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Repatriating Proceeds of a U.S. Avoidance Action to A Foreign Main Proceeding: Does Chapter 15 Authorize Structured Dismissals?

By Richard J. Mason and Patricia K. Smoots

In 1988, well before the enactment of Chapter 15 of the Bankruptcy Code,[1] a U.S. Bankruptcy Court permitted the foreign liquidators of a Hong Kong bank, Axona International Credit & Commerce Limited ("Axona"), to file a plenary U.S. bankruptcy case in order to invoke U.S. avoidance law against certain of Axona's U.S. creditors, and then, subject to certain conditions, suspend the U.S. bankruptcy case and repatriate most of the recovered proceeds for distribution under Hong Kong insolvency law through the Hong Kong proceeding.[2] The bankruptcy court applied the then-current versions of §§ 303 through 305 of the Bankruptcy Code to authorize the procedure,[3] over the vehement objections of a U.S. creditor — ("the Bank"). The bankruptcy court's ruling expressed a high degree of confidence in and deference to the Hong Kong Supreme Court, before which Axona's primary winding-up proceeding was pending (the "Hong Kong Proceeding"), and its rationale reflected a mix of universalist and territorial approaches to cross-border cooperation.[4] The court's decision also took on aspects of orders that are now often called "structured dismissals," a controversial means of concluding a bankruptcy case and one that is currently under review by the U.S. Supreme Court.[5]

This article examines the *Axona* decision in detail, and explores whether, under Chapter 15, which is considered to follow a "modified universalism" approach,[6] insolvency representatives of foreign main proceedings can and should be able to accomplish results similar to those approved in *Axona.* In effect, the procedure used in *Axona* arguably allowed the foreign liquidators to file and use a U.S. bankruptcy case to their advantage and then to opt out of the full administration of the case in favor of a legal system they perceived to be more beneficial to them, in much the way a "structured dismissal" can result in a disposition of bankruptcy estate proceeds in a manner not entirely consistent with the priority scheme and procedural safeguards set forth in the Bankruptcy Code.

The *Axona* bankruptcy court and the district court that affirmed its ruling were motivated by the laudable goals of cross-border cooperation and efficiency, and their decisions were arguably consistent with the state of the developing law as it then existed. In the opinion of the authors, however, if a similar case were to be presented under current Chapter 15, the bankruptcy court would likely take a narrower view of the options available, and conclude that it ought not permit dismissal of a plenary U.S. bankruptcy case and repatriation of the proceeds of U.S. avoidance actions to a foreign main proceeding unless no creditor objected and the foreign representative demonstrated that U.S.-based creditors would not be harmed.

The *Axona* Decision

Axona, a Hong Kong-based bank, did not conduct banking activities in the U.S., but did business with U.S. banks and maintained certain substantial deposits in U.S. accounts, against which three of Axona's U.S. bank creditors ("Attaching Creditors"), obtained *ex parte* attachments ("Attachments") upon Axona's collapse.[7] One U.S.-based creditor — the Bank — through its Hong Kong branch, made a $3 Million unsecured loan to Axona, only to learn that, on the same day, Axona's primary funding source had failed.[8] The Bank quickly implemented a strategy, with the cooperation of Axona management, to replace the unsecured loan with a secured loan (originating in the Bank's New York branch) followed by a prompt setoff against the security to satisfy the loan in full (the "Setoff").[9] About two and a half months after the Setoff, Axona became the subject of the Hong Kong Proceeding, and the Hong Kong court appointed liquidators (the "Liquidators").[10]

Upon discovery of the Attachments and the Setoff, the Liquidators filed an involuntary Chapter 7 case against Axona in New York.[11] The bankruptcy court entered an order for relief over the Attaching Creditors' objections, and the appointed trustee ("Trustee"), working with the Liquidators, commenced various avoidance actions and other adversary proceedings against the Attaching Creditors and the Bank.[12] The Bank raised certain defenses, including objections to the bankruptcy court's jurisdiction to hear the U.S. bankruptcy case, a contention that, absent special circumstances, § 303 cannot constitutionally authorize a foreign debtor with no "business presence" in the U.S. to employ U.S. avoidance laws, and a related argument that the proceedings violated the Bank's rights to due process and equal protection.[13] The Trustee eventually settled with all of the defendants, including the Bank, which agreed to pay $2.77 Million,[14] but as part of its settlement, reserved its jurisdictional and constitutional challenges.[15]

After settling the avoidance actions, the Liquidators and the Trustee jointly moved, under 11 U.S.C. § 305(a)(2), to suspend the U.S. Bankruptcy Case and turn the estate and avoidance proceeds over to the Liquidators to be repatriated and distributed in the Hong Kong Proceeding in accordance with Hong Kong law.[16] The Bank objected, raising its reserved arguments and challenging § 305(c)'s prohibition of any review of decisions under it to suspend or dismiss a case.[17] The Bank argued that it was fundamentally unfair to afford the Liquidators the option of selectively employing U.S. avoidance law when the challenged Setoff could not be avoided under Hong Kong law and where foreign creditors were subjected only to what the Bank considered the narrower avoidance provisions of Hong Kong law.[18] It also complained that the proposed distribution of the funds, once recovered, through the Hong Kong Proceeding, rather than the U.S. bankruptcy case in accordance with the U.S. priority scheme, further disadvantaged it.

The bankruptcy judge cited two early cross-border cases, decided under the Bankruptcy Act, which he concluded guided Congress' adoption of

Bankruptcy Code §§ 303–05.[19] In both cases, a company in a foreign insolvency or winding up proceeding was permitted to file a U.S. bankruptcy case, pursue avoidance actions and repatriate the proceeds for distribution in the foreign jurisdiction.[20] The *Axona* bankruptcy court concluded that Congress, aware of and influenced by these cases, intended to give foreign representatives the flexibility of choosing several options — filing a full-blown plenary case under § 303, complete with U.S. avoiding powers, commencing a limited ancillary case under § 304, or seeking the dismissal or suspension of a pending U.S. case under § 305.[21] The court further noted that the Code authorized the court to dismiss or suspend a bankruptcy case *at any time* if certain factors identified in the Bankruptcy Code favored such relief.[22]

The bankruptcy judge emphatically rejected as "an assault on the plain language of the statutory scheme," the Bank's arguments that the Liquidator's options must be construed more narrowly to be comply with constitutional constraints.[23] The court noted that, not only did § 303(b)(4) authorize the Liquidator's filing of a plenary bankruptcy case and initiation of U.S. avoidance actions, making an examination of Hong Kong avoidance law unnecessary, but said that any of Axona's creditors could have filed an involuntary petition against it and commenced a plenary case under other provisions of § 303(b).[24] Turning to § 305, the court rejected the Bank's contention that, having commenced a U.S. bankruptcy case and exercised avoiding powers through it, the Liquidator was "duty bound" to make distribution through the Bankruptcy Code's priority scheme.[25] To the contrary, the Court concluded that suspension was in keeping with the applicable factors outlined in § 304(c),[26] and that those factors adequately safeguarded the Bank's right to fair treatment.[27]

The court examined each of the factors, exploring comity principles in particular, at length, and noting a "modern trend" toward a "flexible approach which allows the assets to be distributed equitably in the foreign proceeding."[28] The Court also viewed Hong Kong law as "strikingly similar to the Code," with only "minor procedural differences" between them, thus assuring fair treatment of all claim holders,[29] and noted that Hong Kong law subjected preferences and fraudulent conveyances to avoidance.[30] The Court also rejected the Bank's "equal protection" and due process theories, finding that there was nothing objectionable about subjecting U.S. entities, as opposed to non-U.S. entities outside its *in personam* jurisdiction, to U.S. avoidance powers, the application of which the Bank should reasonably have anticipated.[31]

Accordingly, the bankruptcy judge suspended the case and allowed repatriation of most of the avoidance action proceeds to the Hong Kong Liquidators, but imposed the conditions that: (1) all administrative and other priority expenses of the U.S. case be paid through the U.S. estate; (2) the U.S. estate initially was to hold back $500,000 to complete administration; and (3) specific notice and related procedures were implemented to ensure that all U.S. creditors were able to file claims and participate in prompt distributions through the Hong Kong Proceeding.[32] On appeal, the district court affirmed the bankruptcy court's substantive decision.[33]

The overall impact of the *Axona* decision was succinctly summarized in a subsequent paper jointly presented in Hong Kong in 1991 by counsel for Chemical Bank and the Hong Kong Liquidators:

> "an abstention motion can be made at any time in the case, even at the end of a case, after avoidance powers have been successfully invoked."[34]

Axona Considered Under Current Law

To date, the authors have found no reported decisions subsequent to the enactment of Chapter 15 in which foreign insolvency representatives have attempted to employ a repatriation of avoidance action proceeds strategy like that used by the Axona Liquidators. The remainder of this article looks at how courts are likely to approach such an attempt under a hypothetical Chapter 15 proceeding, brought by an Axona-like hypothetical liquidator.

The drafters of the Model Law and Chapter 15 undoubtedly were aware of the issues raised by *Axona* relating to repatriation of avoidance action proceeds, but chose not to address them explicitly.[35] The current Bankruptcy Code thus provides no direct rule on the subject. If our hypothetical foreign representative were today to pursue the same strategy employed by the Axona Liquidators in a hypothetical Chapter 15 proceeding, many of the same competing policies the *Axona* court considered would come into play, but the controlling statutory provisions would focus the bankruptcy court on the stated goals of Chapter 15, with potentially different results.

As a preliminary matter, we consider whether the Axona Liquidators (in whose shoes our hypothetical representative presumably stands) would have received formal recognition under Chapter 15, because if they could not, it is unclear whether our hypothetical representative likewise would have standing under the new Code provisions to commence an involuntary U.S. bankruptcy case.[36] The threshold question is not a difficult one, however. The Hong Kong Proceeding in *Axona* likely would have qualified as a "foreign main proceeding" entitled to recognition under Chapter 15, because it appears that Hong Kong was the center of Axona's main interests, and Axona had assets and potential avoidance claims in the U.S.[37] Consequently, we are comfortable that our hypothetical foreign representative would receive recognition under Chapter 15 and, once recognized, could, subject to some technical requirements, commence a parallel plenary bankruptcy case ("Plenary Case").[38] Once having commenced a voluntary or involuntary Plenary Case, our hypothetical foreign representative would be entitled under Chapter 15 to participate as a party in interest and would have standing to initiate actions to pursue preferences, fraudulent transfers, certain pre-bankruptcy setoffs, or perhaps other avoidance powers under U.S. law.[39]

The hypothetical U.S. plenary estate created by the filing of the Plenary Case would not include all assets of the debtor, but would, under Chapter 15, include only those assets "within the territorial jurisdiction of the United States",[40] defined as "tangible property located within the territory of the

United States and intangible property deemed under applicable non-bankruptcy law to be located [there] including any property subject to attachment or garnishment . . .".[41] This provision, coupled with the explicit provisions for granting a recognized representative standing to exercise the Bankruptcy Code's avoidance powers, seems to leave little doubt that U.S. avoidance actions and their proceeds, would be property of the hypothetical U.S. plenary bankruptcy estate.[42]

Choice of Law

Whether a U.S. Court would apply U.S. law in the Plenary Case to transfers and setoffs like those described in the *Axona* case is debatable. Chapter 15 does not directly address the choice of law issue. One approach taken by U.S. courts in cross-border insolvencies is to apply the law of the U.S. only if the "center of gravity" of the challenged transaction is in the United States.[43] Another approach that has been advocated where there is a competing full insolvency proceeding in a foreign jurisdiction, is to abstain from enforcing U.S. avoidance law under principles of comity.[44] Questions about giving extraterritorial effect to U.S. avoidance statutes might also be raised as a limiting factor in application of U.S. law.[45]

For purposes of this article, rather than delve more deeply into complex choice of law issues, the authors simply assume that the assertion of U.S. avoidance theories results in a recovery in proceedings related to our hypothetical Plenary Case, either through a settlement or judgment, and that the recognized hypothetical foreign representative then moves to dismiss or suspend the Plenary Case and take the recoveries to the foreign main proceeding to be distributed in accordance with non-U.S. law.

Basis for dismissal

Before addressing the potential suspension or dismissal of our hypothetical Plenary Case, we look at bankruptcy dismissal principles in general. There are various provisions in the Bankruptcy Code governing dismissals of plenary cases. In Chapter 7 liquidations and Chapter 11 reorganizations, the bankruptcy court can dismiss a case for "cause," a term for which each chapter provides a non-exhaustive list of examples, but none of which relates to termination of a U.S. bankruptcy case for the purpose of distributing its assets through a foreign proceeding.[46] The examples of "cause" in a Chapter 7 case, for instance, all focus on some failure by the debtor or the estate.[47] The Chapter 11 examples of "cause" are also primarily focused on the debtor's or the estate's failures.[48]

Bankruptcy Code § 305, however, an earlier form of which was relied upon by the *Axona* court, directly addresses the dismissal or suspension of a case under circumstances where there exists a pending foreign proceeding. The section, however, is not limited to cases in which such a proceeding is involved, and applies equally to Chapter 7 and Chapter 11 cases.[49] In practice, § 305 is usually invoked at the outset of a case to persuade the court to decline to exercise jurisdiction. Once a bankruptcy case has progressed beyond its initial stages, a dismissal motion ordinarily will be brought under 11 U.S.C. §§ 707(b) or 1112(b), and a foreign insolvency representative seeking repatriation of proceeds as in our hypothetical, might, therefore, move for dismissal of the hypothetical Plenary Case under one of those provisions.[50] However, because § 305 expressly may be invoked "at any time," and specifically contemplates requests for dismissal or suspension by a foreign representative pursuant to Subsection (a)(2), it would appear to be a better fit.[51]

Indeed, even if the foreign representative moved for dismissal under the broad and undefined standard of "cause" under § 707(b) or § 1112(b), a court would likely turn for guidance to the more specific and focused criteria set forth in § 305.

Section 305 as Revised Upon Adoption of Chapter 15.

When *Axona* was decided, the standard for dismissal or suspension by a foreign insolvency representative under § 305 was different than it is today. Former § 305 provided, in relevant part:[52]

§ 305. Abstention

(a) the court, after notice and a hearing, may dismiss a case under this title, or may suspend all proceedings in a case under this title, at any time, if —

(1) the interests of creditors and the debtor would better be served by such dismissal or suspension; or

(2) (A) there is pending a foreign proceeding; and

(B) the factors specified in section 304(c) of this title warrant such dismissal or suspension.

When Chapter 15 was added to the Bankruptcy Code, § 305 was modified and now reads, in relevant part, as follows:[53]

§ 305. Abstention

(a) The court, after notice and a hearing, may dismiss a case under this title, or may suspend all proceedings in a case under this title, at any time if —

(1) the interests of creditors and the debtor would be better served by such dismissal or suspension; or

(2) (A) a petition under section 1515 for recognition of a foreign proceeding has been granted; and

(B) the purposes of chapter 15 of this title would be best served by such dismissal or suspension.

(b) A foreign representative may seek dismissal or suspension under subsection (a)(2) of this section.

* * *

Section 305 thus imposes two tests, in the disjunctive, such that satisfying either one provides sufficient grounds for dismissal or suspension.[54] As shown, the standards for "dismissal or suspension" under § 305(a)(2) were modified in part to reference and require consideration of the "purposes of Chapter 15."[55] A court considering a motion to dismiss or suspend (abstain from) a case under § 305 today would thus focus on "whether the interests of creditors and the debtor would be better served by such dismissal or suspension" *or* the purposes of Chapter 15 with respect to a recognized foreign proceeding "would be best served by such dismissal or suspension."[56]

Courts interpreting the first of the two tests — § 305(a)(1) — have usually found it to be an extraordinary remedy that should be granted sparingly, only where both the debtor and creditors would be better off as a result of such dismissal or suspension.[57] While, theoretically, a court could look to § 305(a)(1) when a foreign representative seeks dismissal or suspension of a Plenary Case,[58] that section typically is considered when there is a simultaneous out-of-court restructuring process, or merely a two-party dispute between the debtor and a single creditor.[59] Accordingly, if a foreign representative wanted to dismiss or suspend a plenary U.S. case, especially one filed by that representative for the purpose of repatriating the proceeds of U.S. avoidance actions the representative has pursued, the court would probably look to § 305(a)(2).

As noted above, the statutory touchstone to dismissal or suspension under § 305(a)(2) has changed since the *Axona* decision. And, while not drastically different, the new criteria shifts the court's focus to the purposes of Chapter 15. In addition, Chapter 15 makes explicit the requirement that certain avoidance actions may only be brought by a foreign representative in a Plenary Case[60] — a consideration that likely will cause a bankruptcy court to hesitate before dismissing or suspending a Plenary Case filed for the purpose of facilitating avoidance actions based on U.S. law. Moreover, as discussed in more detail below, bankruptcy courts appear to be limiting the circumstances under which they will authorize deviations from the priority scheme laid out in the Bankruptcy Code, such as through structured dismissals.

Consideration of a motion to dismiss or suspend a Plenary Case thus will likely start by measuring the request against the goals of Chapter 15.[61] Those goals are expressly set forth in § 1501(a) of the Code:[62]

(a) The purpose of this chapter is to incorporate the Model Law on Cross-Border Insolvency so as to provide effective mechanisms for dealing with cases of cross-border insolvency with the objectives of —
  - (1) cooperation between—
    - (A) courts of the United States, United States trustees, trustees, examiners, debtors, and debtors in possession; and
    - (B) the courts and other competent authorities of foreign countries involved in cross-border insolvency cases;
  - (2) greater legal certainty for trade and investment;
  - (3) fair and efficient administration of cross-border insolvencies that

protects the interests of all creditors, and other interested entities, including the debtor;

(4) protection and maximization of the value of the debtor's assets; and

(5) facilitation of the rescue of financially troubled businesses, thereby protecting investment and preserving employment.

The first of the articulated goals of Chapter 15 is that of "cooperation".[63] "Cooperation" is a broad concept that does not inherently favor either dismissal or continued administration of the hypothetical Plenary Case. It certainly is not synonymous with relinquishing control of distributions to a foreign representative in a foreign proceeding. Cooperation arguably could be as well or better served through a procedure that merely complements the foreign proceeding by both recovering and distributing assets through the U.S. Plenary Case. This is a particularly strong argument when one considers Bankruptcy Code § 349(a), which expressly reinstates avoided transfers upon dismissal of a case unless the court "for cause, orders otherwise."[64]

Similarly, the Chapter 15 goal of promoting "greater legal certainty for trade and investment" is neither inherently served nor disserved by the dismissal or suspension of a U.S. Plenary Case in favor of a foreign main proceeding. The goal is served by adopting a clear, readily ascertainable rule. On the one hand, the court might be inclined to serve the goal of "greater certainty," by adopting a presumption that a motion for dismissal or suspension should be denied if the purpose is to repatriate U.S. avoidance action proceeds to a foreign insolvency proceeding. Indeed, a well-articulated prohibition against the selective use of U.S. avoidance powers to generate funds to be distributed elsewhere, would provide a readily ascertainable rule. Alternatively, the courts may stop short of a fixed prohibition and impose a strong burden of proof on the foreign representative seeking dismissal or suspension.[65]

Some commentators believe legal clarity is best served by adopting and utilizing the avoidance laws of the foreign main proceeding, and they view such law as a necessary and integrated part of the forum's approach to bankruptcy or insolvency management. That was the conclusion of the Fifth Circuit for example, in the *Condor* case.[66] The court there held that "[w]hen courts mix and match different aspects of bankruptcy law, the goals of any particular bankruptcy regime may be thwarted and the end result may be that the final distribution is contrary to the result that either system applied alone would have reached."[67] The *Condor* court concluded that, in adopting Chapter 15, Congress had "confined actions based on U.S. avoidance law to full Chapter 7 and 11 bankruptcy proceeding — *where the court would also decide the law to be applied to the distribution of the estate.*"[68]

We cannot predict how courts will ultimately analyze the goal of promoting legal certainty in the context of repatriating avoidance proceeds, but there is a strong argument to be made that the goal would be best served by distributing the proceeds of U.S. avoidance actions in the same plenary U.S. bankruptcy case under which they were recovered.

The two purposes articulated in §§ 1501(a)(4) and (5) — "protection and maximization of the value of the debtor's assets" and "facilitation of the rescue" of the debtor's "financially troubled business[]" — would not be seriously implicated in a case like our *Axona*-like hypothetical, unless unusual circumstances were to come into play. Where, as in *Axona,* both insolvency proceedings are pending in jurisdictions capable of protecting assets and/or fully restructuring a business, this factor will not tip the balance toward or away from dismissal or suspension. The factor would be a critical issue, however, if the foreign insolvency proceeding were pending in a jurisdiction with underdeveloped legal processes or where theft or corruption could be expected to deplete the debtor's assets and preclude a true restructuring.

The final articulated objective of § 1501(a)(3) — to promote "fair and efficient administration . . . that protects the interests of all creditors, and other interested parties . . ." — would potentially be the most critical consideration in our hypothetical. It requires a balancing of fairness, efficiency and protection of all interests. There are many considerations that might influence the analysis under this last factor.

First, unless a foreign proceeding is relatively inefficient, a single proceeding will ordinarily be less expensive. However, as discussed above with respect to promoting legal certainty, repatriation may not be "fair" to U.S. creditors and may not safeguard their interests. In *Axona,* for example, the Bank complained that it was subjected to U.S. avoidance standards not applied to Axona's foreign-based creditors and that, to make matters worse, shifting exchange rates (presumably between the U.S., where the Bank was forced to disgorge funds and the foreign forum in which it would receive a distribution) meant that its final recovery would be artificially reduced. U.S. creditors might also be subject to additional costs of asserting or proving their claims in a foreign proceeding or as a result of some form of bias in the non-U.S. allowance and distribution process.

In many instances, moreover, there will be somewhat different priority schemes in place as between the two jurisdictions. Difference in recognizable levels of priority debt, for example, might result in a reduced distribution to U.S. creditors if the U.S. Plenary Case were dismissed or suspended.

Chapter 15 advocates administration of cross-border insolvencies in a way that protects the interests of "all creditors," but if one group of creditors is advantaged to the detriment of others, this factor would seem to lose its significance. A U.S. bankruptcy court might, however, feel obligated to assess "fair" administration by U.S. Bankruptcy Code and priority scheme standards. For example, Congress' express limitation of the use of the Bankruptcy Code's avoiding powers to plenary cases, is a strong indication that Congress wanted proceeds of U.S. avoiding powers to be administered and distributed through the U.S. plenary case and the Bankruptcy Code's priority scheme. Strategies designed to use U.S. avoidance law and foreign proceeding distribution standards, like those employed in *Axona,* thus become an "end run" around that limitation, and, in the authors' views, not one likely to be permitted by a U.S. bankruptcy court after adoption of Chapter 15, absent consent of all interested parties, or, at least, absent any objection by any interested party.

Indeed, the tactic employed in *Axona*, if attempted under Chapter 15, would likely give rise to the same sorts of competing interests and concerns as have been triggered by the recent spate of "structured dismissals," of which *In re Jevic Holding Corp.*, is the most recent to gain nationwide attention.[69] In *Jevic,* the debtor filed a voluntary chapter 11 petition when, two years after having been acquired in a leveraged buyout, it defaulted on its loan.[70] The committee of unsecured creditors pursued avoidance actions against the primary lenders, and eventually the committee, the debtor, and the debtor's primary lenders reached a settlement, proposing a "structured dismissal" of the case, upon which modest distributions were to be made to various constituencies, including general unsecured creditors, but excluding entirely a certain group of priority creditors — certain former employees holding an uncontested WARN Act claim against the debtor.[71] The Third Circuit Court of Appeals, in a decision by a divided panel, affirmed the bankruptcy court's and district court's rulings approving the settlement and authorizing the structured dismissal, even though it would result in distributions that would not comport with the Code's priority scheme.[72] In doing so, however, the Third Circuit recognized and emphasized, in strong terms, that compliance with the Bankruptcy Code's priority scheme is the most important factor in considering a structured dismissal, and that it was only the extraordinary circumstances presented, including the fact that there was "no prospect" of a successful reorganization or liquidation, that justified permitting a dismissal that did not comport with the Code priorities.[73] The Court made clear that structured dismissals could not be approved if they were devised by certain creditors or creditor groups to increase their own share of distributions at the expense of other creditors.[74] The Supreme Court has granted certiorari in the case and hopefully will provide further guidance on the propriety of such arrangements.

The same strong policy limitations on separating Code-based means of enhancing a bankruptcy estate from the priority scheme under which the proceeds are to be distributed except in the most extraordinary circumstances, furnish an additional rationale against a bankruptcy court approval of an *Axona*-like strategy. That analogy also suggests that when the use of U.S. avoidance laws and repatriation of proceeds is designed to favor or implement a foreign insolvency priority structure, the U.S. bankruptcy court would and should be hesitant to approve dismissal or suspension of the plenary case.

Conclusion

If a representative of a foreign insolvency proceeding were to file a plenary U.S. bankruptcy case and employ U.S. law to avoid and recover transfers, and then attempt, like the Liquidators in *Axona*, to suspend the bankruptcy case and repatriate the recoveries to the foreign proceeding for distribution, the U.S. Court should ordinarily sustain the objection of any creditor demonstrating any prejudice by the proposed procedure. The procedure might win bankruptcy court approval, however, if no parties objected and the court concluded that no significant harm would result to creditors of the U.S. plenary bankruptcy estate. Only then would the "purposes of chapter 15 . . . be best served by such dismissal or suspension."

NOTES:

[1]Chapter 15 (11 U.S.C. §§ 1501, et seq.), added to the Bankruptcy Code in 2005, is the U.S. version of the Model Law on Cross-Border Insolvency ("Model Law") promulgated by the United Nations Commission on International Trade Law ("UNCITRAL").

[2]In re Axona International Credit & Commerce Limited, 88 B.R. 597 (Bankr. S.D.N.Y. 1988), (hereinafter, "*Axona*"), *aff'd.,* 115 B.R. 442 (S.D. N.Y. 1990), *appeal dismissed sub nom.,* Chemical Bank v. Togut (In re Axona Int'l. Credit & Commerce, Ltd.), 924 F.2d 31 (2d Cir. 1991).

[3]*See* 11 U.S.C. §§ 303 to 305 (1988). Section 304 was repealed and §§ 303 and 305 were amended in 2005, when Chapter 15 was adopted.

[4]There are two basic models for multi-national insolvency proceedings — universalism and territorialism. According to Professor Lynn LoPucki, a pure universalistic approach "refers to a system in which a single bankruptcy court controls the administration of the debtor's assets and makes the distributions to creditors worldwide" and at the other end of the spectrum, a territorial approach "refers to a system in which each country administers the assets within the country's own territoriality and recognizes other countries right to do the same." Lynn M. LoPucki, *Cooperation in International Bankruptcy: A Post — Universalist Approach*, 84 Cornell L. R. 696, pp. 704, 792 (March, 1999).

[5]*See,* In re Jevic Holding Corp., 787 F.3d 173 (3rd Cir. 2015) (affirming a dismissal of a chapter 11 bankruptcy case pursuant to an order that provided for creditor distributions in a manner that did not comport with the Bankruptcy Code's priority scheme). The decision is on appeal to the U.S. Supreme Court.

[6]Professor Jay Westbrook, who generally supports the principles of universalism, describes the Model Law and Chapter 15 as "modified universalism", i.e., "[i]t accepts the central purpose of universalism, that assets should be collected and distributed on a worldwide basis, but reserves to local courts discretion to evaluate the fairness of the home-country procedures and to protect the interests of local creditors." Jay Lawrence Westbrook, *Choice of Avoidance Law in Global Insolvencies*, 18 Brooklyn, J. Int'l. L. 499, 517 (1991). *See also* Jay Lawrence Westbrook, *Universalism and Choice of Law*, 23 Penn State Int'l. L. R. 625 (2005), Jay Lawrence Westbrook, *Avoidance of Pre-Bankruptcy Transactions in Multinational Bankruptcy Cases*, 42 Texas Int'l. L. J. 899 (2007).

[7]*Axona*, 88 B.R. 597, 599

[8]*Axona,* 88 B.R. at 599–600.

[9]*Id.*

[10]*Id.* at 600.

[11]*Id.,* at 601.

[12]*Id.*, at 601.

[13]*Id.,* at 601–03.

[14]*Id.*, at 602.

[15]*Id.*

[16]*Id.*, at 602.

[17]*Id.,* 88 B.R. at 603. At the time, 11 U.S.C. § 305(c) provided that orders dismissing a case or suspending proceedings in a case were not reviewable.

[18]*See Axona*, 88 B.R. at 603–604, 606, discussing Chemical Bank contended, among other things, that the avoidance of the Setoff was an "impermissible taking." *Id.*

[19]*Axona,* 88 B.R. at 603–606*, citing*, In re Banque de Financement S.A., 568 F.2d 911 (2d Cir. 1977) *("Finabank")*, and In re Israel-British Bank (London) Ltd., 536 F.2d 509 (2d Cir. 1976) (*"IBB"). See, generally,* Kurt H. Nadelman*, Israel-British Bank (London) Ltd.: Yet Another Trans-Atlantic Crossing*, 52 Am. Bankr. L.J. 369 (1978).

[20]*See Finabank*, 568 F.2d at 918–20; *IBB,* 536 F.2d at 511.

[21]*Id.* 88 B.R. at 606.

[22]*Id.*, *citing,* 11 U.S.C. § 305(a).

[23]*Axona,* 88 B.R. at 604. The court also characterized Chemical Bank's constitutional arguments as "nebulous." *Id.* at 603.

[24]*Id.* at 606–07.

[25]*Id.* at 607–08.

[26]Section 304, which was repealed at the time Chapter 15 was added to the Bankruptcy Code, provided in relevant part as follows:

> In determining whether to grant relief under subsection (b) of this section, the court shall be guided by what will best assure an economical and expeditious administration of such estate, consistent with—

(1)just treatment of all holders of claims against or interests in such estate;

(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 such estate;

(4)distribution of proceeds of such estate substantially in accordance with the order prescribed by this title;

(5)comity; and

(6)if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns. ¶ 11 U.S.C. § 304(c) (1988).

[27]*Id.* at 607–08.

[28]*Axona*, 88 B.R. at 608–09 (internal citations and quotations omitted).

[29]*Id.* at 610.

[30]*Id.* at 610. The parties disputed whether the transfers to the Bank were subject to avoidance under the Hong Kong law, but the court never decided that issue.

[31]*Id.* at 615–617.

[32]*Id.*, 88 B.R. at 618–19.

[33]In re Axona Int'l. Credit & Commerce Ltd., 115 B.R. 442, 447–48. It rejected, with little discussion, the Bank's argument that, suspending the bankruptcy case was tantamount to dismissal and thus ran afoul of 11 U.S.C. § 349(b), which requires revesting of voided transfers upon dismissal. *Id.* The district court also held that it had implicit authority to review the bankruptcy court's suspension or dismissal orders notwithstanding § 305(c). *Id.* The Court of Appeals agreed with that conclusion, holding that subsequent amendments to § 305(c) ensured one level of review by an Article III court — the district court — which removed any constitutional infirmity, and therefore dismissed the appeal for lack of appellate jurisdiction. *Chemical Bank v. Togut,* 924 F.2d at 35.

[34]The paper was presented at a conference of the International Bar Association's Section on Business Law and was later published in the Bankruptcy Developments Journal. *See* Henry Lewis Goodman, Mark P. Friedman & William H. Schrag, *Use of United States Bankruptcy Law in Multinational Insolvencies: the Axona Litigation — Issues, Tactics, and Implications for the Future,* 9 Bankr. Developments J. 19 (1992).

[35]Judge Burton Lifland, the bankruptcy judge in *Axona,* was one of the drafters of Chapter 15. All of the proceedings in *Axona* had concluded in 1991. The Model Law was published in 1997, and Chapter 15 was enacted in 2005.

[36]*Compare* 11 U.S.C. §§ 303(b)(4) *with* 11 U.S.C. § 1511. Together, these sections do not make it absolutely clear that an involuntary plenary case can be filed by a non-recognized foreign representative. In *dicta* in In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd., 374 B.R. 122, 132–33 (Bankr. S.D. N.Y. 2007), Judge Lifland concluded that 11 U.S.C. § 303(b)(4) permits unrecognized representatives to file involuntary cases. That view is probably correct, because there is no sound policy for the opposing view and any statutory inconsistency appears to be a slight oversight created by the addition of Chapter 15.

[37]*See* 11 U.S.C. § 1502(4) (defining "foreign main proceeding"); and §§ 1515-1517 (governing recognition of a foreign proceeding). A recent decision holds that a foreign insolvency representative must demonstrate the debtor has assets in the U.S. to obtain recognition under Chapter 15. *See* Drawbridge Special Opportunities Fund, LP v. Barnet (In re Barnet), 737 F.3d 238 (2d Cir. 2013). This decision has generated controversy. *See* Daniel M. Glosband and Jay Lawrence Westbrook, Opinion: No Debtor "Presence" is Required for Chapter 15 Recognition, American Bankruptcy Institute J. (May 2015), p. 24 (contending that *Barnet* was erroneously decided); 8 Collier on Bankruptcy (16th ed.) ¶ 1501.03[3] at p. 1501–8. Even if a court followed the Second Circuit's reasoning in *Barnet*, however, the existence of avoidance actions against defendants in the U.S. would likely overcome resistance to recognition. *See* 11 U.S.C. §§ 1528, 1502(8).

[38]*See* 11 U.S.C. § 1511(a).

[39]*See* §§ 1512 and 11 U.S.C. § 1523(a). Presumably, the representatives of the estate in a full plenary proceeding would likewise have standing to bring avoidance actions. The Axona Liquidators, of course, did not have the advantage of an express, statutory grant of standing, but the appointed Trustee worked with them to bring the actions. It is possible that in an analogous case brought under Chapter 15, a party wanting to keep the proceeding exclusively in the foreign jurisdiction, such as the transferee of a transfer voidable under U.S. law, might seek dismissal or suspension at the outset of a plenary case under 11 U.S.C. § 305 as a tactical matter.

[40]11 U.S.C. § 1528. The estate also includes "to the extent necessary to implement cooperation and coordination under sections 1525, 1526, and 1527, to other assets of the debtor that are within the jurisdiction of the court under sections 541(a) of this title, and 1334(e) of title 28, to the extent that such other assets are not subject to the jurisdiction and control of a foreign proceeding that has been recognized under this chapter."

[41]11 U.S.C. § 1502(8).

[42]*See* Krys v. Farnum Place, LLC, 768 F.3d 239, 244–45 (2d Cir. 2014) (claim against U.S. insolvency estate was in U.S. territorial jurisdiction); In re British Am. Ins. Co. Ltd., 488 B.R. 205, 227 (Bankr. S.D. Fla. 2013) (claim against fiduciaries of debtor was in U.S. territorial jurisdiction).

[43]*See,* for example, the bankruptcy court's decision in In re Maxwell Communications PLC, 170 B.R. 800, 808–09 (Bankr. S.D.N.Y. 1994) *affd.,* 186 B.R. 807 (S.D.N.Y. 1995), *aff'd.,* 93 F.3d 1036 (2d Cir. 1996); and In re Florsheim, 336 B.R. 126, 131.(Bankr. N.D. Ill. 2005).

[44]*See, e.g.,* In re Maxwell Communications Corporation PLC, 93 F.3d 1036, 1050–1054 (2d Cir. 1996).

[45]*See, e.g.,* In re French, 440 F.3d 145–152 (4th Cir. 2006) (applying U.S. avoidance law

to recover non-U.S. real estate for U.S. bankruptcy case). Choice of state avoidance law is also a complex issue in U.S. bankruptcies when the U.S. bankruptcy estate relies on an alternate theory of incorporating state law under 11 U.S.C. § 544(b). *See,* for example, Edwin Smith, The 2014 Amendments to the Uniform Voidable Transactions Act (and, before the amendments, known as the Uniform Fraudulent Transfer Act), 46 Uniform Commercial Code Law Journal, 245, 251 (July, 2015).

[46]*See* 11 U.S.C. § 707(a); and 11 U.S.C. §§ 1112(b)(1), (b)(4).

[47]11 U.S.C. § 707(a)(1)–(3).

[48]11 U.S.C. § 1112(b)(4).

[49]11 U.S.C. § 305. Even though § 305 is titled "Abstention," it refers only to "dismissal" or "suspension" as potential forms of relief, and the term "abstention" is nowhere to be found.

[50]*See, e.g.,* In re RHTC Liquidating Co., 424 B.R. 714, 722 (Bankr. W.D. Pa. 2010) ("*RHTC Liquidating*") (addressing motion for dismissal of case by foreign representative); In re Northshore Mainland Services, Inc., 537 B.R. 192 (Bankr. D. Del. 2015) (addressing creditors' motion to dismiss chapter 11 cases filed by debtors under both § 1112(b) and § 305(a)).

[51]Interestingly, a dismissal under § 305 would be subject to only one level of review whereas a dismissal under the other sections would be subject to two. *See* 11 U.S.C. § 305(c). This single level of review might be attractive to our hypothetical foreign representative. In a circuit with a Bankruptcy Appellate Panel, the number of available levels of review procedures would be more uncertain.

[52]11 U.S.C. § 305(a) (1998).

[53]11 U.S.C. § 305(a).

[54]*See, e.g., RHTC Liquidating,* 424 B.R. at 720 (describing the section as two alternative tests, either of which, if met, will support dismissal).

[55]The factors in repealed § 304(c), in turn, were incorporated, with only some small modifications, into Chapter 15 — specifically, 11 U.S.C. § 1507 — as the factors courts should consider in determining whether a foreign representative can obtain "additional assistance" in an ancillary case.

[56]11 U.S.C. § 305(a).

[57]*See,* In re Globe Communicacoes e Partiapacoes S.A., 317 B.R. 235, 255 (S.D. N.Y. 2004) (citing cases); In re RHTC Liquidating Co. 424 B.R. 714, 720 (Bankr. W.D. Pa. 2010).

[58]*See,* for example, In re RHTC Liquidating Co., 424 B.R. 714, (Bankr. W.D. Pa. 2010) in which the U.S. Bankruptcy Court denied a motion filed by the recognized foreign representative of a Canadian main proceeding to dismiss an involuntary case filed by creditors. There, the court considered but rejected the motion to dismiss under both §§ 305(a)(1) and (2). *Id.* at pp. 721–728. In re Compania de Alimentos Fargo S.A., 376 B.R. 427 (Bankr. S.D. N.Y. 2007).

[59]*See* 2 Collier on Bankruptcy (16th Ed.) ¶ 305.02 at p. 305-6-10.

[60]11 U.S.C. §§ 1521(a)(7), 1523(a). Note, however, that Bankruptcy Code § 549, prohibiting post-petition transfers, does apply in a Chapter 15 ancillary case upon recognition of a foreign representative, and an action to avoid post-petition transfers is not prohibited under § 1521(a)(7). *See,* 11 U.S.C. §§ 1520(a)(2), 1521(a)(7). *And see,* In re Loy, 432 B.R. 551, 563 (E.D. Va. 2010) (finding that, for purposes of determining whether a foreign representative may avoid a transfer under § 549, the "commencement of the case" is the date on which a petition for recognition of a foreign insolvency proceeding is filed). In addition, one bankruptcy court has held that relief to recover a setoff under § 553(b) is not prohibited in a chapter 15 case by § 1521(a)(7). *See,* In re Awal Bank, BSC, 455 B.R. 73, 88 (Bankr. S.D. N.Y. 2011).

[61]Note that it is possible that a foreign representative might attempt to avoid transfers

and recover proceeds under a theory other than under the provisions of the Bankruptcy Code, such as, for example, under the law of the foreign country in which the foreign proceeding. *See, e.g.,* In re Condor Insurance Ltd., 601 F.3d 319 (5th Cir. 2010), in which the Fifth Circuit found that a foreign representative could pursue avoidance actions based on the law of the foreign insolvency proceeding without initiating a plenary U.S. bankruptcy case. The analysis provided herein would not apply to a proposed dismissal of an ancillary proceeding under Chapter 15 where the proceeds to be repatriated had been generated solely through application of the law of the foreign proceeding.

[62]11 U.S.C. § 1501(a).

[63]11 U.S.C. § 1501(a)(1).

[64]11 U.S.C. § 349(b).

[65]A high burden of proof imposed upon a foreign representatiave seeking dismissal or suspension would also be consistent with § 349(a)'s requirement of "cause" for not reinstating avoided transfers upon dismissal of a case. 11 U.S.C. § 349(a).

[66]*See,* In re Condor Insurance Ltd., 601 F.3d 319. The defendant in the *Condor* adversary had argued that avoidance actions were only available in a plenary bankruptcy case brought under Chapter 7 or Chapter 11 of the Code. *Id.,* 601 F.3d at 321. Rejecting that view, the Fifth Circuit concluded that "congress did not intend to restrict the powers of the U.S. court to apply the law of the country where the main proceeding pends," and that, under prior § 304, "avoidance actions under foreign law were permitted when foreign law applied and would provide for such relief." *Id.,* at 327–28, *citing,* In re Metzeler, 78 B.R. 674 (Bankr. S.D. N.Y. 1987). The *Condor* court also rejected what it viewed as the *Axona* bankruptcy court's apparent suggestion that bankruptcy courts had discretion to permit the use of Bankruptcy Code avoidance powers in a § 304 ancillary proceeding. *In re Condor Insurance Ltd.*, 601 F.3d at 328, n. 49, *distinguishing, Axona*, 88 B.R. at 607, n.17.

[67]*In re Condor Insurance Ltd.,* 601 F.3d at 326.

[68]*Id.,* 601 F.3d at 327. (emphasis added)

[69]In re Jevic Holding Corp., 787 F.3d 173, 181 and n. 5 (noting the growing trend of using structured dismissals).

[70]In re Jevic Holding Corp., 787 F.3d 175.

[71]In re Jevic Holding Corp., 787 F.3d 177.

[72]In re Jevic Holding Corp., 787 F.3d 180 (holding that "bankruptcy courts may, in rare instances . . . approve structured dismissals that do not strictly adhere to the Bankruptcy Code's priority scheme").

[73]In re Jevic Holding Corp., 787 F.3d 184–85 (noting that deviation from the Code's priorities could only rarely be justified.)

[74]In re Jevic Holding Corp., 787 F.3d 184. There was a strong dissent, contending that the litigation that led to the settlement was property of the estate and that the proceeds must also be considered estate property for which a "class-skipping" arrangement could not be approved. *Id.,* 787 F.3d at 188, Circuit Judge Scirica, dissenting.