American Bankruptcy Institute

2017 International Insolvency & Restructuring Symposium

America Now!

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ABI International Insolvency Restructuring Symposium

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America Now!

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Introduction – Today's Program

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- Chapter 11 Overview and *China Fishery* Case Study
- Chapter 15 Overview and COMI Transfers
- Chapter 15 and Bankruptcy Code Section 109(a)
- Foreign Recognition and Comity
- International Reach of Avoidance Claims
- Modification of Foreign Stays

Panelists

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Chapter 11 Overview and *China Fishery* Case Study

Benefits of U.S. Bankruptcy Laws for Foreign Companies

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- Traditionally, international restructuring regimes are less likely to allow for the reorganization of a company.
  - Some foreign bankruptcy regimes presume liquidation.
  - Other foreign bankruptcy regimes provide significant powers to creditors, essentially ceding control over the bankruptcy process from the debtors.
- Accordingly, in recent years, more and more international companies have taken advantage of U.S. restructuring laws by filing for either Chapter 11 or Chapter 15 protections in the United States.

Overview of Chapter 11

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- Chapter 11 is one of the most well-developed laws of any insolvency regime in the world for helping troubled companies restructure.
- Advantages available to Chapter 11 debtors include:
  - the ability to confirm a plan with far less than unanimous stakeholder support, even if applicable credit agreements or indentures require unanimity to change fundamental economic terms like tenor and pricing
  - the ability to obtain debtor-in-possession financing on a superpriority basis
  - the ability to assume and assign or reject contracts or leases
  - the ability to sell substantially all of a debtors' assets free and clear of secured and unsecured claims, without the need to obtain shareholder or creditor approval, subject only to secured creditor rights to bid their debt for their collateral
- Chapter 11 is flexible and allows for reorganization plans that convert debt to equity, provide new capital or financing, or provide for the disposition of one or more business lines.

Confirmation of a Chapter 11 Plan

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- Confirming a Chapter 11 plan requires creditor consents, but holdouts cannot easily block confirmation.
- Creditors vote by class, with holders of similar claims generally placed in the same class.
  - However, the debtor, which starts a Chapter 11 case with the exclusive right to file a plan of reorganization, has significant flexibility in setting up classes.
  - For example, bank debt may be in one class (or more than one), senior bond debt in another, subordinated bond debt in yet another, etc.
- In order for a class to accept a plan, two-thirds in amount and greater than one-half in number of the class must vote for the plan.
  - Only parties that actually vote are counted, so the actual accepting percentages can be much lower.

Confirmation of a Chapter 11 Plan – Cram Down

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- Once a class votes to accept a Chapter 11 plan, that vote is binding on all members of the class, even if they abstained or rejected.
- However, even if a class votes to reject the plan, it can be "crammed" down on that class so long as certain requirements are satisfied, such as at least one class of creditors whose rights are impaired by the plan voting to "accept" the plan.
- In addition, the plan must satisfy the "cram down" tests:
  - the plan cannot "unfairly discriminate" against the rejecting class
  - the plan must be "fair and equitable" to the rejecting class—meaning that senior creditors are provided for in full (either in cash or otherwise) before more junior creditors recover.

International Case Study – China Fishery Group – Background and Chapter 11 Filing

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- The China Fishery Group case is a good example of a group of foreign companies with no real ties to the United States making use of Chapter 11's restructuring provisions.
- Background of China Fishery Group:
  - In the 1980s, the Ng family started a frozen seafood trading business in Hong Kong, which is now the twelfth largest fishing company in the world. The business also now owns several Peruvian fishing companies.
  - Due in part to the effects of El Nino on fishing, the Ng family in some instances and disgruntled creditors in other instances instituted insolvency proceedings all over the world in recent years including the BVI, Cayman Islands, Germany, Peru, Singapore and Hong Kong.
  - In June of 2016, facing a deadline under certain deeds of undertaking entered into with creditors that would have obligated the Ngs to move forward with a sale of the Peruvian fishing companies, the Ngs filed various of the China Fishery Group companies for Chapter 11 to take advantage of the automatic stay and avoid the sale.

International Case Study – China Fishery Group – Appointment of Chapter 11 Trustee

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- Following the Chapter 11 filings, certain creditors filed a motion to appoint a Chapter 11 trustee, asserting:
  - a lack confidence in management's ability to protect creditor interests rather than the interests of the Ng family who controls the Chapter 11 debtors and also act as directors at the various debtors; and
  - a likely conflict between the Ng family's interests and the Chapter 11 debtors' interests due to the extensive intercompany debts between the various debtor entities and non-debtor entities, which are controlled by the same or similar management.
- Rather than appointing the Chapter 11 trustee at all entities, Judge Garrity appointed a trustee only at CFG Peru Singapore, which is the direct or indirect parent of the Peruvian fishing companies—where all the value lies for the entire China Fishery Group.
- This was likely to encourage the Trustee to work with the Ng family to come to a resolution in these cases. The Peruvian Opcos are not Chapter 11 debtors.

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Chapter 15 Overview and COMI Transfers

Overview of Chapter 15 and COMI

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- Chapter 15 was added to the Bankruptcy Code in 2005 and incorporates the Model Law on Cross-Border Insolvency to encourage cooperation between the United States and foreign countries with respect to transnational insolvency cases.
- Chapter 15 allows a "foreign representative" of a debtor that has commenced an insolvency proceeding abroad, where the debtor has the center of its main interests, or COMI, to obtain recognition of such proceeding as either a foreign main proceeding or a foreign non-main proceeding in the U.S.
  - Greater relief is available to a foreign representative of a foreign main proceeding than for a representative of a foreign non-main proceeding.
- Bankruptcy Code section 1516(c) provides that, in the absence of evidence to the contrary, a debtor's registered office or habitual residence "is presumed to be the center of the debtor's main interests."
- COMI is determined as of the filing date of the Chapter 15 petition, without regard to the debtor's historic operational activity.

Transferring COMI – *In re Ocean Rig UDW Inc.* – Background

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- In *In re Ocean Rig UDW Inc.,* No. 17-10736 (MG) (Bankr. S.D.N.Y. Aug. 24, 2017), until sometime in 2016, each of the foreign debtors operated as an international offshore oil drilling contractor, owner, and operator of drilling rigs and each had its COMI in the Republic of the Marshall Islands.
- The Marshall Islands does not have a statute or any procedures permitting reorganization, making liquidation the likely outcome to the company's mounting debt crisis.
- Because the Cayman Islands does have statutory laws and procedures that permit restructuring, the foreign debtors sought to shift their COMI to that jurisdiction prior to filing under Chapter 15.

Transferring COMI – *In re Ocean Rig UDW Inc.* – Transfer Mechanics

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- The court held that COMI was properly transferred because the debtors:
  - conducted their management and operations in the Cayman Islands,
  - maintained offices in the Cayman Islands
  - held their board meetings in the Cayman Islands
  - had officers with residences in the Cayman Islands
  - opened bank accounts in the Cayman Islands
  - maintained their books and records in the Cayman Islands
  - conducted restructuring activities from the Cayman Islands
  - provided notices of relocation to the Cayman Islands to paying agents, indenture trustees, administrative and collateral agents, and investment service providers
  - filed a Form 6-K with the SEC showing that their office was in the Cayman Islands.

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Chapter 15 and Bankruptcy Code Section 109(a)

Overview of Bankruptcy Code section 109(a) and Division of Authority Regarding Chapter 15 Applicability

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- Bankruptcy Code section 109(a) governs who may be a debtor under the Bankruptcy Code by requiring a debtor to have a domicile or certain assets in the U.S. to be eligible for relief under the Bankruptcy Code.
- But does section 109(a) apply in a Chapter 15 case?
- A division of authority has arisen between the Second Circuit and a Delaware bankruptcy court with respect to the application of Bankruptcy Code section 109(a) in the Chapter 15 context.
  - The Second Circuit has held that section 109(a) does apply in a Chapter 15 case.
  - Conversely, at least one Delaware bankruptcy court has found that the section 109(a) requirements do not apply to a Chapter 15 debtor.

Section 109(a) in the Chapter 15 Context – *In re Barnet* and *In re Bemarmara Consulting*

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- In *In re Barnet*, 737 F.3d 238 (2d Cir. 2013) the Second Circuit held that the requirements of section 109(a) do apply in Chapter 15 proceedings because Bankruptcy Code section 109 is within Chapter 1 of the Bankruptcy Code, which applies in a case under Chapter 15
- However, in *In re Bemarmara Consulting, A.S.*, No. 13-13037 (Bankr. D. Del. Dec. 17, 2013) the Delaware bankruptcy court held that section 109(a) is irrelevant to the determination of whether a foreign debtor's proceedings should be granted recognition under the Bankruptcy Code, and that granting recognition is mandatory unless doing so is contrary to U.S. public policy.
  - In support of its decision, the court emphasized that section 109(a) describes who may be a "debtor" under the Bankruptcy Code, not who may be a "foreign representative."

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Foreign Recognition and Comity

Chapter 15 Recognition and Corruption in Foreign Insolvency Proceeding

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- What evidence of corruption in a foreign insolvency proceeding is sufficient to block Chapter 15 recognition?
- In *In re Sergey Petrovich Poymanov*, No. 17-10516 (Bankr. S.D.N.Y. July 31, 2017), counsel for Delaware company PPF Management LLC challenged the recognition of the Russian bankruptcy proceedings of Sergey Poymanov, who was using PPF to preserve his claims of corporate raiding.
- Though PPF alleged widespread corruption in the Russian judicial system, it was not able to provide evidence that Poymanov's specific insolvency proceeding had been tainted.
- The court stated that the bar to block Chapter 15 recognition is quite high, explaining that PPF would have to show that such an order would be manifestly contrary to the public policy of the United States. In order to do so, PPF needed to have offered evidence of corruption in the current case, rather than solely alleging that corruption exists in the Russian judiciary generally.

Collateral Estoppel without Chapter 15 Recognition

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- Is it proper for a U.S. court to recognize a foreign insolvency court's factual findings when no Chapter 15 case has been filed?
- In *Trikona Advisers Ltd. v. Chugh*, 846 F.3d 22 (2d Cir. 2017), the Second Circuit affirmed a district court ruling giving collateral estoppel effect to the findings of a foreign insolvency court, even though no Chapter 15 petition had been filed in the U.S. on behalf of the foreign debtor seeking recognition of its Cayman Islands winding-up proceeding.
- According to the Second Circuit, because the party seeking such relief was not a "foreign representative" under Chapter 15, the provisions of Chapter 15 simply did not apply, but the district court nonetheless did not err in granting comity to the foreign insolvency court's factual findings.

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International Reach of Avoidance Claims

Overview of Avoidance Powers provided in the Bankruptcy Code

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- The Bankruptcy Code provides a debtor certain “avoidance powers” to recover property transferred by the debtor to third parties before the petition date.
- Generally, these avoidance actions fall into two categories:
  - the transfers had the effect of preferring one creditor over others;
  - or the transfers were made for the purpose of hindering, delaying or defrauding creditors from collecting on their claims.
- But do such provisions apply to a transfer that occurred outside of the U.S. to a foreign transferee?
- A division of authority arises in this context, as Delaware bankruptcy courts have held that the Bankruptcy Code’s avoidance powers apply to international transfers, whereas New York bankruptcy courts have held that such powers do not have an international reach.

International Reach of Avoidance Powers – *In re FAH Liquidating Corp.*

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- In *In re FAH Liquidating Corp.,* No. 13-13087(KG), 2017 WL 2559892 (Bankr. D. Del. June 13, 2017) the Delaware bankruptcy court held that that avoidance claims under section 548 of the Bankruptcy Code apply to fraudulent transfers made outside the United States.
  - In so holding, the court concluded that the avoidance provisions in Bankruptcy Code section 548 apply to property everywhere in the world because any property recovered by a debtor or trustee becomes property of the estate under Bankruptcy Code section 541, and the debtor's estate should have access to its property regardless of its location.
  - This holding is in line with Fourth Circuit precedent as well as certain S.D.N.Y. decisions.

International Reach of Avoidance Powers – *In re Ampal-Am. Israel Corp.*

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- Conversely, in *In re Ampal-Am. Israel Corp.*, 562 B.R. 601 (Bankr. S.D.N.Y. 2017) the New York bankruptcy court, disagreeing with courts both within and outside its own district, ruled that the avoidance provisions of the Bankruptcy Code do not apply outside the U.S. because.
  - The court reasoned that, based on the language and context of the applicable provisions in the Bankruptcy Code, Congress did not intend for them to apply extraterritorially.
  - Specifically, the court noted that a presumption exists that Congressional legislation is intended to apply only within the territorial jurisdiction of the U.S., and that clear evidence is required to overcome this "presumption against extraterritoriality."

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Modification of Foreign Stays

Modification of Foreign Stays – Background of *In re Sanjel (USA) Inc.*

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- May a U.S. bankruptcy court properly modify a stay that has been entered in a foreign insolvency proceeding through a Chapter 15 recognition order? Should such relief be instead requested in the foreign court?
- Facts of *In re Sanjel (USA) Inc.*, No. 16-50778 (CAG) (Bankr. W.D. Tex. July 29, 2016):
  - The Canadian court in the foreign insolvency proceeding approved a broad stay which shielded the debtor's directors and officers from litigation.
  - In the Chapter 15 case that followed, the U.S. bankruptcy court entered a recognition order that enforced the broad Canadian stay of litigation against the debtor's directors and officers, which is not generally within the scope of the automatic stay under the Bankruptcy Code.
  - Critically, this recognition order would have forever barred certain of the debtor's U.S. employees who sought to bring actions against the debtor's directors and officers for unpaid wages.

Modification of Foreign Stays – Holding of *In re Sanjel (USA) Inc.*

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- The bankruptcy court in *In re Sanjel* held that Bankruptcy Code section 1522(a) permits a U.S. bankruptcy court to modify a recognition order in order to narrow the stay enforced therein, provided that "the interests of the creditors and other interested entities, including the debtor, are sufficiently protected."
  - The court undertook an analysis of the balance of hardships; if such balance lay with the creditors seeking relief, then the recognition order (and the underlying stay) could be modified.
  - Here, the court held that the hardships of the movants outweighed those of the debtor, and therefore modified the recognition order to limit the Canadian stay in the United States, thus allowing the employees to pursue their claims against the directors and officers.
  - As part of this holding, the court emphasized that it would be unduly burdensome to require the employees to seek relief from the stay in the Canadian court where the claims they sought to assert were fully based on statutory rights created by United States law to protect employees within the United States.

Thank you to our
panelists and audience!

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Skadden, Arps, Slate, Meagher & Flom LLP and Affiliates