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COMI and get it: international approaches to cross-border insolvencies

KEY POINTS

- Chapter 15 recognition does not mean that all foreign insolvency judgments and orders will be given a "rubber stamp" and simply enforced in the US. Bankruptcy courts may in the future be required to undertake a COMI-type analysis if there are instances of foreign jurisdictions rejecting the authority of the US bankruptcy court over a debtor due to its limited connections and history with the US. If that is the case, a US bankruptcy court may have little choice but to dismiss the case and allow it to proceed in the jurisdiction of the debtor's COMI.
- The English courts have shown a great deal of willingness to accept jurisdiction over a foreign entity seeking an English law scheme of arrangement. However, to date the English courts have yet to consider a scheme of arrangement where there was real doubt as to whether another jurisdiction would enforce the scheme due to the English court's lack of jurisdiction and there are indications that this may soon change.
- Recent events suggest that it will likely be a jurisdiction that is not signatory to the Model Law that will force either the US or English courts to more fully consider the principle that a debtor's insolvency case should proceed in the jurisdiction where the debtor's COMI is.

In our increasingly global world, cross-border insolvencies have become relatively commonplace. Lehman Brothers and Nortel Networks are just two of the matters where parallel proceedings in multiple jurisdictions were necessary in order to effectively administer the debtors' estates. The relevant legislation and guidance that were established to assist with these types of cross-border matters – namely the Insolvency Regulation (EC) 1346/2000 (the "Regulation"), which applies across the European Union with the exception of Denmark, and the UNCITRAL Model Law on Cross-Border Insolvency (the "Model Law"), which has 25 signatories to date including both the United States and the United Kingdom – have now been in place for 25 years and 19 years respectively. Although the Model Law and the Regulation have different scopes and purposes, they are similar in that both were specifically adopted to ensure that the necessary framework was in place so that cross-border insolvency proceedings could be conducted in an efficient and effective manner while also promoting fairness and transparency. In order to further this goal, both the Model Law and Regulation provide for automatic or simplified recognition of cases pending in jurisdictions that are signatories to or subject to the applicable legislation.

Neither the Regulation nor the Model Law seek to address or harmonise the substantive differences among insolvency regimes in different jurisdictions, but both are similar in that they are based on the premise that a debtor's "centre of main interest" (COMI) is the proper jurisdiction for its primary insolvency case or "main proceeding". In its introduction, the Model Law states that its framework is based on the premise that "the proceeding pending in the debtor's centre of main interests is expected to have principal responsibility for managing the insolvency", with this principle applying regardless of the number of jurisdictions in which the debtor may have assets and/or creditors (*United Nations Commission on International Trade Law, Guide to Enactment and Interpretation of the UNCITRAL Model Law on Cross-Border Insolvency*). Likewise, the Regulation defers to the jurisdiction of the debtor's COMI to open and maintain the "main proceeding", which has universal scope over all of the debtor's assets and liabilities, with any secondary proceedings thereafter limited to assets only located within the jurisdiction in which the secondary proceeding was opened.

Neither the Regulation nor the Model Law explicitly define COMI, other than to posit that it is presumed that a debtor's COMI will be its jurisdiction of incorporation, which presumption can be rebutted, and that it should correspond to where "the debtor conducts the administration of his interest on a regular basis and is therefore ascertainable to third parties" (Regulation, Recital 13). As such, case law has developed a somewhat inexact test to determine COMI for a given debtor. This case law has focused on a cumulative factual analysis looking at where, amongst other factors, operations are maintained, head office functions performed, employees are located and creditors could reasonably expect an insolvency or restructuring case to be commenced. When considered as a whole, these factual indicators should

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dictate the appropriate jurisdiction for a given matter where there are multiple jurisdictions at issue. In an effort to clarify, amongst other things, COMI, substantial reforms to the existing Regulation will come into effect on 26 June 2017 (the "Recast Regulation"), and will include changes to COMI and the presumptions that will apply if COMI is shifted from one jurisdiction to another in the months prior to the commencement of an insolvency proceeding.

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THE JUDGMENT IN *BRAC*

One of the first cases to address COMI in England was *Re BRAC Rent-A-Car International Inc* [2003] EWHC 128 (Ch). BRAC Rent-A-Car International Inc ("BRAC") was a Delaware company with its registered office in the US. It had no employees in the US and other than a small amount of operations in Europe, all its business operations were run from England. An administration was commenced in England in order for BRAC to obtain the benefit of the moratorium against a judgment entered against it in Italy. In light of the then recently passed Regulation, the English court had to consider whether England was the proper jurisdiction for BRAC's insolvency proceeding on the basis that its COMI appeared to be in England, even though it was a Delaware company. On analysing the legislation itself and the factual circumstances surrounding BRAC, the court ultimately found that its COMI was in England and, on that basis, the English administration should be permitted to continue. The analysis focused on what was the logical and predictable jurisdiction for BRAC and those contracting with BRAC, and considered a number of factors, including the address from which it traded, where its employees were located and the governing law of its contracts. In addition to being one of the first cases to address the proper jurisdiction of an international debtor, this decision is notable in that it reached its conclusion on what had then only recently been formally recognised as a fundamental principle of international insolvency law – that the jurisdiction of an insolvency proceeding should be fair, predictable and based on the factual history and circumstances of a debtor.

In the years since the implementation of the Model Law and the Regulation, and the judgment in *BRAC*, the trend of COMI or jurisdiction shifting has been particularly prevalent in both England and the US, both of which are known for their sophisticated, yet markedly different, insolvency regimes. Both jurisdictions have found themselves as the jurisdiction of "choice" for complex, cross-border cases notwithstanding that they are not the COMI or logical jurisdiction of the debtor. Furthermore, despite their differences, both the US and England are similar in their willingness to accept jurisdiction over a proposed insolvency or restructuring when there are, at times, what might appear to be tenuous grounds for doing so. This is possible because although both England and the US are subject to the Model Law, internal laws in both jurisdictions allow their courts to accept jurisdiction over foreign entities whose centre of main interest is located elsewhere, with both the US Bankruptcy Code and the English Companies Act 2006 (which governs schemes of arrangement) permitting such action.

It should be noted that English insolvency procedures governed by the Insolvency Act 1986 (IA 1986) are subject to the Regulation, and any procedures under the IA 1986 may only proceed as "main proceedings" if the debtor's COMI is in England. Schemes of arrangement are specifically not included as an "insolvency procedure" or "winding-up procedure" subject to the existing Regulation, and, although there was some discussion about whether they would be included in the Recast Regulation, have not been included as an applicable procedure in the Recast Regulation. As such, although both Chapter 11 and schemes of arrangement do not require the courts to consider a debtor's COMI and allow the courts the flexibility to accept jurisdiction over cases where the COMI requirement is not met, recent trends suggest that these courts should nonetheless consider recognised principles of international insolvency law when determining if they should exercise jurisdiction. To date, neither jurisdiction has made this a focus or requirement, but this may change.

THE UNITED STATES

A prerequisite to a bankruptcy court's jurisdiction in both a Chapter 11 case as well as recognition of a foreign proceeding under Chapter 15, the debtor must be able to satisfy s 109(a) of the Bankruptcy Code, which requires that a debtor must reside, have a domicile, a place of business or property in the US. It is common for foreign debtors to rely on the "property" element of s 109, with such element being satisfied by, for example, money held in a debtor's lawyer's client account, as was the case in *In re Octaviar Admin Pty Ltd* 511 B.R. 361, 369-74 (Bankr. S.D.N.Y. 2014). The Southern District of New York Bankruptcy Court in the case of *In re Berau Capital Resources Pte Ltd* (61 Bankr. Ct. Dec. 198 (Bankr. S.D.N.Y. 2015) recently further expanded a bankruptcy court's jurisdiction when it found that the fact that the debtor was an obligor under a New York law governed indenture was a "property right" located in New

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York, which was sufficient to satisfy the eligibility requirements under s 109 of the Bankruptcy Code for purposes of Chapter 15 recognition. This decision is especially notable in that reference to the New York law governed indenture was not necessary to find jurisdiction and no objections were filed to the Chapter 15 motion. Although some prospective foreign debtors may rejoice in this further expanding of US bankruptcy court jurisdiction, such potential debtors should be aware that with the benefits of Chapter 15 comes the oversight of the US bankruptcy court for proceedings and enforcement within the jurisdictional bounds of the US.

Chapter 15 recognition does not mean that all foreign insolvency judgments and orders will be given a "rubber stamp" and simply enforced in the US, and such judgment and orders will be subject to the oversight of the US bankruptcy court. A clear example of this was the case of *In re Vitro, S.A.B. de C.V* 473 B.R. 117 (Bankr. N.D. Tex. 2012), where the Northern District of Texas Bankruptcy Court held that the Chapter 15 debtor's Mexican *Concurso* was not enforceable in the US on public policy grounds. While the decision in *Berau Capital Resources* may show the extent to which the bankruptcy court views its jurisdictional reach, and *Vitro* may evidence how the bankruptcy court will exercise the powers given to it once jurisdiction is established, the recent decision of the Delaware Bankruptcy Court in the *Baha Mar* bankruptcy case shows that there is another consideration of jurisdiction and international law that US bankruptcy courts may need to consider – namely, how other jurisdictions view the US bankruptcy court's claims to jurisdiction over foreign debtors.

The Delaware bankruptcy court recently considered issues of jurisdiction in the *Baha Mar* bankruptcy case. Judge Carey noted in his judgment, dismissing all but one of the debtors, that it "was a truly international case with the main contestants hailing from Wilmington, Delaware, to Beijing, China to Nassau, the Bahamas" but that "[t]he central focus of this proceeding [...] is the unfinished Project located in the Bahamas". The decision further noted that "[i]n business transactions, particularly now in today's global economy, the parties, as one goal, seek certainty. Expectations of various factors – including the expectations surrounding the question of *where* ultimately disputes will be resolved – are important, should be respected, and not disrupted unless a greater good is to be accomplished" (*In re Northshore Mainland Services, Inc*, Case No. 15-11402). These considerations, coupled with a refusal of the Bahamian courts to recognise the jurisdiction of the US bankruptcy court over the Bahamian-based debtors or enforce the automatic stay, led Judge Carey to decline to exercise jurisdiction over all but one of the Baha Mar debtors.

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Judge Carey did not consider COMI, which is not a requirement for US jurisdiction under s 109 of the Bankruptcy Code for either a Chapter 11 or a Chapter 15 case. However, the judgment does highlight that a COMI-type analysis may be appropriate when determining whether US jurisdiction should be found in an international case under s 1112(b)(1) of the Bankruptcy Code, which allows a bankruptcy court to dismiss a case for "cause", or s 305(a)(1) of the Bankruptcy Code, which provides that a bankruptcy court may dismiss a case if to do so would be in the interest of creditors and the debtor would be better served by such dismissal, separate and apart from whether jurisdiction is permitted. Bankruptcy courts may be pushed towards undertaking a COMI analysis if there are more instances of other jurisdictions rejecting the authority of the US bankruptcy court over a debtor due to its limited connections and history with the US. If that is the case, a US bankruptcy court may have little choice but to dismiss the case because it would simply not be effective, and instead allow it to proceed in an alternative jurisdiction, which is likely to be where the COMI is found.

ENGLAND

Similarly, the English courts have shown a great deal of willingness to accept jurisdiction over a foreign entity seeking an English law scheme of arrangement. To reiterate schemes of arrangement (which are not proceedings under the IA 1986 but a restructuring mechanism similar to Chapter 11) are not subject to the Regulation and so English courts do not need to determine COMI when sanctioning a scheme of arrangement.

Nonetheless, a foreign entity will frequently still seek to shift its COMI to England in the months prior to it presenting a scheme to the English court, in order to take advantage of English insolvency procedures if the scheme fails. Recognition of schemes within the European Union is typically founded upon the EU Judgments Regulation, which requires EU courts to not question the jurisdiction of a court in another EU member state that has issued a judgment other than on limited public policy grounds. The Model Law is different, in that unlike the Regulation, which is limited to a defined list of procedures for each relevant jurisdiction, the Model Law (as implemented in the US through Chapter 15 of the Bankruptcy Code), provides for recognition of a foreign main proceeding (determined by reference to COMI) or foreign non-

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main proceeding (for proceedings in non-COMI jurisdictions), with "foreign proceeding" being defined as a collective judicial or administrative proceeding in a foreign country under a law relating to insolvency or adjustment of debt for the purpose of liquidation or reorganisation, and which is controlled or supervised by a foreign court.

"Although not an insolvency procedure under English law, schemes of arrangement are generally viewed as fitting within the Model Law and are entitled to recognition in countries that are signatory [to it]"

Although not an insolvency procedure under English law, schemes of arrangement are generally viewed as fitting within the Model Law and are entitled to recognition in countries that are signatory to the Model Law, which is important as Chapter 15 recognition is often viewed as an essential element of a scheme in order to obtain the benefit of the automatic stay in the US. Like the EU Judgment Regulation, recognition under the Model Law is subject to exceptions on public policy grounds, which could include a lack of jurisdiction in the appropriate case.

To date, the English courts have yet to consider a scheme of arrangement where there was real question or doubt as to whether another jurisdiction would enforce the scheme due to a lack of jurisdiction of the English court, but there are indications that this may soon change. More and more non-English companies are seeking English schemes of arrangement, and the connections between these debtors and England have become more and more deliberately constructed, as is evident in the case of *Apcoa Parking Holdings Gmbh* (*Apcoa*) [2014] EWHC 3849 (Ch). Apcoa was a pan-European car park operator whose connection to England for the purposes of jurisdiction was that English law was the governing law of its loan documents, which governing law was changed solely as a basis to create the connection necessary for the English court to accept jurisdiction to approve the scheme. In a thorough analysis, the court reviewed the facts before it in light of applicable case law and the relevant legislation. One aspect that it addressed briefly was whether the scheme would be recognised and enforced under the law of each of the relevant jurisdictions where the scheme would need to apply to be effective. The court ultimately found that the relevant foreign law experts from Germany, Belgium, Denmark, Norway and Austria each concluded that the local court in the applicable jurisdiction would give effect to the scheme. On this basis, the court concluded that it saw "no real reason to doubt that the Schemes would be recognised and enforced in the relevant EU jurisdictions: the court, in giving sanction, should not be acting in vain".

While it is possible that an EU member state or Model Law signatory may challenge an English court's jurisdiction to sanction a scheme, it is more likely that the English courts will be presented with a case where one of the relevant jurisdictions necessary for the scheme to be effective is not subject to the Model Law or the Regulation, and questions the English court's jurisdiction on the basis that a restructuring proceeding should not proceed in England, but instead occur in the location where the entity at issue has its COMI. Although a COMI shift to England is frequently done as part of a scheme, both as a back-up measure to take advantage of English insolvency procedures if the scheme fails and for the purposes of Chapter 15 recognition of the scheme is approved, once the Recast Regulation comes into effect in 2017, this "shift" may be more difficult to achieve and more cases may arise where the debtor's COMI is not England. If there is a question regarding effectiveness in other relevant jurisdictions, then from a practical perspective, an English court may need to undertake a COMI analysis as part of its determination as to whether other jurisdictions will enforce the scheme on jurisdictional grounds to ensure that such scheme is not in vain. Most commentators recognise that the English courts' jurisdiction to sanction a scheme has limits, but note that those limits are not yet defined. The defining line will likely not come from the English courts themselves, but from an English court recognising that its claim to jurisdiction may not withstand the scrutiny of others.

CONCLUSION

The international principle that a debtor's insolvency case should proceed in the jurisdiction where the debtor's COMI is has been accepted by both the US and the UK, as evidenced by the Model Law. What is interesting is that recent events suggest that it will likely be a jurisdiction that is not signatory to the Model Law that will force either the US or English courts to more fully consider this principle. While this may seem somewhat nonsensical, it will only go to show the principle that "a debtor's insolvency proceeding should be driven by the jurisdiction where it has its COMI", is truly a universally accepted principle of international insolvency law. ■

Further reading

- LexisPSL Restructuring and Insolvency: Practice note: Recognition of foreign insolvency proceedings in the US under chapter 15
- Cross-border observations derived from my Lehman judicial experience (2015) 3 JIBFL 131
- LexisPSL Restructuring and Insolvency: Practice note: cross-border recognition of schemes