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Recent Decisions in *Saad*, *Metcalfe*, and *Condor*: Chapter 15 Re-Energized

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In this article, the authors discuss the Saad*,* Metcalfe*, and* Condor *decisions which stand for the propositions that Chapter 15 may not be as difficult to enter as might have been perceived immediately following the* Bear Stearns *and* Basis Yield Alpha Fund *decisions and that, once in Chapter 15, a foreign debtor and third parties may be able to obtain substantial protection under the U.S. bankruptcy system.*

In the wake of the 2008 decisions from the Southern District of New York bankruptcy court in *Bear Stearns* and *Basis Yield Alpha Fund*, which limited the ability of an offshore fund to have its foreign liquidation recognized under Chapter 15 of the U.S. Bankruptcy Code, the scope and utility of Chapter 15 was unclear. However, decisions from the first quarter of 2010 in the *Saad*, *Metcalfe*, and *Condor* cases indicate that the barriers for entry into Chapter 15 are surmountable, and that Chapter 15 protection remains significant. Decided in the context of a recent increase in the number of Chapter 15 filings, these decisions may themselves

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encourage greater use of Chapter 15 in New York (the more traditional venue for recognition of foreign insolvency proceedings), Delaware, and elsewhere.

THE ORIGINS AND SUBSTANCE OF CHAPTER 15

Enacted as part of the Bankruptcy Abuse Prevention and Consumer Protection Act ("BAPCPA") in 2005, Chapter 15 was added to the U.S. Bankruptcy Code to encourage cooperation between the United States and foreign countries with respect to cross border insolvency cases. Chapter 15 is substantially identical to a Model Law proposed by the United Nations Commission on International Trade Law ("UNCITRAL") to address the same subject. Chapter 15 replaced former U.S. Bankruptcy Code Section 304 and provides a more comprehensive scheme for how U.S. bankruptcy courts will address cross border cases. In basic terms, Chapter 15 has three components: (1) the recognition of a foreign insolvency proceeding by the U.S. bankruptcy court; (2) the grant of relief by the U.S. bankruptcy court with respect to U.S. assets and creditors, in support of the foreign insolvency proceeding; and (3) the cooperation of the U.S. bankruptcy court and the foreign court overseeing the foreign proceeding to administer the debtor's insolvency consistently across national boundaries.

BEAR STEARNS AND *BASIS YIELD ALPHA FUND*: CHAPTER 15 LIMITED

Reported decisions in Chapter 15 cases were not common in the first years following the statute's enactment. The few decisions focused on the determination of whether a foreign proceeding would be recognized by a U.S. bankruptcy court — that is, whether the foreign proceeding met the standards for the subsequent grant of relief by the U.S. bankruptcy court in support of the foreign proceeding. In particular, in two widely noted 2008 decisions from the Southern District of New York bankruptcy court, the court declined to recognize the foreign insolvency proceedings of offshore hedge funds undergoing liquidations in the Cayman Islands.

In *Bear Stearns*,[1] the Southern District of New York bankruptcy court addressed Chapter 15 petitions filed to recognize the Cayman Islands liquidation proceedings for two offshore hedge funds managed by Bear Stearns. Although no party objected to recognition, and despite a presumption favoring recognition, the bankruptcy court performed its own analysis of whether the funds' assets and operations in the Cayman Islands were sufficient to support recognition of the Cayman proceeding either as a foreign main proceeding (if the funds had their center of main interests ("COMI") in the Cayman Islands) or as a foreign nonmain proceeding (if the funds satisfied the lesser standard of having an establishment in Cayman). The bankruptcy court ruled — and the district court affirmed on appeal — that recognition should be denied on the facts of this case, because the funds had only a nominal presence in the Cayman Islands and had most of their assets and operations in the U.S. As such, the courts essentially required that any bankruptcy case for a fund primarily located in the U.S. must be filed under Chapter 7 or Chapter 11 of the U.S. Bankruptcy Code, and that the more streamlined process for obtaining relief under Chapter 15 was not available. During the same time period, the Southern District of New York bankruptcy court in *Basis Yield Alpha Fund*[2] denied, for similar reasons, another Chapter 15 petition for recognition of a Cayman liquidation proceeding for an offshore hedge fund.

RECENT DECISIONS IN *SAAD*, *METCALFE*, AND *CONDOR*: CHAPTER 15 RE-ENERGIZED

As the five year anniversary of Chapter 15's enactment nears, and as global economic conditions remain challenging, there has been an increase of Chapter 15 cases in the Southern District of New York and Delaware.[3] Also, a number of new reported decisions have made significant additions to Chapter 15 jurisprudence. Specifically, three decisions in the first quarter of 2010 may signal a change in the use of Chapter 15 moving ahead. First, a recent decision in *Saad*[4] appears to have reopened the door for Cayman funds to use Chapter 15 — at least in the Delaware bankruptcy court. Second, recent decisions from the Southern District of New York bankruptcy court in *Metcalfe*[5] and from the Fifth Circuit Court of Appeals

in *Condor* reaffirm that Chapter 15 can bring meaningful additional relief to a cross border insolvency.

In *Saad*, the bankruptcy court considered yet another Chapter 15 petition for recognition of a foreign main proceeding of a Cayman fund. But in this case, the bankruptcy court found that the fund's center of main interests was in Cayman, and that the foreign insolvency proceeding in Cayman would be recognized as a foreign main proceeding — opening the door for the grant of Chapter 15 relief as to U.S. assets and creditors of the fund. By contrast to the *Bear Stearns* and *Basis Yield Alpha Fund* decisions in New York, the Delaware bankruptcy court in *Saad* found that the fund's management and administration activities were not being conducted anywhere other than Cayman, and that the estimated value of the fund's investments in the Cayman Islands exceeded the estimated value of its investments anywhere else in the world (although substantial investments were made in the U.S.). While these facts distinguish *Saad* from the New York decisions, the *Saad* decision may also signal a more flexible standard for Chapter 15 recognition in Delaware.

In *Metcalfe*, the Southern District of New York bankruptcy court was presented with a Chapter 15 petition for recognition of a Canadian insolvency proceeding under the Canadian Companies' Creditors Arrangement Act. While the recognition of the foreign proceeding as a foreign main proceeding in this case was straightforward — the debtor was a Canadian company with primary operations in Canada — the potential relief that the foreign debtor sought upon recognition was remarkable. The Canadian Monitor representing the foreign debtor in the Chapter 15 case requested that the U.S. bankruptcy court enter an order enforcing in the U.S. provisions of a Canadian court order containing broad third party releases. Those releases provided the released parties, which included any participant in the CAN$32 billion Canadian asset-backed commercial paper ("ABCP") market, with protection "from liability and actions on account of any and all past, present and future claims…in any way related to the third-party ABCP market in Canada."[6] The propriety of the releases was strenuously disputed in the Canadian proceedings, but ultimately the Canadian court approved them on the basis that they were "reasonably connected to the proposed restructuring," which was the largest restructuring

in Canadian history and which was ultimately approved by a nearly unanimous vote of the creditors.

The Monitor urged the U.S. bankruptcy court to accept the findings of the Canadian courts and to enforce the releases on the grounds that the releases would "pass muster under the rigorous standards for release and injunction provisions established by the Second Circuit."[7] But the U.S. court did not rest its decision on whether the releases would have been approved in a U.S.-centered bankruptcy, under what is likely a more stringent standard for such releases than that applied by the Canadian court. Instead, the U.S. bankruptcy court found that "principles of enforcement of foreign judgments and comity in chapter 15 cases strongly counsel approval of enforcement in the United States of the third-party non-debtor release and injunction provisions included in the Canadian Orders, *even if* those provisions could not be entered in a plenary chapter 11 case."[8] Because the U.S. bankruptcy court was convinced that the judicial process leading up to the Canadian order was fair, the releases were enforceable in the U.S. under Chapter 15, notwithstanding that the substantive law for releases in the U.S. under Chapter 11 might have produced a different result.

In *Condor*, the Fifth Circuit Court of Appeals reversed the rulings of the Southern District of Mississippi bankruptcy court and district court on the issue of whether a Chapter 15 proceeding may be used to pursue foreign law avoidance actions against defendants and assets in the U.S. The Fifth Circuit allowed the Joint Official Liquidators of Condor Insurance, a Nevis (Lesser Antilles) company, to pursue Nevis law fraudulent transfer actions to recover $313 million in transfers made by the foreign debtor. The Liquidators alleged that Condor Insurance had made the transfers to an affiliate in the U.S. for the purpose of placing the transferred assets out of the reach of the Nevis entity's creditors. There were two hurdles to the U.S. court permitting the use of Chapter 15 for the prosecution of the fraudulent transfer action. First, Chapter 15 expressly excludes from its scope of relief the prosecution of fraudulent transfer actions under Sections 544 and 548 of the U.S. Bankruptcy Code. Second, Condor Insurance, as a foreign insurance company, was not an eligible debtor in the U.S. under Chapter 7 or Chapter 11, and, accordingly, could not have pursued fraudulent transfer actions under those chapters. However, the Fifth

Circuit overcame both hurdles, ruling that Condor Insurance was an eligible debtor under Chapter 15, even if it could not be a debtor under Chapter 7 or Chapter 11, and that pursuit of the foreign fraudulent transfer action was appropriate under Chapter 15, because it was not a U.S.-law action expressly excluded under Chapter 15. In sum, the Fifth Circuit allowed the foreign Liquidators to use Chapter 15 to pursue a *foreign* cause of action in the U.S. bankruptcy court, even where the equivalent U.S. cause of action could not have been pursued under Chapter 7, 11, or 15.

THE BOTTOM LINE

The *Saad*, *Metcalfe*, and *Condor* decisions stand for the propositions that Chapter 15 may not be as difficult to enter as might have been perceived immediately following *Bear Stearns* and *Basis Yield Alpha Fund* and that, once in Chapter 15, a foreign debtor and third parties may be able to obtain substantial protection under the U.S. bankruptcy system. A message from the U.S. bankruptcy court in the 2008 decisions was that debtors with significant ties to the U.S. must file plenary U.S. bankruptcies under Chapter 7 or Chapter 11, and therefore must follow the substantive bankruptcy laws of the U.S. By contrast, a message from these early 2010 decisions may be that debtors can use Chapter 15 to enforce in the U.S. certain protections under foreign law that may not be available through Chapter 7 or Chapter 11 filings. More generally, these 2010 decisions evidence an invigorated flexibility in entering, and obtaining relief under, Chapter 15.

NOTES

[1] *In re Bear Stearns High-Grade Structured Credit Strategies Master Fund, Ltd.*, 374 B.R. 122 (Bankr. S.D.N.Y. 2007); *aff'd*, 389 B.R. 325 (S.D.N.Y. 2008).

[2] *In re Basis Yield Alpha Fund (Master)*, 381 B.R. 37 (Bankr. S.D.N.Y. 2008).

[3] In 2008, there were 17 cases filed under Chapter 15 in the Southern District of New York and 14 in Delaware; in 2009, those numbers increased to 36 and 25, respectively, through September 30. *See* U.S. Courts Statistical Reports, Bankruptcy Statistics, Calendar Year by Chapter, available at http://www.

uscourts.gov/bnkrpctystats/statistics.htm#june.

[4] *In re Saad Invs. Fin. Co. (No. 5) Ltd.*, Third Revised Order Recognizing Foreign Proceeding, No. 09-13985 (Bankr. D. Del. Feb. 3, 2010).

[5] *In re Metcalfe & Mansfield Alternative Invs., et al.*, 421 B.R. 685 (Bankr. S.D.N.Y. 2010).

[6] 421 B.R. at 692.

[7] *Id.* at 694.

[8] *Id.* at 696 (emphasis added).