Chapter 15 Bankruptcy – A Powerful Tool for Cross-Border Distressed Entities

Under Chapter 11 of the United States Bankruptcy Code, 11 U.S.C. section 101, et seq, a person or a commercial business may file a petition seeking the protections of the Bankruptcy Code with the idea of proposing a plan of reorganization. In the past many years, the plan of reorganization is often a plan of liquidation. General trends of globalization have impacted international business and more companies are finding themselves involved in multiple jurisdictions internationally. Distressed international business has led to a need to recognize that insolvency proceedings may also be international. Thus, Congress enacted the Bankruptcy Abuse Prevention and Consumer Protection Act in 2005, adding Chapter 15 to the Bankruptcy Code.

Chapter 15 of the Bankruptcy Code is based on the United Nations Commission on International Trade Law ("UNCITRAL") Model Law on Cross-Border Insolvency, and was designed to efficiently help international businesses.

The UNCITRAL Model Law has five main objectives: (1) promote cooperation between the United States court and parties of interest and the courts and other competent authorities of foreign countries involved in cross-border insolvency cases; (2) establish greater legal certainty for trade and investment; (3) provide for fair and efficient administration of cross-border insolvencies that protects the interests of all creditors and other interested entities, including the debtor; (4) afford protection and maximization of the value of the debtor's assets; and (5) facilitate the rescue of financial troubled businesses, thereby protecting investment and preserving employment.

Chapter 15 is written in anticipation of the insolvency proceeding being initiated outside the United States. Once the debtor initiates a foreign proceeding, the debtor, through a "Foreign Representative" files a Chapter 15 petition in the United States for recognition of the foreign proceeding.

After notice and a hearing, the court determines if the foreign proceeding will be recognized in the United States. A foreign proceeding may be recognized in one of two forms – a "foreign main proceeding" or a "foreign non-main proceeding." A foreign "main" proceeding is a proceeding pending in the country of the debtor's center of main interest ("COMI"). A foreign "non-main" proceeding is a proceeding pending in a country where the debtor has an "establishment" that is not home to the debtor's COMI.

Courts continually have been tasked with determining if a foreign proceeding is located within the debtor's "COMI" or if the debtor only maintains an "establishment" in the country. Absent evidence to the contrary, a debtor's "COMI" is presumed to be the location of the debtor's registered office. Generally, when determining a debtor's "COMI," a court bases its decision on evidence as of the time the Chapter 15 petition was filed. However, to help offset "COMI" manipulation, a court may look at the debtor's actions during the period in between the initiation of the foreign proceeding and the filing of the Chapter 15 petition.

A foreign proceeding will be recognized as “non-main” if the proceeding is filed in a country where the debtor has an “establishment,” but it is not home to the debtor’s “COMI.” Under Chapter 15, “establishment” means any place of operations where the debtor carries out non-transitory economic activity. If the foreign proceeding is found not to be located within the debtor’s “COMI,” nor is there evidence of an “establishment,” a court may deny recognition entirely.

The distinction between recognition as “main” or “non-main” is important. A Foreign “main” proceeding debtor’s American bankruptcy estate is entitled to certain protections under the Bankruptcy Code. As an example, immediately upon recognition as a foreign “main” proceeding, the automatic stay is implemented, preventing creditors from acting against a debtor’s assets. However, if the foreign proceeding is recognized as “non-main,” a Foreign Representative must request the court to invoke the automatic stay. Another example of relief immediately offered in a foreign “main” proceeding is the ability to invoke Bankruptcy Code Section 363, allowing a debtor to use, sell or lease property outside the ordinary course of business.

Chapter 15 instructs courts to adhere to the cooperative principles of comity, so long as there is no violation of United States public policy. The U.S. Supreme Court has defined comity as “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 convenience, and to the rights of its own citizens, or of other persons who are under the protection of its laws.”

A court’s duty to strive for comity makes Chapter 15 a powerful tool in cross-border insolvencies. Chapter 15 allows debtors to take advantage of two potentially very different insolvency regimes, and under certain circumstances Foreign Representatives may be granted relief available under foreign law that would generally be impermissible under the Bankruptcy Code.

The case *In re Petroforte Brasilerio de Petroleo Ltda.*, 542 B.R. 899 (Bankr. S.D. Fla. 2015), offers an illustration of a United States court applying foreign law traditionally not available to Chapter 11 debtors. In *Petroforte*, the U.S. Bankruptcy Court for the Southern District of Florida granted Petroforte’s Brazilian bankruptcy proceeding recognition as a foreign “main” proceeding, and extended recognition not only to the debtor, but to third parties involved in a transaction deemed to be in large part responsible for the insolvency. *Petrofort,*, 542 B.R. at 902.

Under Brazilian law, a trustee may pierce the corporate veil of third parties if it is demonstrated that those parties intended to defraud creditors. Under United States law, a trustee has far less expansive veil-piercing power. Nonetheless, the court held that even though the third parties were brought into the Chapter 15 proceeding under “different procedures” from that of the Bankruptcy Code, the use of the Brazilian veil-piercing powers was not contrary to United States public policy. *Petroforte*, 542 B.R. at 903.

Chapter 15 has established itself as a viable alternative for cross-border insolvency issues. A distressed cross-border entity should speak with a professional to determine if Chapter 15 is the correct option for their business.

Sugar Felsenthal Grais & Hammer LLP's insolvency and commercial law work often involves cross-border issues and transactions, particularly with regard to Poland and Israel.

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