

A new Chapter 15: changes proposed to the US Bankruptcy Code

By Kyriaki Karadelis, Friday 5 February



A group of leading cross-border insolvency and restructuring practitioners from the US have written an open letter to Congress, requesting amendments to Chapter 15 of the US Bankruptcy Code.

The National Bankruptcy Conference (NBC), a 60-strong group of senior US bankruptcy judges, professors and practitioners, issued the letter on 27 January.

Signed by the NBC's chair, **Richard Levin**, co-head of the restructuring and bankruptcy department at Jenner & Block in New York, the letter details 11 "necessary or desirable" revisions to Chapter 15 that the group says will help it better fulfil its purpose and function as the US's embodiment of the UNCITRAL Model Law on Cross-Border Insolvency.

Chapter 15 provides the mechanisms for dealing with cross-border insolvencies in the US. It gives US courts the power to recognise the foreign representative and foreign proceedings of a debtor in liquidation or in restructuring outside of the country and allows them to grant preliminary relief. It also allows US courts to authorise a trustee or other entity to act in a foreign country on behalf of a US bankruptcy estate.

The NBC writes that the changes should help reduce litigation, enable Chapter 15 to "be interpreted in light of its international origin", and bring it more in line with the Model Law and other statutes adopted in the 40 other countries where the Model Law has been enacted.

The 24-page letter is addressed to Tom Marino and Hank Johnson, chairman and ranking member respectively of the US House of Representatives' subcommittee on regulatory reform, commercial and antitrust law, and to Chuck Grassley and Patrick Leahy, chairman and ranking member of the Senate's committee on the judiciary.

As well as revisions to the US Bankruptcy Code – Title 11 of the US Code – it also stipulates changes to other sections of US law that relate to cross-border bankruptcy proceedings and Chapter 15.

The amendments

Among the proposed amendments is the stipulation that debtor-eligibility requirements do not apply to Chapter 15 cases. This comes in the form of a new clause for section 109(a) of the Bankruptcy Code, which exempts cross-border cases from the rule that only a person residing, or having a domicile in a place of business or property in the US, may be a debtor under Title 11.

The NBC says the additional clause will prevent courts from making the "same mistake" as the Second Circuit Court of Appeals did in the 2013 case *Drawbridge Special Opportunities Fund v Barnet*. In that "wrong" decision, the appeals court remanded a case back to the bankruptcy court on the grounds that the foreign representative had failed to prove the debtor satisfied the eligibility requirements in section 109(a).

"After the Barnet decision, the section 109(a) requirement has been regularly satisfied by the transfer of a small amount of the foreign debtor's property to the United States, usually the establishment of a funded retainer account, as an incidental step in the commencement of a Chapter 15 case," the letter notes.

However, this type of “contrived” property transfer has exposed petitions for recognition under Chapter 15 to the potential challenge that they were not filed in good faith, or that they are manifestly contrary to public policy. It also “inadvertently invites venue shopping” based on newly minted principal assets, the letter notes.

Another of the NBC’s proposed amendments serves to clarify section 1334(c) of Title 28 of the United States Code, which governs the judiciary and judicial procedures in regards to bankruptcy cases and proceedings.

The revision aims to make it clear that while courts cannot abstain from making a decision on whether to grant recognition to a foreign proceeding, they can, after granting recognition, abstain from further ruling on any matters arising under Chapter 15 or in a Chapter 15 case.

This clarifies *In re British American Insurance Company*, a 2013 decision from the US District Court for the Southern District of Florida, in which the court went beyond the intention of the statute, according to the NBC, to find that it could not abstain from deciding claims of breach of fiduciary duty against British American’s directors, after its initial recognition of the Bahamian insurance company’s liquidation proceedings in St Vincent and the Grenadines.

The NBC says that the court’s interpretation of section 1334(c) in *British American* was “plausible” given the present wording of the statute, and unsurprisingly led to other courts making similar rulings in 2015 in *Firefighters Retirement Systems v Citgo Group* and *In re Hellas Telecommunications*.

The revision should limit section 1334(c) to its “original, narrowly-intended purpose”, the letter says.

Other changes recommended by the NBC include clarifications to section 1502 of the Bankruptcy Code that a debtor’s centre of main interests (COMI) should be determined as of the date that the foreign proceeding was commenced, not the date the Chapter 15 petition was filed.

The NBC also advocates the insertion of an explicit provision in section 1523(a) that the look-back period for avoidance actions – actions to reverse transactions entered into by the debtor before it became bankrupt, brought under US law or on behalf of a foreign representative, should be measured from the date of the filing of the foreign insolvency or restructuring proceeding, not the US case.

Thoughts from the NBC

“A couple of the amendments will eliminate the effects of court decisions that we think distort the intent of the law and have the potential to negatively affect the treatment of foreign proceedings,” says Goodwin Procter of counsel **Daniel Glosband** in Boston, who assisted Congress in enacting the original Chapter 15, and who was the International Bar Association’s lead delegate to the UNCITRAL working group that drafted the Model Law.

Glosband says the clarification of the date at which a debtor’s COMI should be measured has the greatest power to change the landscape for Chapter 15 recognition in future.

“The UNCITRAL position is that COMI should be measured as of the date of commencement of the foreign proceeding. This differs from a line of US decisions that measure COMI as of the date that the Chapter 15 petition was filed,” he explains.

“Consistent with the legislative history of Chapter 15 where congress tried to follow the Model Law as closely as possible, the NBC has concluded that it should follow the UNCITRAL position on COMI measurement date. Since adoption of this amendment will reverse the decisions of two judicial circuits, it could change the landscape for foreign proceedings of debtors whose insolvency proceedings are taking place in countries where they did not have a place of business,” he notes.

GRR editorial board member **Don Bernstein**, head of the insolvency and restructuring practice at Davis Polk & Wardwell in New York and a conferee of the NBC, says the time was ripe for change given the upswing in the volume of international insolvency cases since the 2008 financial crisis – and the number of recent court decisions highlighting the need to clarify parts of Chapter 15.

“The decision of the Second Circuit Court of Appeals in *Barnet* applying section 109 to Chapter 15 cases was controversial and, as the NBC notes in its letter, probably wrong,” Bernstein says, describing that amendment as one of the most significant proposed. “I would hope these changes would be viewed as uncontroversial improvements that could be addressed promptly by Congress.”

Canadian practitioner and NBC conferee **Bruce Leonard**, head of the restructuring and insolvency group at Miller Thomson in Toronto and also a member of the **GRR** editorial board, says the NBC’s review of Chapter 15 has been under way almost from the time the law was enacted in 2005.

The proposed revisions will not change the Chapter dramatically, but they will improve its operation and structure, he notes.

In the future, Leonard says he would like to see more refinements to Chapter 15 directed to the problem of corporate group insolvencies. "There still isn't much court-to-court coordination in multinational cases except between Canada and the US, and it would be interesting and constructive to UNCITRAL to make some improvements that would facilitate the restructurings of global corporate groups – a topic on which they are working," he tells *GRR*.

Leonard, who sits on the executive committee of the International Insolvency Institute (III), says there have been important improvements in court-to-court communications, not least because of a set of guidelines the III promulgated with the American Law Institute (ALI) at the start of the millennium.

"The advantages in practice have been too profound to ignore," he says. "But many countries still feel uncomfortable with those kinds of communications; notwithstanding the III and ALI efforts and the provisions in the Model Law that require courts to cooperate with each other to the maximum extent possible."

Further amendments aside, Leonard warns that it may be some time before the NBC's proposed changes make it into Chapter 15. "Unfortunately, it's an election year in the US so there is a rush to pass legislation and a lot of bills will die on the order paper when Congress prorogues," he says, noting that the original version of Chapter 15 was passed by the House or the Senate on a total of eight occasions, but never at the same time – meaning the process had to be started over and over again.

"First we need a bill, which I don't think we have yet, and then we need both Houses of Congress to enact the same version after consideration in their respective committees. It may happen faster than the initial legislation in 2005, but the odds are against it," Leonard says.

The NBC has provided advice on bankruptcy legislation to Congress for nearly 80 years, since the Great Depression of the 1930s. It says in the letter that it would welcome an opportunity to discuss the amendments with the congressmen.

An international aspects committee within the conference has been following case law developments to Chapter 15. It was this committee that proposed the amendments, which were approved by the conference over a number of years since 2010.

The NBC's drafting committee reviews all approved amendments before they are put to congress. Levin, Glosband and the drafting committee chair, **Alan Resnick**, a professor of bankruptcy law at Hofstra University in New York, agreed on the final language of the Chapter 15 amends before they were reproduced in the letter.

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