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Foreign Third-Party Releases May Be Enforced Under Principles of Comity

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Introduction

Chapter 15 of title 11 of the United States Code (the “Bankruptcy Code”) provides a mechanism for a foreign debtor or a foreign representative to seek recognition of a foreign insolvency, liquidation, or bankruptcy proceeding and the enforcement of a foreign court’s orders issued in such proceedings in the United States.¹ A foreign bankruptcy proceeding or plan may contain “provisions that release non-debtors, such as officers, directors, shareholders, or non-debtor affiliates, from claims and causes of action held by creditors or other non-debtor parties.”² There is a split in the United States courts as to whether such a third-party release in a chapter 11 plan can be enforced.³ Several U.S. courts have recognized and enforced foreign reorganization plans that contain third-party releases in chapter 15 cases.⁴

This memorandum will examine the enforceability of third-party releases in the U.S. under chapter 15 in a threefold approach. Part I explores the availability of relief under § 1521

¹ See 11 U.S.C. § 1501(a) (2012).

² See Shantel Watters-Rogers, *Bankruptcy Court Enforces Non-Consensual Third-Party Releases in Chapter 15 Case*, 14 PRATT’S J. BANKR. L. 14-8-VII (2019).

³ See *In re Avanti Commc’ns Grp. PLC*, 582 B.R. 603, 606 (Bankr. S.D.N.Y. 2018) (noting the Fifth, Ninth, Tenth and the District of Columbia Circuits have held the Bankruptcy Code only permits a bankruptcy court to grant releases against a debtor, and prohibits third-party releases absent consent and the Second, Fourth, Sixth, Seventh, and Eleventh Circuits have held third-party releases may be given consensually and, in limited circumstances, may be approved without consent).

⁴ See, e.g., *In re Avanti*, 582 B.R. at 617-18 (recognizing and enforcing a scheme of arrangement, including a release of third-party guarantees).

and § 1507. Part II analyzes the appropriateness of enforcing third-party releases under § 1507. Part III examines the consistency of third-party releases with U.S. public policy under § 1506.

I. Relief in the Form of Third-Party Releases is Unavailable Under § 1521 But Available Under § 1507.

Third-party releases may be enforceable relief as “additional assistance” under § 1507 of the Bankruptcy Code. In determining whether third-party releases fall under the relief of § 1521 or § 1507, courts first consider the specific enumerated relief under § 1521(a)(1)–(7).⁵ If the relief is not explicitly provided for in those provisions, courts then consider whether the third-party release falls more generally under § 1521’s grant of “any appropriate relief.”⁶ If the third-party release is not available under “any appropriate relief” and therefore not formerly available under § 304, courts then consider whether the third-party release would be available as “additional assistance” under § 1507.⁷

A. Neither § 1521(a)(1)–(7)’s Enumerated Relief Nor § 1521(a)’s “Any Appropriate Relief” Provide for Third-Party Releases.

Under § 1521(a), upon recognition of a foreign proceeding, a bankruptcy court may “grant any appropriate relief” necessary to “effectuate the purpose of [chapter 15] and to protect the assets of the debtor or the interests of the creditors.”⁸ Such relief expressly includes:

- 1) staying the commencement or continuation of an individual action or proceeding concerning the debtor’s assets, rights, obligations or liabilities to the extent they have not been stayed under section 1520(a);
- 2) staying execution against the debtor’s assets to the extent it has not been stayed under section 1520(a);
- 3) suspending the right to transfer, encumber or otherwise dispose of any assets of the debtor to the extent this right has not been suspended under section 1520(a);
- 4) providing for the examination of witnesses, the taking of evidence or the delivery of information concerning the debtor’s assets, affairs, rights, obligations or liabilities;

⁵ See *In re Vitro S.A.B. de CV*, 701 F.3d 1031, 1054 (5th Cir. 2012).

⁶ See *id.*

⁷ See *id.*

⁸ 11 U.S.C. § 1521(a) (2012).

- 5) entrusting the administration or realization of all or part of the debtor's assets within the territorial jurisdiction of the United States to the foreign representative or another person, including an examiner, authorized by the court;
- 6) extending relief granted under section 1519(a); and
- 7) granting any additional relief that may be available to a trustee, except for relief available under sections 522, 544, 545, 547, 548, 550, and 724(a).⁹

Courts have found such “appropriate relief” to be the same type of relief that was previously available under § 304.¹⁰ Additionally, there are certain limits to this relief: the court may grant relief under § 1521 “only if the interests of the creditors and other interested entities, including the debtor, are sufficiently protected.”¹¹ The interests of the creditors will be sufficiently protected as long as the relief contemplated under § 1521 balances the interests of the creditors and debtors.¹²

Courts will not grant relief under § 1521 when the relief sought does not fall within the categories of enumerated relief or the general grant of “any appropriate relief.”¹³ For example, in *In re Vitro*, the foreign representative sought enforcement of a plan of reorganization approved by a Mexican court that included discharging obligations of third-party guarantors.¹⁴ The Fifth Circuit noted that the requested relief was not available under any of § 1521's specific provisions because “none of the types of relief enumerated under § 1521 . . . matches the type of relief” sought.¹⁵ The circuit court further explained that the requested relief fell outside of § 1521(a)'s grant of “any appropriate relief” because a non-consensual, non-debtor release through a

⁹ 11 U.S.C. § 1521(a)(1)–(7).

¹⁰ See *In re Vitro*, 701 F.3d at 1054 (“We understand ‘appropriate relief’ to be relief previously available under Chapter 15's predecessor, § 304.”).

¹¹ 11 U.S.C. § 1522(a)–(b).

¹² See *In re Tri-Cont'l Exch. Ltd.*, 349 B.R. 627, 637 (Bankr. E.D. Cal. 2006) (analysis of § 1522 “emphasize[s] the need to tailor relief and conditions so as to balance the relief granted to the foreign representative and the interests of those affected by such relief, without unduly favoring one group of creditors over another”).

¹³ See *In re Vitro*, 701 F.3d at 1058–59.

¹⁴ *Id.* at 1039.

¹⁵ *Id.* at 1058.

bankruptcy proceeding is not routinely granted under U.S. law.¹⁶ As a result, the circuit court refused to hold that relief in the form of third-party releases falls under § 1521.¹⁷

Therefore, a court will likely find that § 1521(a)'s specific provisions of relief and general grant of "any appropriate relief" do not provide for relief in the form of third-party releases.¹⁸

B. Third-Party Releases Do Fall Under § 1507's "Additional Assistance."

In addition to § 1521's "any appropriate relief," § 1507(a) gives courts authority to grant post-recognition relief in the form of "additional assistance" to a foreign representative; to provide relief not otherwise available under the Bankruptcy Code.¹⁹ Chapter 15 specifically contemplates that the court should be guided by principles of comity and cooperation with foreign courts in deciding whether to grant the foreign representative additional post-recognition relief.²⁰ In determining whether to provide additional assistance under § 1507, courts consider whether such additional assistance, consistent with the principles of comity, will reasonably assure:

- 1) just treatment of all holders of claims against or interests in the debtor's property;
- 2) protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceeding;
- 3) prevention of preferential or fraudulent dispositions of property of the debtor;
- 4) distribution of proceeds of the debtor's property substantially in accordance with the order prescribed by this title; and
- 5) if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns.²¹

¹⁶ *Id.* at 1059.

¹⁷ *Id.* at 1058.

¹⁸ In *In re Sino-Forest Corporation*, the bankruptcy court stated it was unnecessary to determine whether relief in the form of third-party releases was available under § 1521(a)'s specific provisions of relief or general grant of "any appropriate relief" because the court in *In re Metcalfe* decided third-party releases were available under § 1507. 501 B.R. 655, 663 n.3 (Bankr. S.D.N.Y. 2013) (declining to decide whether the "any appropriate relief" language in § 1521 would also provide a basis for the relief).

¹⁹ See 11 U.S.C. § 1507(a); see also *In re Vitro*, 701 F.3d at 1055.

²⁰ See *In re Atlas Shipping A/S*, 404 B.R. 726, 738 (Bankr. S.D.N.Y. 2009).

²¹ 11 U.S.C. § 1507(b)(1)–(5).

Upon recognition as a foreign main proceeding, “relief . . . is largely discretionary and turns on subjective factors that embody principles of comity.”²² The determination of whether to enforce a plan confirmed in a foreign proceeding should be made on a case-by-case basis.²³

Courts will therefore grant third-party releases as “additional assistance” under § 1507 when the principles of comity support enforcement of the plan at issue.²⁴ For example, in *In re Metcalfe*, the court considered recognition of a Canadian plan of reorganization that contained third-party releases.²⁵ The plan was adopted with near-unanimous creditor support.²⁶ Additionally, the plan was approved by Canadian courts.²⁷ Noting that it was not clear whether the third-party releases contained in the Canadian plan would be permitted under U.S. law, the court explained that the proper inquiry was whether the Canadian plan’s provisions should nevertheless be enforced under chapter 15.²⁸ The court found that there was no basis for it to second-guess decisions of the Canadian courts and that the principles of comity supported enforcement of the plan.²⁹ Accordingly, the court granted post-recognition relief by enforcing the non-debtor third-party releases.³⁰

Therefore, a court will likely conclude that § 1507 permits third-party releases as post-recognition relief in the form of “additional assistance.”

²² *In re Metcalfe & Mansfield Alt. Invs.*, 421 B.R. 685, 697 (Bankr. S.D.N.Y. 2010) (quoting *In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd.*, 389 B.R. 325, 333 (S.D.N.Y. 2008)).

²³ *See In re Oi S.A.*, 587 B.R. 253, 265 (Bankr. S.D.N.Y. 2018) (citing *In re Treco*, 240 F.3d 148, 156 (2d Cir. 2001) (stating, with respect to former § 304, “[a]lthough some of the considerations in determining whether to defer to a certain country’s bankruptcy proceedings may be constant from case to case, other factors vary”)).

²⁴ *See In re Metcalfe*, 421 B.R. at 696.

²⁵ *Id.* at 687.

²⁶ *Id.* at 700.

²⁷ *Id.*

²⁸ *Id.* at 694–96.

²⁹ *Id.* at 700.

³⁰ *Id.*

II. Granting Comity to, And Therefore Enforcing, Third-Party Releases Is Appropriate When the Plan Satisfies the Requirements in § 1507(b)(1)–(5).

Third-party releases are appropriate and will be enforced when the plan at issue meets the factors in § 1507(b)(1)–(5).³¹ Chapter 15 was intended to “provide effective mechanisms for dealing with cases of cross-border insolvency.”³² However, when dealing with cases of cross-border insolvency and judgments from foreign jurisdictions, U.S. courts often have to deal with outcomes that would otherwise not be available in the U.S.³³

In determining whether to grant relief as “additional assistance,” courts consider whether the foreign plan satisfies the statutory factors for affording comity.³⁴ First, § 1507(b)(1) is satisfied where the foreign insolvency law provides a “comprehensive procedure for the . . . equitable distribution of the debtor’s assets”³⁵ Second, § 1507(b)(2) is satisfied where creditors are given adequate notice of the timing and procedures for filing claims, and such procedures do not create additional burdens for a foreign creditor seeking to file a claim.³⁶ Third, § 1507(b)(3) is satisfied where an action may be brought to avoid transfers made to third parties with the intention to harm creditors or damage the debtor’s estate.³⁷ Fourth, § 1507(b)(4) is

³¹ See *In re Oi S.A.*, 587 B.R. 253, 267 (Bankr. S.D.N.Y. 2018).

³² 11 U.S.C. § 1501(a) (2012).

³³ See *In re Schimmelpenninck*, 183 F.3d 347, 353 (5th Cir. 1999) (“[I]t is not necessary that the result achieved in the foreign bankruptcy proceeding be identical to that which would be had in the United States.”).

³⁴ See *In re Treco*, 240 F.3d 148, 158 (2d Cir. 2001).

³⁵ See *In re Oi*, 587 B.R. at 267; see also *In re Avanti Commc'ns Grp. PLC*, 582 B.R. 603, 618 (Bankr. S.D.N.Y. 2018) (holding, where creditors were afforded an opportunity to be heard in a meaningful manner – *i.e.* by giving near-unanimous support for the scheme of arrangement that included third-party releases, UK bankruptcy law provided a comprehensive procedure for the equitable distribution of the debtor’s assets).

³⁶ See *In re Oi*, 587 B.R. at 268 (finding § 1507(b)(2) satisfied because, under Brazilian bankruptcy law, foreign creditors have the same status, the same rights and protections, and are subject to the same procedures, as local creditors with respect to the filing of claims).

³⁷ See *id.* (noting the possibility under Brazilian bankruptcy law for any creditor, the Brazilian public attorney’s office or the judicial administrator to bring an action to avoid fraudulent dispositions of the debtor’s property provides sufficient protection to prevent fraud).

satisfied where the foreign distribution scheme is simply “substantially in accordance” with the Bankruptcy Code rather than mirroring its distribution rules.³⁸

Therefore, a court will likely grant comity to, and thereby enforce, a foreign plan including third-party releases that satisfies the requirements in § 1507(b)(1)–(5).

III. A Foreign Plan That Meets the Fundamental Standards of Fairness is not Manifestly Contrary to U.S. Public Policy Under § 1506.

A foreign plan will not be manifestly contrary to U.S. public policy under § 1506 if it meets the fundamental standards of fairness.³⁹ Section 1506 places a public policy limitation on recognition, providing that “[n]othing in this chapter prevents the court from refusing to take an action governed by this chapter if the action would be manifestly contrary to the policy of the U.S.”⁴⁰ However, this public policy exception is narrowly construed and “applied sparingly.”⁴¹ Foreign judgments “are generally granted comity as long as the proceedings in the foreign court ‘are according to the course of a civilized jurisprudence, *i.e.* fair and impartial.’”⁴² The fact that the law in the U.S. may have provided different results is not, alone, grounds for denial of recognition and enforcement.⁴³ The key determination required by the court is whether the procedures used in the foreign jurisdiction “meet [the] fundamental standards of fairness [in the U.S.]”⁴⁴

³⁸ See *id.* at 268–69 (holding the Brazilian distribution system was substantially in accordance with U.S. law because priority was afforded to secured creditors as ensured by the Bankruptcy Code); cf. *In re Vitro S.A.B. de CV*, 701 F.3d 1031, 1065 (5th Cir. 2012) (holding the relief requested under the Mexican plan – a non-consensual discharge of non-debtor guarantors – was not substantially in accordance with the Bankruptcy Code because the plan depended on insider votes and the Bankruptcy Code prevents insiders from themselves pushing a plan through where there is a class of dissenting creditors).

³⁹ See *In re Rede Energia S.A.*, 515 B.R. 69, 107 (Bankr. S.D.N.Y. 2014).

⁴⁰ 11 U.S.C. § 1506 (2012).

⁴¹ See *In re Rede*, 515 B.R. at 92.

⁴² *Id.* (quoting *In re Toft*, 453 B.R. 186, 194 (Bankr. S.D.N.Y. 2011)).

⁴³ See *In re Metcalfe & Mansfield Alt. Invs.*, 421 B.R. 685, 697 (Bankr. S.D.N.Y. 2010) (“The relief granted in the foreign proceeding and the relief available in a U.S. proceeding need not be identical.”).

⁴⁴ See *id.*

In determining whether to extend comity to a foreign main proceeding's plan or reorganization, the court should consider (1) whether the foreign proceeding provided a full and fair opportunity for creditors to be heard consistent with due process, and (2) whether the plan was approved by the debtor's creditors and the foreign court.⁴⁵ Further, in analyzing procedural fairness, the Second Circuit has considered the following factors:

(1) Whether creditors of the same class are treated equally in the distribution of assets; (2) whether the liquidators are considered fiduciaries and are held accountable to the court; (3) whether creditors have the rights to submit claims which, if denied, can be submitted to a bankruptcy court for adjudication; (4) whether the liquidators are required to give notice to potential claimants; (5) whether there are provisions for creditors meetings; (6) whether a foreign country's insolvency laws favor its own citizens, (7) whether all assets are marshalled before one body for centralized distribution; and (8) whether there are provisions for an automatic stay and for the lifting of such stays to facilitate the centralization of claims.⁴⁶

Where the proceedings in the foreign court progressed according to the course of a civilized jurisprudence and where the procedures followed in the foreign jurisdiction meet the fundamental standards of fairness in the U.S., there is no violation of public policy.⁴⁷ For example, in *In re Rede*, the court considered granting relief requested by foreign representatives of debtors that were the subject of a reorganization proceeding pending in Brazil.⁴⁸ The debtors' assets were marketed through a competitive bidding process and resulted in the evolution and improvement of return to unsecured creditors.⁴⁹ Additionally, the Brazilian court determined that the debtors' assets and liabilities could be consolidated for plan purposes.⁵⁰ The plan was crammed down, on acceptance of a single secured creditor.⁵¹ The court noted that, although Brazilian bankruptcy law and procedures differed from U.S. law in certain respects, it will not

⁴⁵ See *In re Agrokor d.d.*, 591 B.R. 163, 189 (S.D.N.Y. 2018) (citing *In re Metcalfe*, 421 B.R. at 698–99).

⁴⁶ *Finanz AG Zurich v. Banco Economico S.A.*, 192 F.3d 240, 246 (2d Cir. 1999).

⁴⁷ See *In re Rede*, 515 B.R. at 107.

⁴⁸ *Id.*

⁴⁹ *Id.* at 99.

⁵⁰ *Id.* at 100.

⁵¹ *Id.*

decline to extend comity and grant additional relief “simply because Brazilian bankruptcy law is not identical to U.S. bankruptcy law.”⁵² Therefore, because Brazilian bankruptcy law meets the fundamental standards of fairness and accords with the course of civilized jurisprudence, the court held that granting comity to and enforcing the plan would not violate public policy.⁵³

Accordingly, a court will likely conclude that a foreign plan will not be manifestly contrary to U.S. public policy under § 1506 if it meets the fundamental standards of fairness.

Conclusion

Although Circuits are split on whether the Bankruptcy Code permits a bankruptcy court to grant releases against a third-party in a chapter 11 plan, several courts have allowed it in chapter 15 cases because of the importance of comity in chapter 15. However, because chapter 15 grants courts authority and discretion to recognize and enforce foreign proceedings on the basis of comity and cooperation with foreign courts, determinations of whether third-party releases granted in a foreign jurisdiction may be enforced in the U.S. under chapter 15 are made on a case-by-case basis. A third-party release granted in a foreign jurisdiction may be available relief under § 1507’s “additional assistance” and will likely be granted comity, and therefore enforced, when doing so would not violate § 1506’s public policy limitation. The case-by-case determination means that a court could deny enforcement of third-party releases if the requirements of § 1507 are not satisfied, if the goals of chapter 15 would not be furthered by enforcement, or if enforcement would prejudice the rights of United States citizens or violate domestic public policy.

⁵² *Id.* at 104.

⁵³ *Id.* at 107; *see also In re Oi S.A.*, 587 B.R. 253, 269 (Bankr. S.D.N.Y. 2018) (concluding Brazilian bankruptcy law is consistent with U.S. policy and provides to creditors meaningful protections similar to those provided under U.S. law).