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Do Foreign Representatives Need to Satisfy the Recognition Requirement?

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Introduction

A foreign representative must obtain recognition of a foreign proceeding pursuant to section 1517 of title 11 of the United States Code (the "Bankruptcy Code") prior to applying directly to a court in the United States for any relief such as operating the debtor's business operations in the U.S. or seeking assets and discovery from U.S. entities. However, under section 1509(f), a foreign representative may sue in a United States court to collect or recover a claim which is the property of the debtor without first obtaining recognition. The scope of this exception, though, remains unclear.

This memorandum explores whether recognition under chapter 15 of the Bankruptcy Code is a prerequisite for a foreign liquidator or debtor to bring litigation in the U.S. Part I discusses the general requirement of recognition under section 1509 before a foreign representative can bring a suit in U.S. courts. Part II provides a brief overview of the cases where the courts have allowed foreign representatives to circumvent the recognition requirement. Part III concludes by highlighting the scope and desirability of the section 1509(f) exception after exploring its possible interpretations.

I. Section 1509 generally requires recognition before a foreign representative can bring an action in U.S. courts

Section 1509 provides a foreign representative with direct access to the court for purposes of seeking recognition.[1] If the court grants recognition under section 1517, the foreign representative has the right to sue and be sued in courts in the United States, and apply directly to a court for appropriate relief.[2] In addition, U.S. courts are required to grant comity and cooperation to the foreign representative.[3] In contrast, if recognition is denied, the court may make any appropriate order to deny comity and cooperation.[4] In any case, and subject to sections 306 and 1510 of the Bankruptcy Code, the foreign representative is subject to otherwise applicable non-bankruptcy law of the United States.[5] Finally, in the limited circumstance wherein the foreign representative claims to recover the property of a debtor, the initial step of recognition may be skipped.[6]

A. Chapter 15 and its Purpose in the Context of Recognition

Chapter 15, which is based on the United Nations Commission for International Trade Law (UNCITRAL) Model Law on Cross Border Insolvency, was enacted to address certain objectives set forth in section 1501 of the Bankruptcy Code, including the following: cooperation between U.S. and foreign courts; greater legal certainty for trade and investment; protection and maximization of the value of the debtor's assets; and facilitation of the rescue of financially troubled businesses.[7] Chapter 15's legislative history clarifies that it was designed to be the

[1] 11 U.S.C. § 1509(a) (2012).
[2] *See id*. § 1509(b)(1)-(2) (describing the jurisdictional rights and consequences of the foreign representative under 11 U.S.C. § 1507).
[3] *Id.* § 1509(b)(3).
[4] *Id.* § 1509(d) (stating the consequences if recognition is denied).
[5] *Id.* § 1509(e).
[6] *Id.* § 1509(f).
[7] 11 U.S.C. § 1501.

"exclusive door to ancillary assistance to foreign proceedings,"[8] with its "primary purpose" to "facilitate the consolidation of multinational bankruptcy into one single proceeding."[9]

With essentially two objectives, i.e., obtaining comity from a United States court for a foreign insolvency proceeding and obtaining cooperation in the form of the relief necessary to carry out the objectives of the foreign insolvency proceeding, in some respects, chapter 15 is the bankruptcy analogue to domesticating a foreign judgment.[10]

B. Section 1509(f) Exception to the Recognition Requirement

Section 1509(f), however, provides a critical exception to the general rule of recognition by permitting a foreign representative "to sue in a court in the United States to collect or recover a claim which is the property of the debtor."[11] But even this exception is limited as noted in the legislative history: "[s]ubsection (f) provides a limited exception to the prior recognition requirement so that collection of a claim which is property of the debtor, for example an account receivable, by a foreign representative may proceed without commencement of a case or recognition under this chapter."[12]

Although section 1509(f) permits the foreign representative to sue in U.S. courts to collect or recover a claim regardless of the procedural status of the petition for recognition, the extent of this exception depends on how expansively the phrase property of the debtor is interpreted.[13] While the legislative history does not indicate so explicitly, the example of an

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[8] U.S. H.R. Rep. 109-031, 110 (2005).
[9] *In re ABC Learning Centres Ltd*., 728 F.3d 301, 305-06 (3d Cir. 2013).
[10] W. Neal McBrayer, *Achieving Recognition and Relief Pending Recognition in a Chapter 15*, 2012 WL 3279172 (2012).
[11] 11 U.S.C. § 1509(f).
[12] *See* H. Rep. 109–31(I) at 110–11 (2005), *as reprinted in* 2005 U.S.C.C.A.N. 88, 173.
[13] Brendan M. Driscoll, *International Comity After Chapter 15: A Residual Right to Recognition?* 17 J. Bankr. L. & Prac. 5 Art. 5.

account receivable—a concrete piece of property that is the subject of everyday transactions and lawsuits—suggests that the section 1509(f) exception to the recognition requirement may be aimed at preserving the efficiency of the bankruptcy courts.[14]

II. RANGE OF INTERPRETATIONS OF THE 1509(F) EXCEPTION IN CASE LAW

Chapter 15, instead of being simply another option, is the proper route for enforcing foreign insolvency orders in the United States. In *Oak Point Partners Inc. v. Lessing*,[15] the defendant, a German foreign representative, in a U.S. debt collection lawsuit sought to have the action dismissed on grounds of international comity because of a pending German insolvency proceeding. The court held that chapter 15 is the sole avenue for recognition of foreign insolvency proceedings, absent a "true conflict" of U.S. and foreign laws.[16] Furthermore, the court in *Millard* characterized recognition of a foreign proceeding as a "*sine qua non* for access to the U.S. Courts."[17]

However, the Bankruptcy Appellate Panel for the Ninth Circuit Court of Appeals, providing the first extended explanation as to the purpose of chapter 15, held that chapter 15 does not constrain a foreign representative from acts that do not require judicial assistance.[18] There, the foreign trustee of a Japanese debtor was allowed to exercise his authority over the foreign debtor's Hawaiian assets without authorization from a U.S. court.[19] More significantly, the court rejected the contentions based on the long-standing doctrine of international comity and

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[14] *Id.*
[15] No. 11-CV-03328, (N.D. Cal. Apr. 19, 2013).
[16] *Id.*
[17] *In re Millard*, 501 B.R. 644, 653 (Bankr. S.D.N.Y. 2013) ("Section 1509 of the Code, captioned 'Right of direct access', effectively establishes the bankruptcy court as a gatekeeper for a foreign representative's access to the U.S. Courts, with recognition as the means to open the gate.").
[18] *In re Iida*, 377 B.R. 243, 258 (B.A.P. 9th Cir. 2007).
[19] *Id.* at 263.

the legislative purpose behind chapter 15, emphasizing that it was enacted as a "fundamentally procedural" statute and "did not constitute a change in the basic approach of U.S. law, which . . . has long been one of honoring principles of comity."[20] Noting that nothing in the statute required prior judicial permission for acts that do not implicate matters of comity or cooperation by courts, the court concluded that chapter 15 does not restrain a foreign representative from discharging his duties in the U.S., so long as those duties do not violate the public policy and do not require judicial assistance.[21]

Any other result could have had a negative impact on international capital flow and liquidity, and reduce predictability and asset pricing uniformity in the international markets—precisely those facets of international commerce that chapter 15 is tailored to protect and facilitate.[22] The distinction between the permissive and mandatory nature of the statute is critical, with *Iida* underscoring that the permissive nature of old section 304 of the Bankruptcy Code has carried over to chapter 15.[23]

Furthermore, in *In re Loy*, wherein the issue was the filing of *lis pendens* by a foreign representative, the court held that because it was "a ministerial task conducted by the clerk of [the] court" and did not "implicate the comity or cooperation of a court," prior chapter 15 recognition was not required.[24] Additionally, the court noted that even if *lis pendens* filing did implicate comity or cooperation, recognition was still not required as it was merely the first step in a suit to recover claim against the debtor, which may be done without recognition under

[20] *Id.* at 256.
[21] *Id.* at 258.
[22] Kenneth H. Brown et. al., *Stranger in Paradise? The Role of A Foreign Bankruptcy Trustee in Chapter 15*, Am. Bankr. Inst. J., April 2008, at 26.
[23] *Id.* at 26, 68.
[24] 380 B.R. 154, 166 (Bankr. E.D. Va. 2007).

section 1509(f).[25] *Loy* suggests that section 1509(f) can be interpreted broadly, thereby permitting U.S. non-bankruptcy courts to grant many kinds of relief to a foreign representative in a non-qualifying proceeding as long as that relief is related in some way to "collect[ing] or recover[ing] a claim which is property of the debtor."[26]

A. Options Available to a Foreign Representative

While a foreign representative who has not obtained chapter 15 recognition will be denied the benefits of the automatic stay, courts have noted that a foreign representative has other potential remedies available, for example filing an involuntary case under chapters 7 or 11 of the Bankruptcy Code, and suing under section 1509(f) to collect or recover a claim which is property of the estate.[27]

Section 1509(d), in specifying that a bankruptcy court "may" issue any appropriate order to prevent foreign representative from obtaining comity from courts in United States after being denied recognition under chapter 15, highlights the discretionary nature of the court's power.[28] Consequently, a foreign representative's ability to file for recognition outside the bankruptcy arena based on the doctrine of comity is not necessarily conditioned on the foreign proceeding being recognized under chapter 15.[29]

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[25] *Id.* at 166-67.
[26] Alesia Ranney-Marinelli, *Overview of Chapter 15 Ancillary and Other Cross-Border Cases*, 82 Am. Bankr. L.J. 269, 303–04 (2008).
[27] *In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd*., 374 B.R. 122, 132 (Bankr. S.D.N.Y. 2007), *aff'd*, 389 B.R. 325 (S.D.N.Y. 2008) (noting that 11 U.S.C. § 303(b)(4), which the 2005 Amendments neither repealed nor amended, continues to authorize a foreign representative to commence an involuntary proceeding under either chapter 7 or chapter 11 without explicitly requiring recognition as a condition precedent).
[28] *See* 11 U.S.C. § 1509(d).
[29] *See* H.R. Rep., No. 109-31, pt. 1, at 110 (specifying that §1509(d) incorporated into chapter 15 to preclude foreign representatives whose foreign proceeding was denied recognition under chapter 15, from seeking relief in other U.S. courts based on comity).

Additionally, in *In re Bozel*, a liquidator in a foreign proceeding of a parent of a subsidiary that was a debtor in chapter 11 was not required to obtain recognition before seeking relief in U.S. bankruptcy court to enforce the liquidator's corporate governance rights over the subsidiary/chapter 11 debtor-in-possession (the "DIP") because no foreign proceeding involving the DIP was commenced, nor was a foreign representative of the DIP seeking relief.[30] As another example, if a Part VII transfer is denied recognition under chapter 15, a U.S. policyholder might try to bring a claim against the transferring company instead of the target company, because the transfer was not recognized under U.S. law, in which case section 1509(f) will enable a foreign representative to sue in a U.S. court.[31]

B. Cases Allowing Direct Access to Foreign Representatives

Recently, in *Trikona Advisers Ltd. v. Chugh*, the Second Circuit identified the four circumstances under which chapter 15 applies as specifically set forth in section 1501(b) of the Bankruptcy Code: (i) assistance sought in the U.S. by a foreign court or a foreign representative in connection with a foreign proceeding; (ii) assistance sought in a foreign country in connection with a case under the Bankruptcy Code; (iii) a foreign proceeding and a case under the Bankruptcy Code with respect to the same debtor are pending concurrently; or (iv) creditors or other interested persons in a foreign country have an interest in requesting the commencement of, or participating in, a case or proceeding under the Bankruptcy Code.[32] The Second Circuit noted that inherent in those scenarios, however, is the assumption that (i) the U.S. court is being

[30] *In re Bozel S.A.*, 434 BR 86, 94-95 (Bankr. S.D.N.Y. 2010).
[31] Jennifer D. Morton, *Recognition of Cross-Border Insolvency Proceedings: An Evaluation of Solvent Schemes of Arrangement and Part VII Transfers Under U.S. Chapter 15*, 29 Fordham Int'l L.J. 1312, 1359–60 (2006).
[32] 846 F.3d 22, 31 (2d Cir. 2017).

asked either to assist in the administration of a foreign liquidation proceeding itself; or (ii) a foreign court is being asked to assist in administration of a liquidation proceeding in the U.S.[33]

The appellant in *Trikona* argued that because an application for recognition of the "foreign proceeding" (i.e., the Cayman proceeding) was not made or pending in the U.S., it was impermissible for the District Court to "recognize" the judgment of the Cayman court.[34] However, the proceeding in the District Court did not stem from any of the enumerated circumstances set forth in section 1501(b) of the Bankruptcy Code. Accordingly, the Second Circuit held that "Chapter 15 does not apply when a court in the U.S. simply gives preclusive effect to factual findings from an otherwise unrelated foreign liquidation proceeding," especially because the District Court proceeding was a "non-bankruptcy action, brought in the District of Connecticut and governed by Connecticut law."[35] Notably, in response to appellant's argument that chapter 15 of the Bankruptcy Code preempts the state law doctrine of comity, the Second Circuit explained that such a conclusion could not have been the intent of Congress given "the very narrow purpose of Chapter 15."[36]

Similarly, in *Petersen Energia Inversora, S.A.U. v. Argentine Republic*,[37] the Southern District of New York declined to dismiss a claim based on lack of standing by highlighting the exception afforded by section 1509(f). In *Petersen*, Plaintiffs, Spanish limited-liability companies, owned shares of Defendant YPF S.A., an Argentinian publicly-held limited liability stock company, amounting to just over 25% of the company. In 2012, the Republic of Argentina expropriated 51% of YPF's shares by declaring public need, leading to a substantial decrease in

[33] *Id.*
[34] *Id.*
[35] *Id.*
[36] *Id.* at 35.
[37] 15-CV-2739 (LAP), 2016 WL 4735367 (S.D.N.Y. Sept. 9, 2016).

the value of YPF's shares. Consequently, YPF did not make an expected dividend distribution to shareholders, forcing the Plaintiffs to default and undergo insolvency proceedings in Spain. After Plaintiffs received approval of a liquidation plan, Plaintiffs' receiver brought this action alleging that Defendants breached obligations arising out of YPF's bylaws upon Argentina's expropriation of YPF shares. Defendant moved to dismiss on various grounds including lack of standing arguing that Plaintiffs' receiver did not first obtain recognition for the foreign insolvency proceedings. The court denied the motion to dismiss, reasoning that Plaintiffs were not requesting comity or cooperation from the court with respect to their foreign insolvency proceedings, but were seeking to recover an independent claim that was the property of their receivership, rendering the prior recognition unnecessary to confer standing.

THE SCOPE AND DESIRABILITY OF THE SECTION 1509(F) EXCEPTION

The flow of the cases to date delineates the possible avenues for foreign representatives to access within and without the bankruptcy context. *Trikona* and *Petersen* highlight foreign representatives' right to sue if the underlying claim is independent of bankruptcy or existed prior to the bankruptcy. It follows that chapter 15 does not prevent a foreign representative from taking actions that do not directly imply judicial assistance. Therefore, section 1509(f) preserves foreign representatives' access to U.S. courts by allowing them to bypass the recognition process when they do not require comity.

Chapter 15, as did section §304 before it, provides a foreign representative certain rights to administer, with the assistance of a U.S. bankruptcy court if necessary, the assets of a foreign debtor located in U.S. without needing to seek the imprimatur of a federal bankruptcy tribunal

before taking legally permissible actions with respect to those assets.[38] However, given the adverse scenario of a section 1509(d) order, which allows a court discretion to make any appropriate order to deny comity and cooperation, state courts may not be receptive enough to open their doors to an unrecognized foreign representative with no right of direct access.[39]

The practical solution to this problem, in line with the purposes of chapter 15, is to interpret section 1509(f) broadly, permitting many types of relief to fall under the process of collecting or recovering a claim which is property of the debtor. Any steps that a foreign representative takes to further the process, like the *lis pendens* filing in *Loy*, can bypass the direct implication of comity and therefore fall within the scope of section 1509(f).

The extent of section 1509(f) exception, however, remains unclear because the need for comity in certain instances may be ambiguous. Regardless, section 1509(f) seems to offer an alternative basis for foreign representatives to have their day in court in cases where the recognition requirement might actually be superfluous.

Conclusion

Recognition appears to be a prerequisite only in cases that require the comity of the U.S. courts directly with respect to a foreign proceeding. However, in case a foreign representative is looking to collect or recover property of the debtor, or taking some steps towards the same, the recognition requirement should not be an obstacle. At the end, the choice to obtain recognition

[38] Brown, Am. Bankr. Inst. J., April 2008, at 26.

[39] Timothy T. Brock, *The Assault on Offshore Havens in Bear Stearns Undermines New Chapter 15: Part II*, Am. Bankr. Inst. J., February 2008, at 24, 73–74 ("Without the right of direct access to U.S. courts and real party-in-interest status that recognition allows, it is unclear whether an unrecognized foreign representative would have standing under a state's law to bring an action on the entity's behalf. Moreover, state courts might shy away from allowing suits otherwise authorized by §1509(f) in the face of a bankruptcy court order issued under §1509(d).").

depends on the primary goals of a foreign representative given the benefits that come along with recognition. Given the relative ease of satisfying the threshold requirements for recognition, in addition to the streamlined procedures and statutory presumptions making the process simple and expedient, dependence on section 1509(f) entails an unworthy risk that can be efficiently guarded against by obtaining recognition.