

# **NATIONAL BANKRUPTCY CONFERENCE**

***Report of the Committee on International Aspects***

**2016 Annual Meeting**

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Last year the Committee on International Aspects submitted to the Conference, and the Conference approved, a letter suggesting specific amendments to clarify and augment chapter 15, the U.S. adoption of the UNCITRAL Model Law on Cross-Border Insolvency. The letter was conveyed to Congress, but there has not been any substantive response. We believe that we should follow up on the suggestions made but not propose any further amendments at this time.

Instead our report this year is on two Model Laws which UNCITRAL Working Group V on Insolvency Law has been drafting and which appear to be coming to a conclusion. Both laws will, if adopted, have an impact on insolvency law worldwide, and we solicit comments from members of the Conference on the drafts. One of the draft laws is on the Recognition and Enforcement of Insolvency-Related Judgments and the other is on the Cross-Border Insolvency of Multinational Enterprise Groups. Both have been framed as stand-alone laws, and therefore include many provisions that are already part of the Model Law – and Chapter 15. Both could be reformulated as much simpler amendments to the Model Law, or Chapter 15 as the case may be, but the sense of the Working Group has been to draft comprehensive documents that could be adopted by countries that have so far failed to adopt the Model Law.

The draft Model Law on the Enforcement of Insolvency-Related Judgments is further along and will be described first. After another round of discussion and drafting at the meeting of the Working Group in December in Vienna, the pending draft could conceivably be completed at the Working Group's meeting in New York

next May, and then sent to the UNCITRAL Commission for formal adoption. The U.S. and other nations will then be in a position to consider adoption of the provisions.

The most current available drafts of the Model Laws are attached hereto. They will be further revised at the meeting of Working Group V from December 12-16, 2016.

#### Draft Model Law on Recognition and Enforcement of Insolvency-Related Judgments

The immediate impetus for the drafting of a Model Law on Insolvency-Related Judgments was the decision of the UK Supreme Court in *Rubin v. Eurofiance, S.A.*, [2012] UKSC 46. There the UK Supreme Court held that a default judgment by a U.S. Bankruptcy Court in an avoidance case could not be enforced against an English defendant who had not specifically appeared in the U.S. case but could only be pursued in a new, plenary action against the defendant. A narrow holding of the decision was that the English version of the Model Law (which is the same for these purposes as the U.S. version) does not provide for the enforcement of bankruptcy avoidance judgments and that such judgments can be enforced only in accordance with general judgment enforcement principles applicable in England (which generally refuses to enforce foreign default judgments).

However, the English Court went further and, among other things, described the Model Law as essentially procedural, and subsequent U.K. decisions, ostensibly building on *Rubin*, have held that the Model Law does not, for example, provide for

the enforcement in England of relief available in a foreign insolvency case where English law would not provide such relief, at least where the contract at issue was governed by English law. One English decision focused on the wording of Article 21 of the Model Law, section 1521 of Chapter 15, which lists several examples of forms of relief available in a Model Law case and concludes with “granting any additional relief that may be available to” a local trustee. Although the section provides for any “appropriate relief, including ....” the English courts to date have narrowly construed its provisions and limited the relief available. The courts of at least one other jurisdiction, Korea, have held that the Model Law does not authorize recognition of a bankruptcy discharge granted by a foreign nation. The U.S. construction has been broader and more open to the enforcement of foreign insolvency laws, although there is no appellate case on point so far. See, e.g, *In re Rede Energia, S.A.*, 515 BR/ 69 (Bankr. S.D.N.Y. 2014).

In light of the conflict in decisions, the draft of the Model Law on the Enforcement of Insolvency-Related Judgments is designed to provide for enforcement of both a judgment against an individual defendant (for example, in a turnover or avoidance action), and a judgment that we would ordinarily describe as a confirmation order or decree providing for a general bankruptcy discharge. This is incorporated in the definition of “insolvency-related judgment” in Article 2(e), which includes a confirmation order or liquidation decree and a bankruptcy discharge (see Article 2(e)(v)). On the other hand, the definition of “insolvency-related judgment” is not unlimited. For example, it is still not agreed whether it will cover turnover or contract actions brought by an estate representative where

the debtor is pursuing rights held by the pre-bankruptcy estate, or whether it will be restricted to actions that accrue after the filing of the bankruptcy petition. Some of the European countries want to limit the scope of the provision (see Article 2(e)(iv)), apparently based on provisions of the European Insolvency Regulation; the U.S and other common law countries have opposed that limitation.

The definitions in Article 2 of “foreign proceeding” and “foreign representative” are substantially similar to those in the Model Law. Article 3 is also substantially the same as Article 3 of the Model Law; the alternative wording used in the provision numbered Article 3 *bis* is the handiwork of the representative of the EU, who would have this law not apply to any judgment covered by the Hague Convention on the Enforcement of Judgments, whether or not the nation enforcing the foreign judgment had actually adopted the Hague Convention. Several delegations, including the United States, have rejected that limitation, although there is no dispute that the current draft is intended to be generally congruent with the Hague Convention, without any overlap or gaps. The Hague Convention has a broad (and ill-defined) exception for matters related to insolvency, which, simply stated, this law is intended to fill.

Articles 4 and 5 of the current draft are self-explanatory,. Articles 6, 7 and 8 are substantially identical to Articles 7, 6 and 8 of the Model Law, except that the “public policy” exception in Article 7 of this draft includes a reference to “the fundamental principles of procedural fairness of this State.” The draft returns to this issue in Article 12 (see below).

Article 9 provides in substance that a judgment is enforceable under this draft only if enforceable in the state where it was rendered; thus a judgment on appeal can be recognized and enforced only if the originating state would enforce it pending appeal. Articles 10 and 11 are substantially self-explanatory and are generally analogous to Article 15 of the Model Law (section 1515 of Chapter 15). Recognition and enforcement are intended to be easy and straightforward in principle, although subject to the provisions of Article 12, entitled “Grounds to refuse recognition and enforcement ....” This section, one of the key provisions of the law, contains what we would call the “due process” objections to enforcement. Sections 12(a) through (d) are generally familiar. Article 12(e) is designed to preserve the primacy of the court with jurisdiction over the insolvency proceeding where the judgment originated. Article 12(f) is another restriction on enforcement; in my personal opinion, it still needs careful consideration. Subsection (iv) is designed to apply to judgments against directors of a debtor who are sued on claims of breach of fiduciary duty or misfeasance.

Article 12(g) applies only to judgments in the nature of confirmation orders and discharges and is designed to make applicable the fundamental protection of the Model Law (and Chapter 15) that any relief must adequately (or in the U.S. version, sufficiently) protect the interests of creditors and other interested persons, including the debtor. Finally, Article 12(h) incorporates in this draft the provisions of the Model Law and Chapter 15 regarding recognition only of main and nonmain proceedings, except that a judgment relating to the recovery of assets of the debtor could be enforced even though the existence of assets in a jurisdiction is not,

standing alone, sufficient to support either a main or a nonmain proceeding under the restrictions of the current Model Law (and Chapter 15).

Articles 13 and 14 are generally self-explanatory and similar to provisions in the Hague Convention. Article 15 provides for provisional relief pending an order of recognition and enforcement.

### Draft Model Law on Facilitating the Cross-Border Insolvency of Multinational Enterprise Groups

The draft of a Model Law to facilitate the Insolvency of Multinational Enterprise Groups is not as far along as the draft on judgment enforcement but its principal provisions seem to be in place. The current Model Law – and Chapter 15 – apply only to the insolvency of individual entities and do not have provisions that explicitly provide for group insolvencies, although it has been argued that the cooperation provisions of the law requiring coordination and cooperation between and among estates apply to members of corporate groups in insolvency proceedings in separate nations.

Like the judgment enforcement draft, the Model Law on Group Insolvencies is drafted as a stand-alone law, rather than an amendment to the existing Model Law, but it obviously designed to augment the Model Law, and it repeats many of the Model Law provisions. It may be questioned whether, assuming it is presented to Congress for adoption, it should be framed as a new law or reconstituted as an amendment to Chapter 15. The current draft has obviously been influenced by the

amendments to the European Union Insolvency Regulation, which were adopted last year and go into effect in 2017. These amendments, among other things, provide for a group insolvency proceeding that has authority to develop a group solution but must ordinarily seek recognition and ratification from the court with jurisdiction over the local proceeding of a group member.

Unlike the current Model Law, the enterprise insolvency draft contains many provisions that deal not only with recognition and relief granted to a foreign representative, provisions that in effect provide for U.S. enforcement of foreign insolvencies, but also provisions that would apply in a domestic insolvency proceeding, when the U.S. would be the home venue for a “group proceeding.” Section 103(k) of the Bankruptcy Code currently provides that most of the provisions of Chapter 15 apply only in a case under that chapter, although there are a few exceptions. If the group enterprise law is adopted, many more of its provisions would have to apply in chapter 7 and chapter 11 cases because they provide, in effect, that a debtor in a plenary chapter 7 or 11 case in the U.S. may act as a “group representative” in a cross-border “planning proceeding” that attempts to coordinate the insolvency proceedings of “enterprise group members.” The Bankruptcy Code provides for this relief domestically simply by permitting affiliates to file in the same venue.

In substance, the current draft provides that one member of an enterprise group, defined in Article 2(b) as “two or more enterprises [entities engaged in business] that are interconnected by control or significant ownership,” may be



authorized to act as the “representative of a planning proceeding in which enterprise group members are participating for the purpose of developing a group insolvency solution.” (Article 2(e)). “Planning proceeding” is currently defined in Article 2(g) as a “main proceeding” commenced in respect of an enterprise member “that is a necessary and integral part of a group insolvency solution, in which one or more additional group members are participating for the purpose of developing a group insolvency solution and in which a group representative has been appointed.”

As will be seen below, the COMI or “center of main interests” of an enterprise (similar to principal place of business) has been maintained as an important principle of the new draft, but the Working Group has so far avoided any effort to locate the “Group COMI” or to determine the identity or location of the COMI of the “principal” member of the group. The “planning proceeding” need only take place in the jurisdiction of an enterprise group member that is “a necessary and integral part of a group insolvency solution” and not a mere strawman. Any enterprise group member in an insolvency proceeding in a foreign court may then participate in a planning proceeding, subject, however, to the power of the local court to limit or control such participation. Articles 11, 13, 15.

The purpose of a planning proceeding, as noted above, is to develop a “group insolvency solution,” which is defined in the current draft in Article 2(f) as “a set of proposals” for the reorganization, sale or liquidation of some or all of the operations or assets of one or more group members “that would be likely to add to the overall combined value of the group members involved.” Article 2(f)(iii) goes on to provide that the proposals be submitted for approval in the jurisdiction in which a particular

group member has its center of main interests or an establishment (which would be the predicate for filing a nonmain proceeding), but it is not clear that each group member must file in its COMI or in a jurisdiction in which it carries on economic activity (the location of an establishment under the Model Law as currently drafted). In my opinion any such requirement would undermine the statutory goals.

In any event, the draft law is structured so as to give the “group representative” appointed in a “planning proceeding” limited powers to affect or influence insolvency proceedings pending in other jurisdictions. He or she may apply for recognition of the planning proceeding (Article 13), may seek and obtain interim relief in aid of the planning proceeding (Article 14), and may obtain a decision on recognition of the planning proceeding. (Article 15). After recognition of the foreign planning proceeding, the local court may grant “any appropriate relief,” including the approval of the treatment in the group proceeding of creditors located locally, and it may entrust the distribution of assets located locally to the group representative or another person “provided that the court is satisfied that the interests of creditors in this State [local creditors] are adequately protected.” Article 16. The draft goes on to provide that the group representative has standing to participate in a local proceeding (Article 17), that in granting or denying relief, the local court must be satisfied “that the interests of the creditors and other interested persons, including the debtor, are adequately protected” (Article 18), and that the local court may approve “local elements of a group insolvency solution.” (Article 19)

The current draft is thus modest in the authority it provides to the court of the “group proceeding” to affect or influence a court with authority over a “local” proceeding of a member of the group (assuming that all the members do not file in the group proceeding court). The only requirements in the law are the cooperation and coordination provisions of Articles 3 through 10, which are similar to the cooperation and coordination provisions of Articles 25-27 of the current Model Law (which have rarely if ever been treated as enforceable). Thus the new draft creates a basis for cooperation and communication between a local court and foreign courts and group representatives (Article 3), and between group representatives, foreign representatives and foreign courts. (Article 7) It provides explicit authority for entry into protocols (Article 10) , and it identifies several forms of “cooperation to the maximum extent possible”, including “sharing and disclosure of information,” “negotiation of agreements [protocols],” “allocation of responsibilities,” and “coordination of the administration” of group members and the negotiation of a group insolvency solution. (Articles 4 and 8). It provides that a single insolvency representative may be appointed over proceedings in more than one jurisdiction, subject to qualification and the supervision of the local court. Query whether the list of means of cooperation in Article 4 should be expanded to provide explicitly for the possibility of mediation and arbitration of intercompany claims, and for the cross-filing of claims by or on behalf of members of the corporate group.

The importance of promoting cooperation among courts and estate representatives with authority over the separate proceedings of members of an enterprise group should not be underestimated. Traditionally there has been little

or no cooperation, as each estate representative has sought to liquidate the assets under his or her control, with no concern for reorganization or the interests of the group. One goal of this Model Law is to change this attitude. However, there is no question that cooperation is superimposed on a system that protects local interests and local courts. At the insistence of several delegates, Article 1 sets forth three so-called overriding principles of the law, including that “the jurisdiction of the courts of the State in which the centre of main interests of an enterprise group member is located remains unaffected [unimpaired];” and any “process or procedure” required by such jurisdiction in connection with a group member’s participating in a group proceeding is “unaffected.”

In this draft Articles 11 and 13-19 are generally intended to govern the recognition and relief available in a local jurisdiction where an insolvency proceeding is pending with respect to a group member. Article 12 provides for, in many cases, similar relief available in the jurisdiction of the planning proceeding itself, which may be a jurisdiction where one group member is located or may be the jurisdiction in which multiple members have filed on grounds that their COMI is the same as another member (or located at headquarters). The planning proceeding court may grant broad interim relief and may grant relief provided for in Article 20 or 21 of the Model Law, such as a stay of individual actions or proceedings and entrustment of distribution of assets to an individual. Nevertheless, Article 12 provides that this relief is effective only in the state where the group proceeding is pending, and the group representative seemingly must seek similar relief in the local court if some of the members of the group have filed locally.

The Working Group has not decided, and the current draft is not clear, as to the extent to which the court administering the group proceeding can grant local creditors the recovery they would have received locally whether or not a local proceeding has been opened. Cases in England – most notably, *In re Collins & Aikman*, [2005] EWHC (Ch) 1754 -- have developed the principle of virtual secondary proceedings – that is, in order to deter local creditors from opening or maintaining an expensive and potentially burdensome local proceeding, the court of the “main proceeding” may authorize distribution to local creditors of what they would have received in a local case., notwithstanding the order of distribution of the main proceeding. The U.S. provides for somewhat similar relief on a non-statutory basis through first-day orders that usually provide that foreign creditors of a U.S. debtor be paid in full immediately, or a U.S. debtor will keep a foreign subsidiary that it wishes to preserve out of an insolvency case altogether and, if necessary, provide financing to keep the subsidiary’s creditors unimpaired.

The current draft provides for virtual relief with respect to nonmain local or secondary proceedings, in that the Court administering the group proceeding may provide creditors in a foreign state “the treatment in this State that they would have received in a non-main proceeding in that other State.” Article 20(1). Article 21 provides for the same relief to creditors who have opened or have threatened to open a local “main” proceeding (a proceeding in the COMI), and Article 22 would authorize “additional relief” for the benefit of such creditors. However, Articles 21 and 22 are, at the moment, entitled “supplemental provisions” that would not be part of the Model Law but provisions that a nation could consider for adoption

without UNCITRAL's imprimatur. The current draft, for the time being, thus perpetuates the dichotomy in the EU Regulation amendments, which provide for "virtual" relief but only for the benefit of creditors of nonmain secondary proceedings. The EU amendments also require that the local creditors in a virtual secondary jurisdiction vote on whether to accept the proposal, an unwieldy provision that has been much criticized. The current draft of the Model Law does not require a local vote, but it is still based on the fiction, held by many delegates to the Working Group, that the COMI of an entity can be clearly determined and that the right to open a proceeding there should be treated as sacrosanct.

A subcommittee of the Committee to Rethink Chapter 11 of this Conference has recommended that consideration be given to amendments to the Bankruptcy Code that would provide a statutory basis for administering group proceedings under the Bankruptcy Code, at least for integrated groups. There is currently little in the Bankruptcy Code or Rules that provide therefor. Three overriding principles have been suggested for new legislation – that the notion of a "corporate enterprise" be added to the statute; that structural priority of creditors be respected; and that creditors be entitled to a form of "adequate protection" based on their rights under the group structure. These proposals might be more closely considered at the same time as amendments to the Bankruptcy Code relative to cross-border group insolvencies.