foreign proceeding.[4] The bankruptcy court was methodical in its analysis and agreed with the objector on two of the three elements, described below.

Collective Proceeding

The essence of a collective proceeding is that it must address the interests of all creditors, rather than adjudicating the rights and obligations of individual creditors.

The bankruptcy court found that the Cayman proceeding did not focus on the creditor body but rather was implemented to address the challenged transaction.

The court pointed to the failure to so much as identify creditors or provide them actual notice of the proceeding, to quantify and classify the company's liabilities, or consider a methodology for making distributions.[5]

Reorganization or Liquidation Purpose

A foreign proceeding must have at its heart a reorganization or liquidation purpose.

The bankruptcy court found that, while the order appointing the JPLs authorized them to take certain actions that that would serve to preserve and collect estate assets, and take other actions that might benefit creditors, there was no evidence that their appointment was leading to a reorganization or liquidation — or that they had authority to do so.

Indeed, it pointed to other Cayman proceedings that had been granted Chapter 15 recognition on grounds that the company is or is likely to become unable to pay its debts, and "the company intends to present a compromise or arrangement to its creditors' or grants authority to enter into a compromise or arrangement" with creditors.[6]

With regard to the requirement that the proceeding be conducted under a law that relates to insolvency or debt adjustment, the bankruptcy court agreed. It concluded that, although not without question, the Cayman proceeding related to a law — the Companies Act — that itself relates to insolvency.[7]

According to the bankruptcy court, the Cayman proceeding was "most akin to a corporate governance and fraud remediation effort, and is not a collective proceeding for the purpose of dealing with insolvency, reorganization, or liquidation" and denied recognition.[8]

Recognition was denied without prejudice. If circumstances change, the JPLs may, after further orders from the Cayman Islands, return to the bankruptcy court to request recognition.

Conclusion

The case provides an important reminder for foreign practitioners contemplating relief under Chapter 15. Consideration should be given to the need or desire for a Chapter 15 ancillary proceeding prior to commencing any proceeding.

Does the debtor have assets in the U.S. that might be at risk of interference by creditors? Might the debtor be best able to maximize the value of any assets through an efficient 363 sale in a Chapter 15?

Will the debtor benefit from the recognition and enforcement of local orders over creditors and others located in the U.S.?

And, as in Global Cord, would expansive discovery under Rule 2004 serve to further investigations regarding wrongdoing or otherwise benefit creditors? These are only a few questions that practitioners should consider before commencing a proceeding abroad.

When a Chapter 15 proceeding can be anticipated, the relief requested from foreign courts should be tailored in a manner that maximizes the likelihood of recognition as a foreign proceeding.

While the definition is broadly construed by bankruptcy courts,[9] Global Cord shows that courts will carefully examine each element to ensure that Chapter 15 is not abused. Care must be taken to satisfy the more limiting criteria of foreign proceedings, noted above.

As a premise, orders appointing liquidators and administrators should also appoint them as foreign

representatives with authorization to commence a Chapter 15 proceeding. For those types of proceedings that do not have a history of acceptance in the U.S., it is not enough that similar proceedings from the same jurisdiction have been recognized.

In such instances, orders appointing liquidators and administrators might require notice to all creditors and provide mechanism for their participation in the proceeding — although such notice and participation may not be otherwise required.

This, perhaps combined with a directive to perform some analysis of creditor claims and to consider mechanisms for distributions if needed, might better position a foreign representative to argue that the local proceeding is collective in nature.

Satisfying the requirement that the proceeding has a reorganization or liquidation purpose may be more challenging if that is not the primary objective of the foreign proceeding. In such instances, orders might authorize alternative relief, expressly referring to statutory provisions that relate directly to insolvency or debt adjustment.

Orders might authorize provisional liquidators to consider, negotiate and, if needed, enter into restructuring agreements with creditors in the event that their primary task — investigations and asset recovery, for example — fails to identify and recover assets needed to pay creditors in full.

Importantly, mere authorization may not be sufficient, and foreign representatives should take some steps in furtherance of any such alternative relief in order to be best positioned to successfully commence a Chapter 15 case in the US.

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[1] 11 U.S.C. § 101(23).

[2] See In re Global Cord Blood Corporation, Case No. 22-11347 (December 5, 2022).

[3] See Id. at 9.

[4] See Id. at 1.

[5] See Id. at 16-21.

[6] See Id. at 22-30.

[7] See Id. at 21-22.

[8] See Id. at 2.

[9] see Id. at 14.