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Federal Bar Association

Bankruptcy Section Newsletter
June 2011

This newsletter is published by the Federal Bar Association, Bankruptcy Section, for the Western District of Michigan. Prepared by lawyers with busy practices, every effort is made to publish on a quarterly basis. For your records, here are the dates of newsletters for the recent past: December, 2010, June 2010, October 2009, June 2009, March 2009, October 2008, July 2008, April 2008, January 2008, October 2007, August 2007, April 2007, January 2007, October 2006, July 2006, February 2006, October 2005, June 2005, February 2005, October 2004, May 2004, January 2004, October 2003, July 2003, April 2003 and January 2003.

To view this email in its best format (green and tan background, with the tree logo at the top), we suggest that you set your internet software to "HTML" view. On versions of INTERNET EXPLORER, click "tools" then "options" then "environment". Under the "views" tab, click "default read view" and set to "HTML", instead of "plain text".

IN THIS ISSUE

Editor's Note

The membership is invited to submit short articles addressing notable recent developments. Submissions need not be filled with citations or considered "law review" caliber. Rather, mere observations or short analyses of relevant issues and/or creative arguments, whether set forth in pleadings or published/unpublished decisions, are welcome.

In addition, members should contact the editor if they wish to post announcements or other news (e.g., promotions, awards, appointments, and firm mergers) in the Announcements section of the upcoming newsletter.

This edition of the newsletter will be my last as editor. I wish my successor a great deal of success and look forward to future editions.

Letter from the Chair

June 14, 2011
Norman C. Witte, Chair

It is with considerable sadness that the bankruptcy bar mourns the passing of Denni Chamberlain on June 9th. Denni served as Judge Hughes' career law clerk and before that served in the same capacity for Judge Howard. His pleasant demeanor and keen wit will be greatly missed.

Of course, this time of year the big news is the FBA Bankruptcy Section seminar which is just around the corner. Fran Ferguson, our event chair, and Judge Dales, our education chair, have been working hard to make this event both informative and entertaining. Please register early, and take advantage of our new on-line registration system.

In coming months we will be discussing possible new members to add to the Steering Committee. We are interested in hearing from members throughout the Western District. In addition to the Steering Committee, there are plenty of other opportunities to serve, whether you would like to work on the newsletter, help organize the annual seminar, or lend a hand with holiday events. If you have an interest in becoming more involved with the Bankruptcy Section please drop me an email or give me a call. I can be reached at ncwitte@wittelaw.com or (517) 913-5104.

A gentle reminder: all members of the Bankruptcy Section are supposed to be members of the FBA for the Western District of Michigan. Dues, at $35 are cheap (less than a tank of gas!) and it's easy to register on-line at https://www.westmichiganfederalbar.org/FBAApp/. The FBA has many worthwhile programs besides ours, many of which would be helpful even to attorneys who practice bankruptcy law

Quick Links...

United States Bankruptcy Court, Western District of Michigan

Local filing statistics

United States Trustee Program, including means test tables and other BACPA data

United States Bankruptcy Courts

Chapter 13 Trustee Brett N. Rodgers

Chapter 13 Trustee Mary K. Viegelahn Hamlin

Federal post judgment rate of interest

State Bar of Michigan

American Bankruptcy Institute

National Association of Bankruptcy Trustees

National Conference of Bankruptcy Judges

National Association of Consumer Bankruptcy Attorneys

National Association of Chapter 13 Trustees

Federal Bar Association of Western Michigan

Pro bono procedures and client retainer agreement exclusively. In addition, members get their names and addresses listed on the FBA's web page. At $35, that's pretty cheap marketing. . . .

Last, but certainly not least, I wish to express the great appreciation of all members of the Steering Committee to John Gregg, who is stepping down as our newsletter editor. Editing the newsletter is a time-consuming and often thankless job, but is vital to our organization. John, thank you for a job well-done. Your time and efforts are appreciated.

News from the Bankruptcy Court

A. Pilot Program - Telephonic Appearances before Judge Hughes (Grand Rapids Motion Days)

Judge Hughes will be implementing a pilot program to test the viability of telephonic court appearances through CourtCall (an independent conference call company). Attorneys interested in participating will be permitted to appear telephonically before Judge Hughes during any of his regularly scheduled Grand Rapids motions days beginning June 9, 2011. For more information, please visit http://www.miwb.uscourts.gov/cms/index.php/home/court-news/.

B. Bankruptcy Best Practices Seminar 2011

The United States Trustee for the Western District of Michigan and the Chapter 13 and 7 Panel Trustees are offering workshops for attorneys who practice bankruptcy. For more information regarding dates and registration, please visit http://www.miwb.uscourts.gov/cms/index.php/home/court-news/.

Articles

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ELIGIBILITY OF MICHIGAN MUNICIPALITIES FOR RELIEF UNDER CHAPTER 9 OF THE BANKRUPTCY CODE

In the last decade, Michigan has experienced a significant erosion of its once thriving manufacturing base, a dissipation of

New dollar amounts in bankrutpcy

Information on reporting bankrutpcy fraud skilled laborers, and an inability to attract new industries, among other things. When General Motors Corporation and Chrysler LLC filed for bankruptcy and numerous financial institutions collapsed under the weight of toxic mortgage debt and other risky investments, many commentators and pundits labeled those events as the climax of the United States' financial distress.

Recently, focus has shifted to the financial status of state and local governments. In that regard, it is no secret that the financial resources of both state and local governments have been exposed to reveal declining tax revenues, increasing health care obligations, poor investments, incongruous salaries of municipal employees and underfunded pension plans. As a result, local governments and other municipal entities have expressed their desire to file for relief under Chapter 9 of the Bankruptcy Code. However, as discussed in greater detail below, municipalities are not eligible for Chapter 9 absent specific statutory authority under applicable state law, among other things.

The purpose of this Article is to provide an overview of the elements that must be satisfied in order for a Michigan municipality to be eligible to file for relief under Chapter 9 of the Bankruptcy Code.

A. Threshold Requirements Under 11 U.S.C. § 109(c)

Section 109 of the Bankruptcy Code sets forth the eligibility requirements for a "person" or "municipality" to file for relief under the Bankruptcy Code.[1] With respect to municipalities, section 109(c) provides that an entity may be a debtor under Chapter 9 if and only if such entity:

(1) is a municipality;
(2) is specifically authorized, in its capacity as a municipality or by name, to be a debtor under such chapter by State law, or by a governmental officer or organization empowered by State law to authorize such entity to be a debtor under such chapter;
(3) is insolvent;
(4) desires to effect a plan to adjust such debts; and
(5) (A) has obtained the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;
(B) has negotiated in good faith with creditors and has failed to obtain the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;
(C) is unable to negotiate with creditors because such negotiation is impracticable; or
(D) reasonably believes that a creditor may attempt to obtain a transfer that is avoidable under section 547 of this title.

11 U.S.C. § 109(c).

The burden is on the debtor to establish eligibility under section 109(c) of the Bankruptcy Code. *In re Pierce County Hosing Authority*, 414 B.R. 702, 710 (Bankr. W.D. Wash. 2009); *In re Valley Health Systems*, 383 B.R. 156, 161 (Bankr. C.D. Cal. 2008); *In re City of Bridgeport*, 129 B.R. 332, 339 (Bankr. D. Conn. 1991). The burden is not so stringent though, as to deny access to relief in furtherance of the Bankruptcy Code's underlying policies. *Hamilton Creek Metro. Dist. v. Bondholders Colo. Bondshares (In re Hamilton Creek Metro. Dist.)*, 143 F.3d 1381, 1384 (10th Cir. 1998); *see In re City of Vallejo*, 408 B.R. 280, 289 (Bankr. N.D. Cal. 2009) (rejecting clear and convincing burden of proof).

On its face, section 109(c) seems relatively straightforward. However, as discussed below, satisfying the threshold elements for relief under Chapter 9 can be quite complex.

1. Characterization as a "Municipality"

With respect to the first requirement, the debtor must be a "municipality," which is defined by section 101(40) as a "political subdivision or public agency or instrumentality of a state." 11 U.S.C. § 101(40). In general, municipalities that can file for relief under Chapter 9 include cities, counties, school districts, townships, hospitals, sanitary districts and revenue generating entities such as authorities formed under State law that provide services paid for by users as opposed to taxpayers.

Courts have examined the following factors, among others, in order to determine whether an entity is a municipality:

(i) whether the entity serves a public function;
(ii) whether the nature of the state or municipal control over the entity includes the direct management of the entity's finances; and
(iii) whether the state categorizes or refers to the entity under state law as a municipal entity as opposed to a private entity.

See, *e.g.*, *In re Las Vegas Monorail Co.*, 429 B.R. 770 (Bankr. D. Nev. 2010); *In re County of Orange*, 183 B.R. 594 (Bankr. C.D. Cal. 1995); *In re Westport Transit Dist.*, 165 B.R. 93 (Bankr. D. Conn. 1994); *In re Ellicott School Bldg. Authority*, 150 B.R. 261 (Bankr. D. Colo. 1992).

The recent decision of *In re Las Vegas Monorail* illustrates one of the threshold issues for entities seeking to file for relief under Chapter 9. In *Las Vegas Monorail*, the debtor owned and operated a monorail financed by bonds. The bonds were sponsored or issued by the Nevada Department of Business and Industry, and the bond proceeds were loaned to the debtor.

Importantly, the bonds were revenue bonds payable solely from revenues of the debtor, and were underwritten by a bond insurer. When the debtor failed to generate sufficient revenues from operations to satisfy the bond obligations, the debtor filed for Chapter 11. The bond insurer objected to the debtors' status as a Chapter 11 debtor in possession and instead contended that the debtor was a "municipality" under the Bankruptcy Code. According to the bond insurer, because the debtor was a municipality, it was not eligible for bankruptcy without specific statutory authorization from the State of Nevada, which the debtor had not obtained.

The Bankruptcy Court for the District of Nevada undertook a comprehensive examination of the legislative history and purpose of Chapter 9 and, in particular, the scope of the term "municipality." The court then focused on whether the debtor was an instrumentality of the state, which, according to the court, depends on, among other things, whether the entity serves a public function, whether the state's control includes the direct management of finances, and whether the state categorizes or refers to the entity under state law as a municipal entity as opposed to a private entity.

Applying these factors, the court determined that the debtor's finances were not subject to state control, the day to day operations of the debtor were controlled by officers who were not selected by public officials, and the debtor had the ability to incur debt unrelated to the revenue bonds. Moreover, the court noted that the debtor was incorporated under Nevada law as a non-profit corporation and was similarly treated by public agencies of the state as a private entity. Finally, the court recognized that the debtor's operating funds were derived from fares paid by the general public, not from the debtor's authority to impose taxes.

As the finances of various entities continue to erode, *Las Vegas Monorail* and other decisions should provide some guidance to "hybrid" entities such as state fairs, transportation authorities, and investment funds with a nexus to local and sate governments seeking relief under the Bankruptcy Code.

2. Specific State Authorization

The second requirement, that a municipality have specific state authorization prior to filing for bankruptcy, is an extremely problematic obstacle to overcome in numerous states. Under the Bankruptcy Code, the state authorization must be "exact, plain, and direct with well-defined limits so that nothing is left to inference or implication." *In re County of Orange*, 183 B.R. 594, 604 (Bankr. S.D. Cal. 1995); *see also In re Alleghany-Highlands Econ. Dev. Auth.*, 270 B.R. 647, 649 (Bankr. W.D. Va. 2001).

Several recent decisions throughout the country provide guidance as to whether a municipality is authorized to file for Chapter 9 under applicable state law. *See*, *e.g.*, *In re New York City Off-Track Betting Corp.*, 427 B.R. 256 (Bankr. S.D.N.Y. 2010); *In re Slocum Lake Drainage Dist. of Lake County*, 336 B.R. 387 (Bankr. N.D. Ill. 2006); *In re Timberon Water and Sanitation Dist.*, 2008 WL 5170581 (Bankr. D.N.M. June 18, 2008) (resolution from water and sanitation district derived from general statutory enabling powers insufficient to constitute specific authorization).[2]

For example, in *New York City Off-Track Betting*, an entity filed for Chapter 9 relief based solely on an executive order issued by the governor of the State of New York. However, the entity was not specifically authorized by any state statute to file for bankruptcy, nor did any statute convey authority to the governor to issue an order authorizing such a filing. After several creditors of the debtor asserted that the executive order alone was insufficient to specifically authorize a filing in accordance with section 109(c)(2), the Bankruptcy Court for the Southern District of New York held that the governor's broad authority under state law to issue executive orders was sufficient to authorize the filing. The court noted that section 109(c)(2) does not require that an order authorizing a bankruptcy filing be based on a state statute expressly granting specific authority. Rather, according to the court, an executive order constitutes specific authority if the executive order falls within the officer's broad authority under state law.

In another decision, the Bankruptcy Court for the Northern District of Illinois dismissed the Chapter 9 bankruptcy case of a drainage district. *In re Slocum Lake Drainage Dist. of Lake County*, 336 B.R. 387 (Bankr. N.D. Ill. 2006). In *Slocum Lake*, the court rejected an argument by the debtor that it was authorized to file for Chapter 9 because under applicable state law it was authorized to generally exercise the powers and manage and control the affairs of the municipality. The court found that applicable state law failed to contain a specific authorization for a bankruptcy filing. In addition, the court noted that no financial advisor or commission had been appointed to recommend a bankruptcy filing as was required under state law. The court, therefore, dismissed the case.

In Michigan the legislature has adopted fairly intensive procedures for municipalities in financial distress. The Local Government and School District Fiscal Accountability Act, MCL §§ 141.1501, *et seq.* (2011) (the "Fiscal Act"), sets forth the prerequisites to the eligibility of a municipality to file for relief under Chapter 9. The Fiscal Act applies to all municipalities and contains specific provisions related to school districts.

According to the Fiscal Act, the state financial authority of a local government (i.e., the state treasurer or a superintendent of public instruction) may conduct a preliminary review to determine whether a financial problem of a local government exists upon the occurrence of certain events, including, among other things:

(i) the governing body or chief administrative officer of the local government requests a preliminary review;
(ii) the state financial authority receives a request from a creditor with an undisputed claim that remains unpaid six (6) months after its due date[3];
(iii) the state financial authority receives a petition containing specific allegations of local government financial distress[4];
(iv) a local government has been assigned a long-term debt rating within or below the BBB category or its equivalent by one or more nationally recognized credit agencies;
(v) the state financial authority receives notice that employees and retirees of the local government have not been paid or provided benefits, as applicable, for at least seven (7) days from the date of the scheduled payment or benefit; and
(vi) the state financial authority receives notice of a default in a bond payment or violation of a bond covenant.

MCL § 141.1512(1). After a review team is appointed by the governor and has conducted its review, the review team is required to present a report to the governor. MCL § 141.1513(3). The report presented to the governor must include one of the following conclusions: (i) the local government is not in financial distress or is in a condition of mild financial distress, (ii) the local government is in a condition of severe financial distress but a consent agreement containing a plan to resolve the problem has been adopted, (iii) the local government is in a condition of severe financial distress and no consent agreement has been adopted, or (iv) a financial emergency exists and no satisfactory plan exists to resolve the emergency. MCL § 141.1513(4); *see* MCL § 141.1514 (identifying levels of financial distress).

Within ten (10) days after receiving the report, the governor is required to make a determination with respect to the local government's financial condition and, depending on the severity of the financial condition, notify the local government that it needs to request a hearing with the state financial authority or its designee. MCL § 141.1515(1) - (2). Upon a finding of a financial emergency, the governor must declare the local government in receivership and appoint an emergency financial manager. MCL § 141.1515(4); MCL § 141.1515(5) (qualifications of emergency financial manager).

Upon appointment, the emergency financial manager is required to issue orders to the local government to implement a written financial and operating plan for the local government. MCL § 141.1517(1). The financial plan must establish procedures for, among other things, (i) the operation of the local government with the resources available in accordance with the emergency financial manager's revenue estimate, and (ii) the payment in full of the scheduled debt service requirements on all bonds and notes, as well as any other uncontested legal obligations. MCL § 141.1518(1).

The emergency financial manager may undertake numerous actions, including (i) analysis of the circumstances contributing to the condition and recommending actions to correct the same, (ii) the amendment, approval, revision or limitation of the local government's budget, (iii) approval of a plan for payment of all outstanding obligations of the local government, (iv) approving or disapproving any appropriation, contract, expenditure or loan, and (v) rejection, termination or modification of collective bargaining agreements, and (vi) consolidation of departments of the local government. MCL § 141.1519(1). At least one Michigan court has held that an emergency financial manager has the authority to reduce the salaries of city counsel members. *Attorney General v. Flint City Council*, 269 Mich. App. 209, 713 N.W.2d 782 (2006).

Moreover, the emergency financial manager may recommend to the governor and the state treasurer that the local government be authorized to seek relief under Chapter 9 of the Bankruptcy Code. MCL § 141.1523(1). The recommendation by the emergency financial manager must include a determination by the emergency financial manager that either (i) no feasible financial plan can be adopted that will satisfactorily resolve the financial emergency in a timely manner, or (ii) an adopted financial plan, in effect for at least 180 days, cannot be implemented so as to satisfactorily resolve the financial emergency. MCL § 141.1523(2).

It is imperative that any municipality contemplating bankruptcy undertake a comprehensive review of applicable state law prior to filing. Absent express authorization, any bankruptcy filing will be subject to dismissal upon the motion of creditors or even by the court *sua sponte*.

3. Insolvency

The third requirement to be eligible for relief under Chapter 9 is that the municipality be insolvent. With respect to municipalities, insolvency is defined as the municipality's inability to pay its debts as they become due or generally not paying debts as they become due unless such debts are subject of a bona fide dispute. 11 U.S.C. § 101(32)(C)(ii); *see In re City of Vallejo*, 208 B.R. 280 (N.D. Cal. 2009); *In re Pierce County Housing Authority*, 414 B.R. 702 (Bankr. W.D. Wash. 2009). As with insolvency analyses under other chapters of the Bankruptcy Code, an insolvency analysis under Chapter 9 is extremely intensive question of both fact and law.

The insolvency test under section 109(c)(3) is prospective, with the reference point being the date that the petition is filed. *In re Pierce County Housing Auth.*, 414 B.R. 702, 710-11 (Bankr. W.D. Wash. 2009). It must be determined, as of the petition date, whether the municipality will be unable to pay its debts as they become due in the future. Id. Where a municipality has sufficient cash reserves or has the ability to raise taxes and reduce spending to satisfy its outstanding obligations, a debtor may be deemed solvent. *See In re City of Bridgeport*, 132 B.R. 85, 92 (Bankr. D. Conn. 1991); *see Hamilton Creek Metro. Dist. v. Bondholders Colo. Bondshares (In re Hamilton Creek Metro. Dist.)*, 143 F.3d 1381, 1384 (10th Cir. 1998).

However, at least one court has held that a municipality will still be eligible for Chapter 9, notwithstanding the fact that it could have hypothetically undertaken additional actions, such as levying special assessments, to strengthen its financial position. *In re Sullivan County Reg'l Refuse Disposal Dist.*, 165 B.R. 60, 66 (D.N.H. 1994) (holding that the ability to levy a special assessment is not relevant for insolvency, but may be relevant to good faith negotiations under section 109(c)(5)(B)); *see In re City of Vallejo*, 408 B.R. 280, 295 (B.A.P. 9th Cir. 2009); *In re Villages at Castle Rock Metro. Dist. No. 4*, 145 B.R. 76, 84 (Bankr. D. Colo. 1990).

4. Plan of Adjustment

The fourth requirement, that a municipality desire to effectuate a plan to adjust its debts, concerns something separate and distinct from a good faith filing requirement. 11 U.S.C. § 109(c)(4); *see City of Vallejo*, 308 B.R. 280, 295-96 (holding section 921(c) provides creditors with ability to contest filings on good faith grounds). Courts have evaluated the intent of the municipality on an objective level by determining whether the municipality intended to use Chapter 9 to rehabilitate its affairs, or whether the municipality was solely attempting to circumvent creditor claims. *In re Sullivan County Reg'l Refuse Disposal Dist.*, 165 B.R. 60, 66 (D.N.H. 1994).

The few decisions that address this eligibility requirement deem it to be extremely subjective based on the facts and circumstances of the particular case. Compare *In re County of Orange*, 183 B.R. 594, 607 (Bankr. C.D. Cal. 1995) (comprehensive settlement proposal demonstrated, along with other actions, efforts to resolve claims) with *In re Sullivan County Reg'l Refuse Disposal Dist.*, 165 B.R. 60, 76 (Bankr. D.N.H. 1994) (post-petition submission of draft plan of adjustment satisfied element). Municipalities may prove their "desire" to effectuate a plan by, for example, (i) attempting to resolve claims, (ii) submitting a draft plan of adjustment, or (iii) presenting "other evidence customarily submitted to show intent." *In re City of Vallejo*, 408 B.R. 280, 295 (9th Cir. B.A.P. 2009).

In *City of Vallejo*, the city's labor unions asserted that the debtor failed to undertake adequate post-petition actions to effectuate a plan and that the evidence demonstrated that the case was filed in bad faith with the intent only to renegotiate union contracts. *City of Vallejo*, 308 B.R. at 294-95. On appeal, the Bankruptcy Appellate Panel for the Ninth Circuit affirmed the bankruptcy court based on evidence in the record supporting the subjective inquiry. The BAP noted that the debtor submitted a sworn statement of qualification stating that the debtor desires to adjust its debts. After considering the evidence before it, the court found that the unions failed to contradict or impeach those statements. In addition, the court found that the debtor had negotiated with the unions for approximately six months prior to the petition date, and continued negotiations after the petition date. As such, the court believed that the debtor had exhausted all of its options before filing for bankruptcy. Finally, the court found persuasive the fact that, post-petition, the debtor continued its efforts to formulate a plan of adjustment pursuant to which claims would be satisfied or discharged.

When a municipality identifies bankruptcy as an option, it should attempt to formulate and negotiate the terms of a plan of adjustment with its primary creditors, or at the very least attempt to resolve claims, to the best of its ability under the circumstances in order to avoid any allegation that it is seeking to evade an obligation to one creditor.

5. Creditor Relations

The last element, that the municipality negotiate with creditors regarding impairment of their claims, can be deceptively complex. The municipality must demonstrate that (i) it has reached an agreement with its creditors, (ii) it has negotiated with its creditors in good faith, (iii) negotiations would be impractical, or (iv) a creditor would be able to obtain a preference. 11 U.S.C. § 109(c)(5). While the first of the four alternative requirements under section 109(c)(5) is fairly self-explanatory, the remaining three alternative requirements have been the subject of dispute.

a. Agreement with Creditors

As noted above, the first alternative under section 109(c)(5) is that the municipality has reached an agreement with its creditors. Specifically, such an agreement must be with creditors holding at least a majority in amount of the claims of each class that the municipality seeks to impair under a plan of adjustment. 11 U.S.C. § 109(c)(5)(A).

Although very little discussion has been afforded this subsection in published decisions, it appears somewhat analogous to a consensual agreement that is typically reached with creditors when filing a prepackaged plan of reorganization in Chapter 11. It is unclear, however, the precise form of the agreement that must be obtained. As discussed below, a municipality should, at the very least, attempt to circulate, and obtain approval with respect to, a plan of adjustment prior to filing for Chapter 9. Because section 1126(b) of the Bankruptcy Code applies in Chapter 9, a municipality that has reached an agreement with its creditors should attempt to solicit votes required for confirmation on a prepetition basis. *See* 11 U.S.C. § 901(a) (section 1126(b) applies in Chapter 9)[5].

b. Negotiation with Creditors in Good Faith

In order for a debtor to satisfy the requirement that it has negotiated with its creditors in good faith, the debtor will need to demonstrate that it negotiated prior to the petition date and has failed to obtain the agreement of creditors holding at least the majority in amount of the claims of each class that the debtor intends to impair under a plan of adjustment. *See* 11 U.S.C. § 109(c)(5)(B).

According to the courts, the requirements set forth in section 109(c)(5) do not stand on their own. Rather, section 109(c)(5) must be read in conjunction with section 109(c)(4). *See, e.g.*, *In re Cottonwood Water and Sanitation District, Douglas County, Colo.*, 138 B.R. 973, 979 (Bankr. D. Colo. 1992) (the "plan" referred to in section 109(c)(4) is the plan of adjustment negotiated prepetition in good faith).

It is not sufficient for a debtor to have generally engaged in negotiations regarding the debts owed. Rather, the debtor must have engaged in good faith negotiations with its creditors concerning the terms of the plan of adjustment to be proposed under section 941 of the Bankruptcy Code. *See, e.g.*, *In re City of Vallejo*, 408 B.R. 280, 296-97 (9th Cir. B.A.P. 2009) (complete plan not required, but outline or term sheet of plan designating classes of creditors and treatment is necessary); *In re Ellicott School Bldg. Auth.*, 150 B.R. 261, 266 (Bankr. D. Colo. 1992) ("take it or leave it proposal" does not constitute good faith negotiations); *In re Cottonwood Water and Sanitation District, Douglas County, Colo.*, 138 B.R. 973, 979 (Bankr. D. Colo. 1992).

In *Cottonwood Water and Sanitation*, the debtor and its bondholders engaged in negotiations prior to the petition date. When the debtor filed for Chapter 9, the bondholders contended that the negotiations were not related to the terms of the plan of adjustment. The bankruptcy court noted that when a municipality files for bankruptcy, the negotiating posture of the parties changes, in large part due to the automatic stay.

Therefore, according to the court, the negotiation contemplated in section 109(c)(5)(B) "insures that creditors have an opportunity to negotiate concerning a plan on a level playing field with the debtor before their rights are further impaired by the [automatic stay]."

In a similar decision, the Bankruptcy Court for the District of New Hampshire considered whether the debtor had engaged in good faith negotiations prior to filing its petition for relief under Chapter 9. *See In re Sullivan County Reg'l Refuse Disposal Dist.*, 165 B.R. 60, 76 (Bankr. D.N.H. 1994). In *Sullivan County*, it was undisputed that the debtor met with its primary creditor to negotiate with respect to a contract dispute. However, the court found that the debtor evaded attempts to develop a feasible repayment plan until only a few weeks prior to the petition date. Moreover, the court emphasized that even in the weeks immediately prior to the petition date, the debtor failed to exert significant efforts to exercise their assessment power against the debtor's member municipalities. Finally, the debtor asserted a right of setoff that, according to the court, clearly did not exist under the terms of the contract and only acknowledged the lack of any such right during the course of the dismissal hearings. Based on the aforementioned factors, the court found that the debtor had not negotiated with its creditors in good faith prior to filing for bankruptcy.

Similar to *Cottonwood Water and Sanitation*, the court in *Sullivan County* further found that the debtor failed to propose to the primary creditor or any other creditors a comprehensive plan comparable to a plan of adjustment that could be effectuated under Chapter 9. While the court recognized that section 109(c)(5)(B) does not require presentation of a formal plan, the court stated that some sort of comprehensive plan is nonetheless required.

Cottonwood Water and Sanitation and *Sullivan County* require municipalities to engage in negotiations with creditors regarding any potential plan of adjustment prior to the bankruptcy filing. Based on these decisions, municipalities will not satisfy the requirement under section 109(c)(5) by threatening a bankruptcy filing. Instead, the municipality must at least attempt to establish a dialogue and, if possible, negotiate a plan of adjustment prior to filing for Chapter 9.

c. Negotiations Impracticable

In the event that a municipality fails to negotiate with creditors in good faith regarding the terms of a plan of adjustment prior to the petition date, such error may be deemed harmless. Section 109(c)(5) recognizes that in certain situations, negotiations with creditors regarding a plan of adjustment may be "impracticalable." Whether negotiations with creditors are impractical depends on the circumstances of the case. *In re City of Vallejo*, 408 B.R. 280, 297 (9th Cir. B.A.P. 2009).[6]

According to the courts, municipalities may demonstrate impracticability by the number of their creditors, the need to file a petition immediately to preserve their assets, or the need to act quickly to protect the public from harm. *In re City of Vallejo*, 408 B.R. 280, 297 (9th Cir. B.A.P. 2009) (reciting non-exclusive list of factors); *see In re Pierce County Housing Authority*, 414 B.R. 702 (Bankr. W.D. Wash. 2009) (impracticable to negotiate with, and even identify, thousands of tenants and guests of toxic mold infested apartment facilities). Municipalities, however, need not engage in negotiations with creditors to the point that an impasse is reached. *In re Valley Health Sys.*, 383 B.R. 156, 163 (Bankr. C.D. Cal. 2008).

In *City of Vallejo*, the municipality's unions argued that the Chapter 9 case should be dismissed because the municipality failed to negotiate with creditors prior for filing bankruptcy. In response, the municipality argued that such negotiations would have been impracticable, because it could not identify unknown creditors, including retirees. The court agreed with the municipality and held that negotiations were impracticable. First, the court found that the municipality could not meaningfully negotiate with the indenture trustee for bondholders, which was also the municipality's largest creditor, because the municipality was not able to submit a viable long term financial plan without first adjusting its labor costs. Second, the court found that even if the municipality could identify unknown creditors, including retirees, it would have been futile to include them in complex, on-going negotiations with the unions. Finally, the court found that the bankruptcy filing was warranted without negotiations because the municipality needed to preserve its ability to continue providing the community with uninterrupted services. According to the court, any delay in filing for bankruptcy due to identification of unknown creditors would have compromised the services upon which the community relied.

Similarly, in *Valley Health Systems*, the indenture trustee for the municipality's bondholders argued that the municipality did not attempt to negotiate the terms of a plan of adjustment prior to filing for bankruptcy. The Bankruptcy Court for the Central District of California disagreed, however. The court found that the municipality filed the bankruptcy in good faith because a bankruptcy filing was the only means by which to preserve its assets. The court further emphasized that absent a bankruptcy filing, the municipality's business operations would have been interrupted. According to the court, in the event that the municipality had not filed for bankruptcy, it would not have been able to provide healthcare services to its patients while simultaneously preparing a business plan that would serve as the underpinnings for a plan of adjustment and negotiations with all of the municipality's creditors in each class.

The court noted that prior to filing the petition, the municipality had communicated with its major creditors, advised them that the municipality intended to file for bankruptcy, and assured them that the municipality would negotiate a plan of adjustment as soon as it had completed a viable business plan. The court found important the fact that the municipality had at all times acted in conformity with state law by, among other things, approving the filing at a properly noticed public meeting with opportunity for participation by the attendees.

The court also recognized that the municipality had exhausted its efforts to resolve its financial distress through a restructuring and the sale of some of its assets, both of which were unsuccessful. Finally, the court emphasized that the sheer number of creditors, consisting of eleven classes, rendered negotiations impracticable.

d. Creditor Would Otherwise Obtain Preference

Section 109(c) also provides that a municipality is eligible for bankruptcy if the municipality reasonably believes that a creditor may attempt to obtain a preference pursuant to section 547 of the Bankruptcy Code.[7] 11 U.S.C. § 109(c)(5)(D). With respect to municipalities, it is unclear if the filing, or even threat, of a lawsuit is sufficient to satisfy the requirement.

In *Sullivan County Regional Refuse Disposal Dist.*, the municipality contended that it reasonably believed that a creditor was attempting to obtain a preference when the creditor threatened to terminate an agreement upon which the municipality relied for waste disposal services. 165 B.R. 60, 76 n. 50 (Bankr. D.N.H. 1994). The court found this argument unpersuasive, noting that contract termination does not constitute a preference. *See also In re New York City Off-Track Betting Corp.*, 427 B.R. 256, 278 (Bankr. S.D.N.Y. 2010) (passing testimony and limited evidence proffered by municipality failed to meet evidentiary burden). The court did not, however, address whether the filing of a lawsuit for money damages is sufficient to satisfy this requirement.

Arguably, the threat, or filing, of a lawsuit may not be sufficient if the creditor is seeking a money judgment. Rather, a plausible argument can be made that only after entry of a judgment and the threat of execution or levy would a municipality reasonably believe that a creditor is attempting to obtain a judgment. However, where a creditor is seeking to exercise post-judgment relief, the municipality would seem to have a reasonable belief that a creditor is attempting to obtain a preference.

B. Good Faith Under 11 U.S.C. § 921(c)

In addition to the eligibility requirements under section 109(c), the Bankruptcy Code imposes a "good faith" requirement. Section 921 of the Bankruptcy Code provides that "[a]fter any objection to the petition, the court, after notice and a hearing, may dismiss the petition if the debtor did not file the petition in good faith or if the petition does not meet the requirements of this title." 11 U.S.C. § 921(c). The language of section 921(c) is permissive. Therefore, a court maintains discretion to dismiss under section 921(c) unless the defect in the filing is in the debtor's eligibility to file for Chapter 9 under section 109(c). *In re County of Orange*, 183 B.R. 594, 599 (Bankr. C.D. Cal. 1995) (citation omitted).

The following factors should be considered in determining whether a Chapter 9 bankruptcy was filed in good faith: (i) the debtor's subjective beliefs; (ii) whether the debtor's financial problems fall within the situations contemplated by Chapter 9; (iii) whether the debtor filed its petition for reasons consistent with the purposes of Chapter 9; (iv) the extent of the debtor's prepetition negotiations; (v) the extent to which alternatives to bankruptcy were considered; and (vii) the scope and nature of the debtor's financial problems. *In re Pierce County Housing Authority*, 414 B.R. 702, 714 (Bankr. W.D. Wash. 2009) (citing 6 Collier 921.04[2], at 921-6); *In re Valley Health Sys.*, 383 B.R. 156, 161 n. 8 (Bankr. C.D. Cal. 2008) (same).

In *In re Sullivan County Regional Refuse Disposal District*, 165 B.R. 60 (Bankr. D.N.H. 1994), certain creditors moved to dismiss the petitions of two disposal districts because, among other things, the districts allegedly lacked good faith when they filed for Chapter 9 under section 921(c). The Bankruptcy Court for the District of New Hampshire agreed, finding that the decision to file for bankruptcy was not the end result of considerable debate. According to the court, the districts, acting through their joint committee of member municipalities, did not properly consider the alternatives available to them and only elected to file upon an oral motion without any previous substantive discussion or even reference to a potential bankruptcy in the meeting agenda.

The court further noted that the decision to file for bankruptcy appeared to be a "late hour litigation tactic" in order to force a compromise with the districts' largest creditor. The court commented:

"Municipalities that wish to come into bankruptcy under Chapter 9 . . . must, at a minimum, demonstrate that before filing they either used their assessment or taxing powers to a reasonable extent, or in their pre-petition negotiations have committed to the use of those powers as part of a comprehensive and appropriate work out of their financial problems."

Because the districts did not properly attempt to use its assessment and/or taxing powers to satisfy its obligations before filing, the court held that the petitions should be dismissed due to a lack of good faith. *But see In re Pierce County Housing Authority*, 414 B.R. 702 (Bankr. W.D. Wash. 2009) (distinguishing *Sullivan County* by noting that the decision to file for bankruptcy was made only after several years of negotiations and mediations).

Section 921(c) requires a municipality to undertake substantial review and analysis prior to filing for bankruptcy. The courts that have considered whether to dismiss petitions for lack of good faith clearly place importance on a municipality's attempts to resolve its issues with creditors prior to filing. Accordingly, the courts appear skeptical with respect to a municipality's motives absent evidence that bankruptcy was the last resort only after considerable efforts to consensually resolve issues. A municipality considering Chapter 9 should therefore explore, and exhaust, all reasonable efforts to avoid a bankruptcy filing. Any decision to file should be predicated on sufficient notice to the public and subject to debate in an open forum. The failure of a municipality to follow these guidelines may be fatal to the good faith requirement under section 921(c).

C. Conclusion

Municipalities are certain to continue to suffer from poor investments, rising labor costs, and a depletion of their tax base in the forthcoming months. It thus appears likely that the United States will witness a wave of municipal bankruptcy filings in the near future. As a prerequisite to any bankruptcy filing, it will be imperative for municipalities to attempt to negotiate resolution with their constituencies and comprehensively explore and exhaust any alternatives prior to filing for bankruptcy. Absent such careful planning, municipalities will subject themselves to attacks by creditors at the early stages of a bankruptcy case due to their eligibility and alleged lack of good faith.

Footnotes:

1. *See*, *e.g.*, Michigan Town Is Left Pleading for Bankruptcy, Monica Davey, New York Times, December 27, 2010.

2. In a recent decision from the United States Bankruptcy Court for the Southern District of Alabama, the court dismissed a city's bankruptcy case because the city did not have outstanding bonds as of the petition date, rendering the city without specific authorization to file for bankruptcy under applicable Alabama state law. *In re City of Prichard, Ala.*, Case. No. 09-15000 (Bankr.

S.D. Ala. Oct. 19, 2010). The case is currently on appeal. *City of Prichard, Ala. v. Prichard Retirees*, Case No. 10-00622 (D. Ala.).

3. The claim must exceed the greater of $10,000.00 or one (1) percent of the annual general fund budget of the local government. The creditor must notify the local government at least thirty (30) days in advance prior to making any request to the state treasurer.

4. The petition must be from a number of registered electors residing within the jurisdiction of the local government equal to not less than five (5) percent of the total vote cast for all candidates for governor within the jurisdiction of the local government at the last preceding gubernatorial election.

5. Section 1126(b) provides that votes solicited prepetition may be counted so long as the solicitation was in compliance with any applicable non-bankruptcy law governing the adequacy of disclosure, or, if no such law exists, after disclosure of adequate information, as defined in section 1125 of the Bankruptcy Code. This allows the debtor to solicit acceptances of its proposed plan without first having to obtain court approval of a disclosure statement.

6. In the context of Chapter 9, one court has described "impracticable" as "not practicable; incapable of being performed or accomplished by the means employed or at command; infeasible. In the legal context, impracticability is defined as a fact or circumstance that excuses a party from performing an act, esp. a contractual duty because (though possible) it would cause extreme and unreasonable difficulty." *In re Valley Health Sys.*, 383 B.R. 156, 161 (Bankr. C.D. Cal. 2008)

7. Section 547 of the Bankruptcy Code sets forth the elements of a preferential transfer. In order for a transfer during the preference period to constitute a preferential transfer, and thus be avoidable, the plaintiff must demonstrate that the payment was the transfer of property of the debtor (i) which occurred within ninety (90) days before the bankruptcy filing (or one year if it is to an insider) (ii) to or for the benefit of a creditor (iii) on account of an existing debt (iv) while the debtor was insolvent and (v) that allows the creditor to receive more than it would have received in a chapter 7 liquidation. 11 U.S.C. § 547(b).

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THE LAW OF CROSS-BORDER INSOLVENCY PROCEEDINGS: A BRIEF SUMMARY OF ITS SOURCES, DEVELOPMENT AND PRESENT STATUS

I. Introduction

In this era of multinational enterprise groups and intensified globalization, insolvency proceedings involving related businesses commenced in more than one nation have become relatively commonplace. A prominent example of cross-border insolvency proceedings[1] are those involving Lehman Brothers, which cases were commenced on and after September 15, 2008 in North America, Europe, Asia and Australia and involved more than 1,000 related legal entities. In cross-border cases, the primary challenge to insolvency administrators, courts, creditors and other stakeholders is how to quickly and efficiently reorganize or liquidate these related business entities in distant forums with differing legal systems without losing enterprise value through failures in communication and coordination.

Legal efforts to coordinate "cross-border" insolvency cases are not novel but have intensified within the last twenty years as the world economy has become more integrated. For example, in 1697, the Dutch states of Holland and Utrecht entered into a convention whereby an administrator appointed in one territory was permitted to collect, liquidate and administer assets located in the other territory "according to the local law of the place of appointment."[2] The dissolution of the Austro-Hungarian Empire in 1918 resulted in a series of bilateral treaties governing administration of assets of insolvent debtors entered into by new states arising from the collapse of that political system.[3] In 1933, the Scandinavian countries of Denmark, Finland, Iceland, Norway and Sweden concluded the Nordic Bankruptcy Convention, which directed that the insolvency law of the state in which insolvency proceedings were pending would govern the disposition of all assets of the debtor, notwithstanding the presence of assets in other contracting states and granted to the administrator powers to administer assets located in the other states.[4]

II. Development, Promulgation and Adoption of the Model Law on Cross-Border Insolvency

Beginning in the 1990s, a movement began to regulate cross-border insolvency cases to fill the large gaps existing in many national laws governing these proceedings. One of the first products of this trend was the Model Law on Cross-Border Insolvency developed by the United Nations Commission on International Trade Law (referred to herein as the "Model Law" or the "UNCITRAL Model Law"), which the General Assembly of the United Nations approved by Resolution 52/158 on January 30, 1998. This resolution explicitly recognized that "increased cross-border trade and investment leads to greater incidence of cases where enterprises and individuals have assets in more than one State" and, as a consequence, when a debtor holding such multinational assets "becomes subject to an insolvency proceeding, there exists an urgent need for cross-border cooperation and coordination in the supervision and administration of the insolvent debtor's assets and affairs." This resolution voiced the General Assembly's collective belief that "fair and internationally harmonized legislation on cross-border insolvency that respects the national procedural and judicial systems" of all states would "contribute to the development of international trade and investment." The resolution concluded with a recommendation that all nations review their legislation on cross-border insolvency matters and, while performing that review, "give favorable consideration to the Model Law."

The Model Law applies in the following four situations:

(a) Where a foreign court administering an insolvency case or a foreign insolvency administrator seeks the assistance in the state adopting the Model Law "in connection with a foreign proceeding." (b) Where assistance is sought in a foreign state involving a proceeding pending in the adopting state. (c) Where a foreign proceeding and a proceeding in another state concerning the same debtor "are taking place concurrently." (d) Where creditors or other interested parties in a foreign state seek to commence or participate in an insolvency proceeding in the adopting state.

Model Law, Article 1.

The Model Law adopts the following key definitions that are used throughout its text:

- "foreign proceeding": a "collective judicial or administrative [insolvency] proceeding" wherein the debtor's assets and affairs "are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation."
- "foreign main proceeding": a foreign proceeding in a state where the debtor has the "centre of its main interests," otherwise referred to as "COMI."[5]
- "foreign non-main proceeding": a foreign proceeding, other than a foreign main proceeding, pending in a state where the debtor has an "establishment."
- "establishment": any place of operations where the debtor conducts "a non-transitory economic activity with human means and goods and services."

Id., Article 2.

In summary, the Model Law authorizes domestic insolvency courts to recognize official representatives appointed in foreign ancillary proceedings and foreign creditors to enable them to participate, without discrimination, as interested parties in a main insolvency proceeding commenced in the domestic court. *Id.*, Articles 9-14. The Model Law also establishes a procedure whereby a foreign representative may apply to the domestic court for recognition of a foreign main or non-main proceeding in which that representative has been appointed. *Id.*, Articles 15-18. A foreign main proceeding will be recognized if it "is taking place in the State where the debtor" has its COMI. *Id.*, Article 17(2)(a). A foreign non-main proceeding will be recognized if the debtor has an "establishment" in the foreign State. *Id.*, Article 17(2)(b). Upon the granting of such recognition, Articles 19-24 of the Model Law prescribe mandatory relief that must be, and discretionary relief that may be, granted by the domestic court upon recognition of a foreign proceeding. Once a foreign main proceeding is recognized, a broad injunction against the commencement or continuation of credit actions or proceedings against the debtor its assets is stayed and the debtor's right to "transfer, encumber or otherwise dispose" of assets is suspended. *Id.*, Article 20(1). Other actions that courts may take upon the recognition of a foreign main or non-main proceeding are listed in Article 21 of the Model Law and include the imposition of a stay against actions or proceedings (to the extent non previously stayed under Article 20) and provision for the examination of witnesses.

Cooperation involving foreign courts and foreign representatives is addressed in Articles 25-27. In the four situations described in Article 1 of the Model Law, the domestic court is directed to cooperate with foreign courts or foreign representatives "to the maximum extent possible" and, in doing so, the domestic court may "communicate directly with, or to request information directly from, foreign courts or foreign representatives." *Id.*, Article 25. Foreign representatives are directed and permitted to do the same. *Id.*, Article 26. "Cooperation" may include (i) appointing a person or body to act at the domestic court's direction; (ii) coordinating the administration of assets, (iii) approving and implementing "agreements concerning the coordination of proceedings", commonly referred to in practice as "protocols"; and (iv) coordinating proceedings concerning the same debtor. *Id.*, Article 27. Finally, the Model Act addresses certain procedures for the domestic court and foreign courts to follow in cross-border insolvency proceedings. *Id.*, Articles 28-32.

At present, 18 countries have adopted the Model Law or some version thereof. Signatories include Canada, Great Britain, Japan, Mexico and the United States. In October 2005, the

United States Congress substantially overhauled the United States Bankruptcy Code and enacted Chapter 15 of the Bankruptcy Code, which is a slightly modified version of the Model Law. In general, the provisions of the Model Law are binding upon courts in signatory states in cross-border insolvency cases involving those countries.

III. Adoption of the Model Law in the United Kingdom and the European Union's Insolvency Regulation

The United Kingdom ("UK") now has a "complete three piece suite" of cross-border legislation which assists in achieving the principles declared by the United Nations Commission on International Trade Law when it adopted the Model Law on 30 May 1997. Adoption of the Model Law by the UK in the form of the Cross-Border Insolvency Regulations 2006 ("the 2006 Regulations") was the latest piece of the jigsaw in international co-operation which commenced in the UK many generations ago originally in the form of case law allowing comity between nations with similar judicial, administrative and legislative principles. The other two parts of the "three piece suite" are found in Section 426 ("Section 426") of the Insolvency Act 1986 and in the EU Insolvency Regulation 1346/2000 ("The EU Regulation"). Section 426 codified co-operation between the UK and other designated countries and territories, largely those in the British Commonwealth, as well as each of the countries comprising the United Kingdom (for these purposes, Scotland and Northern Ireland). Consequently, UK office holders (e.g. liquidators and administrators) have access to (i) insolvency procedures in other EU states through the EU Regulation; (ii) to the numerous designated countries under Section 426; and (iii) on the wider global platform, to those subscribers to the UNCITRAL Model Law.

The 2006 Regulations are the UK equivalent to Chapter 15 of the United States Bankruptcy Code and are implemented in the UK via Section 14 of the Insolvency Act 2000 which brought the 2006 Regulations into effect. Schedule 1 of the 2006 Regulations sets out the UNCITRAL Model Law as adapted to apply in the UK. The 2006 Regulation equivalents are found in the national insolvency laws of the other UNCITRAL Model Law signatories. The 2006 Regulations accordingly apply to "foreign main" and "non-main" proceedings. Foreign proceedings are "foreign main" proceedings if the collective insolvency proceedings have been commenced in the debtor's COMI. In such cases, an automatic stay is imposed by the UK court handling the insolvency proceedings to protect the debtor's assets, i.e., preventing their dissipation and the commencement and continuation of collection and lien enforcement proceedings against the debtor.

Proceedings are "foreign non-main" proceedings if they are those outside the debtor's COMI. In these situations, the imposition of a stay against creditor action will be in the discretion of the court. In addition, the definition and scope of COMI has been clarified in case law. Some recent UK decisions illuminating the meaning of COMI and its consequences are discussed below in Section VII.

The European part of the "three piece suite," *i.e.*, the EU Regulation adopted by the Council of the European Community (now Union) on May 29, 2000, became effective and binding upon the Member States of the European Union on May 31, 2002. Like the Model Law, the EU Regulation does not change the substantive insolvency laws of EU Member States. The EU Regulation primarily addresses procedures in "collective insolvency proceedings" pending in two or more member states that "entail the partial or total divestment of a debtor and the appointment of a liquidator." EU Regulation, Article 1. Among the Member States, it replaces previous conventions on cross-border insolvency cases enacted by them, including the Nordic Bankruptcy Convention of 1933.

Article 3 of the EU Regulation sets forth rules of jurisdiction over cross-border insolvency proceedings. First and foremost, only the courts of a Member State in which the debtor's "center of main interests," or "COMI", is situated has jurisdiction to "open" insolvency proceedings of a "company or legal person," and the place of the debtor's "registered office" is presumed to be that of the debtor's COMI "in the absence of proof to the contrary." EU Regulation, Article 3(1).[6] If the debtor has its COMI in a Member State, courts in another Member State will have jurisdiction to open insolvency proceedings involving that debtor only if the debtor has an "establishment" in that state.[7] These "secondary proceedings" commenced outside of the debtor's COMI must be "winding up proceedings", as defined in EU Regulation Article 2(c). *Id.*, Article 3(3). The insolvency law of the Member State in which main or secondary proceedings are opened "shall determine the conditions for the opening of those proceedings, their conduct and their closure." *Id.*, Article 4(2).

Article 16 of the EU Regulation provides the general principles of recognition of main and secondary insolvency proceedings in Member States. First, Member States must recognize any judgment "opening" insolvency proceedings issued by a court in another Member State that has jurisdiction. *Id.*, Article 16(1). Nevertheless, recognition of a main insolvency proceeding by Member States will not bar the commencement of secondary insolvency proceedings in another Member State. *Id.*, Article 16(2). Furthermore, the effects of a secondary proceeding in a Member State "may not be challenged in other Member States." *Id.*, Article 17(2).

Secondary proceedings may be commenced by the liquidator appointed in the main proceeding and these secondary proceedings may affect only the assets of a debtor situated in the Member State hosing the secondary proceeding. *Id.*, Articles 27, 29.[8] The liquidator in the main proceeding and the liquidator in the secondary proceeding are "duty bound to communicate information to each other" and to cooperate with one another. *Id.*, Article 31(1). Unlike the Model Law, the EU Regulation contains no requirement that the courts of Member States hosting main and secondary proceedings communicate or cooperate with one another.

Where secondary proceedings may be closed and assets liquidated in the absence of a "rescue plan, a composition or a comparable measure", the liquidator in the main proceeding may nevertheless propose such a measure to the court. *Id.*, Article 34(1). If the liquidation of assets in a secondary proceeding produces sufficient funds to pay all allowed claims in those proceedings, the liquidator in this proceeding must "immediately transfer any assets remaining to the liquidator in the main proceeding." *Id.*, Article 35.

Finally, upon the opening of main and secondary proceedings, the liquidator appointed in those proceedings or the court conducting the proceedings must "immediately inform known creditors who have their habitual residences, domiciles or registered offices in the other Member States" of the pendency of the proceedings, the existence of any time limits, the identity of any entity entitled to accept the filing of claims and "other measures laid down." *Id.*, Article 40. All creditors having a habitual residence, domicile or registered office in a Member State (other than the Member State in which the proceedings were opened) have the right to file written claims in that proceeding. *Id.*, Article 39.

As previously noted, the United States, the United Kingdom and Mexico have adopted the Model Law or some variant thereof. Germany has not adopted the Model Law but, as a Member State of the European Union, is subject to the EU Regulation. The following is a brief summary of recent developments in each of these four countries concerning these laws governing cross-border insolvency cases.

IV. United States of America

As previously stated, in October 2005, the United States Congress enacted the Bankruptcy Abuse Prevention and Consumer Protection Act, which made sweeping changes in the United States Bankruptcy Code (the "Code") and also added Chapter 15 to the Code. Chapter 15 essentially adopted the Model Act with changes to conform to the language and structure of the Code. In the five years since its enactment, many cross-border insolvency proceedings have been commenced under Chapter 15 in American bankruptcy courts, especially in the United States Bankruptcy Court for the Southern District of New York and the United States Bankruptcy Court for the District of Delaware.

One hallmark of Chapter 15 practice in the United States specifically encouraged by the Model Act is the extensive use of protocols by the bankruptcy courts in cross-border cases. In these protocols, which were first developed in the Chapter 11 cases of Maxwell Communications Corporation and related companies commenced in 1991, normally determine whether the American court or the foreign court will handle particular aspects of the cross-border cases and also provide for other forms of coordination. In 2000, the American Law Institute adopted and promulgated Guidelines Applicable to Court-to-Court Communications in Cross-Border Cases as part of its project on *Transnational Insolvency: Principles of Cooperation Among the NAFTA Countries*, which guidelines have been incorporated in many of the protocols between American bankruptcy courts and foreign courts. Court-to-court protocols also often address the manner of communications between the different courts, the conduct of joint hearings in the cases, recognition of foreign stays of proceedings, retention and compensation of professionals retained by the insolvent estates and transmission of notices to creditors and interested parties. In addition, insolvency administrators appointed in cross-border cases often adopt protocols for the sharing of information and the coordination of the various proceedings. Complex protocols among administrators have been recently adopted in the *Lehman Brothers* and *Madoff Securities* cross-border cases.

In a recent decision of the United States Bankruptcy Court for the Southern District of New York, *In re Lyondell Chemical Company*, 402 B.R. 571 (Bankr. S.D.N.Y. 2009), the court entered a broad injunction against the commencement of creditor actions against certain foreign, non-debtor third parties related to the Lyondell debtors on the ground that such actions could negatively impact the bankruptcy estates of these debtors. The injunction was imposed for an initial 60-day period to permit Lyondell's parent company to commence an insolvency proceeding in Europe and thereby protect its assets from creditor action. These types of extraordinary, extraterritorial stays have been imposed in other American bankruptcy cases. *See*, *e.g.*, *Truvo USA LLC v. The Bank of New York Mellon Corporation (In re Truvo USA LLC)*, Adversary Proceeding No. 10-03341 (AJG), Docket No. 26 (Bankr. S.D.N.Y. July 14, 2010).

Some recent American court decisions have refused to recognize alleged foreign main and non-main proceedings as requested in Chapter 15 petitions filed by foreign administrators. The seminal decision in this area is *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). In this case, Bankruptcy Judge Burton R. Lifland refused to recognize liquidation proceedings pending in the Cayman Islands involving two Bear Stearns' hedge funds. The bankruptcy court first determined that the presumption that the funds COMI was in the Cayman Islands had been rebutted by evidence to the contrary and, thus, those proceedings were not "foreign main proceedings." Next, the court held that the funds had no "establishment" in the Cayman Islands in order to qualify the proceedings as "foreign non-main proceedings." *See also In re Basis Yield Alpha Fund (Master)*, 381 B.R. 37 (Bankr. S.D.N.Y. 2008); *In re SPhinX, Ltd.*, 351 B.R. 103 (Bankr. S.D.N.Y. 2006), *aff'd*, 371 B.R. 10 (S.D.N.Y. 2007).

Finally, The Fifth Circuit Court of Appeals, in a case of first impression under Chapter 15, held that an American bankruptcy court in Chapter 15 proceedings has jurisdiction to adjudicate foreign avoidance actions under foreign law commenced by the administrator. *Fogerty v. Petroquest Resources Inc. (In re Condor Ins. Ltd.)*, 601 F.3d 319 (5th Cir. 2010). Here, the liquidation proceeding of a foreign insurance company in Nevis was recognized as a foreign main proceeding by the American bankruptcy court and, shortly thereafter, the liquidators commenced an action to recover $313 million transferred from Nevis to the United States as a fraudulent transfer under Nevis law. Although section 1521(a)(7) of the Code permits an American bankruptcy court to grant to an administrator any additional relief available to a trustee" under the Code, this Code provision specifically prohibits the granting of authority to commence actions to avoid fraudulent transfers arising under the Code. On the basis of this statutory provision, the bankruptcy court dismissed the liquidators' complaint for lack of subject-matter jurisdiction but, on appeal, the Fifth Circuit Court of Appeals reversed the decision below. According to the Fifth Circuit, the foreign liquidators could commence actions to recover fraudulent transfers under Nevis law even though they were precluded from commencing similar actions under the Code; nothing in Chapter 15 prohibited this result.

As the court decisions described above demonstrate, American bankruptcy judges have been active in interpreting key provisions of the Model Law (as embodied in Chapter 15) and, in some situations, perhaps have stretched their boundaries. As described below, Mexican judges have also not been shy in interpreting Mexico's version of the Model Law to reach a desired result.

V. Mexico

Mexico adopted the Model Law, with some specific modifications, by enacting in May, 2000 the *Ley de Concursos Mercantiles* (the "Concurso Law"). At the turn of the new millennium Mexico was making efforts to be part of the globalization trend by adopting other model laws, such as the Arbitration Model Law. There were then unique circumstances influencing the creation of an entirely new insolvency regulation establishing an effective and efficient regime governing cross-border insolvency proceedings of Mexican corporations, especially those corporations requiring access to foreign capital markets.

Prior to the enactment of the Concurso Law, Mexico's prior insolvency law was the *Ley de Quiebras y de Suspension de Pagos*, which had been adopted in April, 1943. Mexico was then a different country and, towards the end of the Twentieth Century, this law was far from effective in facilitating reorganizations of Mexican businesses. First, the prior law was heavily focused on the liquidation rather than the rearrangement of companies. The law did contain a section for the financial restructuring of companies but was too rigid concerning the methods of proposing and implementing reorganization plans for troubled Mexican businesses. Second, and perhaps more importantly, the procedural framework of Mexico's 1943 law encouraged lengthy litigation which stalled the prompt reorganization of financially distressed businesses. Even today, cases are pending in the Mexican judicial system that are governed by the 1943 law, some of which were commenced more than ten years ago.[9] Needless to say, Mexico's prior insolvency law permitted many abuses by companies who obtained the legal protection from creditors but had little or no incentive to achieve a financial restructuring.

The Concurso Law accomplished a sea change in the Mexican legal environment by providing for more flexible reorganization proceedings via a court-supervised plan mandating restructuring of troubled companies within a reasonable time. This law divides insolvency proceedings into two consecutive phases, the first of which is the "conciliation" phase[10], which is similar to the exclusivity period in the Chapter 11 of the United States Bankruptcy Code. During this phase, the debtor and its creditors are required to implement a plan within one year after the case is commenced with the assistance of a conciliator who is a private practitioner appointed by the courts to help negotiate the plan. If a plan is not confirmed by the court within one year[11], the second phase is triggered. This second, liquidation phase requires the prompt sale of the assets of the company in parts or in bulk.

The Concurso Law does not recognize the concept of a creditor's "hostile" plan; any business reorganization plan must be accepted by the debtor or liquidation will inevitably follow. Viewed against the history of prior law, where debtors could delay fulfilling their obligations without incurring any significant sanctions and enjoy the typical stay protections in insolvency proceedings, the Concurso Law was first received with much skepticism. This skepticism was intensified by the fact that insolvency proceedings under the Concurso Law were matters of exclusive federal jurisdiction which, in the past, was slowly exercised by the courts, if at all. Thus, the business and legal communities were forced to adapt and learn how this law would function on the basis of trial-and-error.

The first high profile case commenced under the Concurso Law involving significant debt was that of Mexico's largest paper producer, Corporacion Durango ("Durango"), which was commenced in 2004. This case involved debt in excess of $1.2 billion (U.S.). Upon the commencement by Durango of its insolvency case under the Concurso Law, Durango attempted to restructure its debts by means of a "prepackaged" reorganization plan even though the law at that time did not contain such provisions. Durango also filed for bankruptcy protection in the United States under then-Section 304 of the United States Bankruptcy Code[12] because Durango owed significant sums to American creditors, and, thus, required a stay imposed by an American bankruptcy court against collection actions in the United States by these creditors. This case proved to be a seminal one for the new, cross-border insolvency era in Mexico that followed. In these cross-border proceedings, Durango was able to restructure its debts within six months with the protection of an American bankruptcy court, even before the concurso was actually accepted by Mexican courts.[13] Upon approval of the reorganization plan by the Mexican court, this plan was thereafter recognized by the American bankruptcy court in which Durango's cross-border case was pending. This outcome in a high-profile case established a precedent and model for future restructurings under the Concurso Law. Shortly after the Durango case was resolved, Satelites Mexicanos, Mexico's satellite company operating under a government license, accomplished a two-step reorganization through a concurso proceeding and, upon approval of the reorganization plan in Mexico, filed a Chapter 11 petition under the United States Bankruptcy Code to finalize its restructuring. This second success established the foundations for what was to follow in 2008 and 2009. These two cases also influenced the Mexican congress to amend the Concurso Law in 2007 to include provisions specifically providing for prepackaged reorganization plans.

Following the turmoil of the global financial crisis, including the defaults in mortgage-backed securities and the negative exposure of some Mexican companies to derivative transactions, many reorganization cases were commenced in 2008 in Mexico, including Durango's second, cross-border proceeding that concluded successfully in nine months.[14] Nevertheless, in the hostile economic climate of the world financial crisis, the Concurso Law faced its hardest tests with many proceedings being commenced.

One such case, however, stands out. Controladora Comercial Mexicana ("CCM") saw its debt mushroom exponentially from one day to another because of its exposure to derivative transactions with financial institutions. After two years of negotiations, CCM commenced a pre-packaged, Concurso case along with a case under Chapter 15 of the United States Bankruptcy Code. CCM completed its court-supervised restructuring in the record time of three and one-half months. Other cross-border cases followed and they all adhered to the script that was fashioned in the first Durango case. CCM contributed importantly to the further development of this script. No other Mexican cross-border insolvency case has been followed so closely by Wall Street than this one, given the high stakes that many of its denizens had in this insolvency. CCM demonstrated not only that a complex restructuring can be done in Mexico, but also that the restructuring can be accomplished in a time period comparable to confirmation of prepackaged Chapter 11 plans in the United States.

In conclusion, the Concurso Law and its cross-border insolvency capabilities have evolved within the past ten years into an efficient framework for the smooth and expeditious reorganization of global Mexican businesses. Although there will always be a risk that a particular Mexican business in a Concurso case may not be able to restructure its business, this failure will not be caused by a weakness in the legal framework, but by other factors that are perhaps unique to that business.

VI. Germany

Before the Regulation went into force, cross-border insolvencies were addressed only in one provision of the German Insolvency Act (i.e., Section 102, Insolvency Act of 2000), despite the fact that a new Insolvency Act had just been enacted in 2000.[15] This was widely regarded as inadequate. After the EU Regulation became effective on May 31, 2002, the German Bundestag decided to introduce more detailed provisions on cross-border insolvencies in a separate new section of the Insolvency Act, viz., Part 11 of the Insolvency Act, Section 335 *et seq*. These new provisions became effective on March 20, 2003.

Since then, Germany has two separate sets of rules governing cross-border insolvencies. Only the EU Regulation applies in these cases if the debtor has its COMI in a Member State. Id., EU Regulation, Article 3 and Recital No. 14. To the extent the EU Regulation applies in cross-border cases, national rules of the German Insolvency Act are not operative. Provisions of the

German Insolvency Act (e.g., Sections 335, et seq.) will govern only if the debtor has its COMI outside a Member State. The national provisions of the Insolvency Act and not the EU Regulation would therefore apply in cross-border insolvencies involving the United States.[16] Although the provisions of the EU Regulation applying to insolvency proceedings for debtors having their COMI within the European Union are separate from Germany's national rules applying to proceedings for debtors having their COMI outside the Union, the EU Regulation rules are in substance largely identical to Germany's national rules. Germany's legislature has used the EU Regulation as a "blueprint" for the new Sections 335 *et seq*. of the Insolvency Act. However, there are also differences. While, for example, under the EU Regulation "secondary proceedings" may only be opened by courts of a Member State if the debtor has an "establishment" in that state, under the national German rules secondary proceedings may be opened only if the debtor has (i) an "establishment" in Germany or (ii) "assets" in Germany and the creditor can establish a "specific interest" (*besonderes Interesse*) why secondary proceedings should be opened in Germany. *Id*.; Section 354, ¶¶ 1, 2 of the German Insolvency Act. The conditions under which secondary proceedings may be opened are therefore broader under Germany's national law than under the EU Regulation. Like the EU Regulation, Germany's national law obliges the insolvency administrator (*Insolvenzverwalter*) to communicate information to other liquidators appointed in main or secondary proceedings of the same debtor. German courts, however, are not required to host main or secondary proceedings to communicate or cooperate with foreign courts.

After the EU Regulation came into force in 2002, German courts were involved in a number of conflicting decisions with courts of other Member States. In particular, English courts had interpreted COMI broadly and opened main proceedings not only for the parent company which had its COMI in England, but also for its German subsidiaries, arguing that "head office functions" and "mind of management" of these subsidiaries were not situated in Germany but in the parent's English domicile.[17] Some German courts nonetheless refused to follow this approach.[18] In other cases, German courts adopted a similar approach in cross-border insolvencies with Austria, again with the goal of opening main proceedings in Germany for the German parent company as well as its Austrian subsidiary.[19] Ultimately, the European Court of Justice rebuffed the "head office functions" approach in the "Eurofoods/Parmalat" decision.[20] Conflicting decisions have diminished in number, however, since the Eurofoods/Parmalat decision.

Nevertheless, in recent years German companies have increasingly attempted to use the "COMI approach" of the EU

Regulation to migrate to other Member States in order to benefit from foreign insolvency proceedings. For example, Deutsche Nickel AG and Schefenacker AG successfully migrated their respective COMIs to England to escape German insolvency proceedings.[21] Similar attempts by other enterprises turned out to be unsuccessful when German courts ruled that these companies still had their COMI in Germany.[22]

The stimulus for German companies attempting to move their COMI to other Member States is that certain provisions of the German Insolvency Act are considered rigorous and jeopardize successful business reorganizations. Three primary arguments exist for migration. First, a reorganization under German insolvency proceedings is difficult to plan. Although one of the main goals of the Insolvency Act is the reorganization of the debtor, neither the debtor nor its primary stakeholders have the ability to select the insolvency administrator (*Insolvenzverwalter*) in a particular case. The administrator is appointed by the court and most courts refuse to consider the desires of main creditors before making this appointment. Second, under German law restructuring arrangements with debtors outside formal insolvency proceedings require the consent of all creditors; specific "company voluntary arrangements"[23] allowing restructuring outside insolvency proceedings without the consent of all debtors are unknown. Finally, "debt for equity swaps" are currently very difficult to accomplish in German insolvency proceedings.

The migration of German companies to other European countries (in particular, England) in recent years has occurred notwithstanding that one of the main goals of the Regulation was to avoid forum shopping.[24] This migration has placed pressure on the Bundestag to make German insolvency law more attractive for restructuring measures. Therefore, the Germany Ministry of Justice (Bundesjustizministerium) has just recently proposed further amendments to the Insolvency Act.[25] The draft new law aims[26] at giving creditors greater influence concerning the appointment of the administrator. Moreover, according to this proposal, an "insolvency plan" ("*Insolvenzplan*", cf. Insolvency Act, Sections 217 *et seq*.)[27] may in the future also include binding provisions for capital measures or other remedies affecting shareholders of the debtor. Such measures could be implemented under the revised Insolvency Act if the insolvency plan is approved if the majority of creditors, including the shareholders of the debtor, and the majority of claims of each group of creditors treated in the plan vote to accept the plan. *Id.*, Section 244 of the draft Insolvency Act. Votes considered to be "obstructive" may be disregarded when certain requirements are met. If approved, also the debtors' shareholders will be bound by the plan without any need to decide on capital measures or the like in a shareholders meeting. This proposed new law would also facilitate debt for equity swaps. The overall aim of this legislative proposal is to render German insolvency proceedings more attractive and to avoid migration of companies for restructuring or insolvency purposes. It remains to be seen if the new law will enter into force as currently proposed by the Federal Ministry of Justice.

VII. United Kingdom

The United Kingdom and the United States share what has been defined as a "common law" jurisprudence, in which rules obtained from authoritative case law often add an extra dimension to and shape the boundaries of legislative acts, in contrast to the "civil law" system of Germany and the bulk of other states comprising Continental Europe. In civil law systems, the language of legislation normally governs the litigating parties rights and duties and the role of "judge-made" law is significantly less important than in common-law legal systems.

In the recent case of *Stanford International Bank Limited [2009] EWHC 1441 (Ch); [2010] EWCA Civ 137*, the English Court had to decide if it would assist the US receiver/US Department of Justice or the Antiguan liquidators and restrain the assets of Stanford International Bank Limited ("SIB") in England under the 2006 Regulations. The questions to be decided included: Were the Department of Justice's proceedings main or non-main? Were they "foreign proceedings" for the purposes of the 2006 Regulations? Under Article 16 (3) of the Model Law it is stated that "*In the absence of proof to the contrary the debtors registered office is presumed to be its COMI*." It is interesting to note that Article 16 (3) of the Model Law closely resembles Article 3 (1) of the EU Capital Regulation. The English Judge in the case of SIB, Mr. Justice Lewison, who was later supported by the Court of Appeal when the case went on appeal, noted that the respective framers of the Model Law and the EU Regulation deliberating chose to apply the same definition of COMI to then proposed legislation. As a result, Mr. Justice Lewison examined a landmark decision under the EU Regulation for guidance, namely the decision of the European Court of Justice on the question in the case of "*Eurofood*" [2006] Ch 508. Hence Mr. Justice Lewison in SIB applied a detailed analysis of the evidence to see if the presumption that SIB's COMI was its registered office location was rebutted or reinforced. In accordance with the *Eurofood* case the factors determining this had to be objective and ascertainable by third parties. Applying those standards, the judge concluded that the COMI in the case of SIB was Antigua and not the US. He also concluded that the U.S. Department of Justice's investigation was not a collective proceeding and was therefore not a "foreign proceeding" whether main or non-main. The factors applied were many and varied. The physical headquarters were in Antigua; the business was conducted on a substantial scale in Antigua; there was a large building there with 88 of the 93 employees, contracts were all under Antiguan law; some board meetings were held there; accounts were audited by Antiguan accountants in Antigua; the Company was regulated by the Antigua FSRC; certificates of deposits stated: "*executed in St John's, West Indies*"; although US investors were the largest contingent by value they did not have an overall majority by value worldwide; monthly and quarterly account statements to all creditors were sent from Antigua; the bulk of investments were outside the US.

Another significant decision relating the application of the Model Law in the UK is that of *Rubin v Eurofinance SA [2009] EWHC 2129 (Ch); [EWCA Civ 895]*. Here, the questions facing the court were: (i) whether a trust subject to New York Law (i.e. not a corporate entity and therefore having no personality under English Law) could be a "debtor" for the purposes of the 2006 Regulations; and (ii) whether the Model Law could be used to enforce in one jurisdiction a money judgment given in insolvency proceedings in another. The judge at first instance in this case held that "debtor" under the United States Bankruptcy Code included a trust and the English court should accept the American definition for that purpose. The 2006 Regulations, however, he held could not be used to enforce a judgment *in persona*. The fundamental principle of English private international law only allows such a debt to be enforced if the defendant was present within the foreign court's jurisdiction or had submitted to it. When the case went to appeal, the Court of Appeal held that the New York proceedings could be recognized as a foreign main proceeding, agreeing with the judge at first instance. However, the Court of Appeal concluded that the judgments obtained in New York adversary proceedings were obtained in the collective enforcement regime of bankruptcy proceedings and therefore were recognized under the 2006 Regulations.

Pan Oceanic Maritime Inc ("Pan Oceanic") was a company incorporated in Delaware that was the subject of a Chapter 11 case under the United States Bankruptcy Code. Pan Oceanic's trustee was a foreign representative in the American foreign main proceedings and he applied to the English Court for recognition and relief. In this case, the court held that the automatic stay provisions in Article 20 of the 2006 Regulations which came about on the recognition of foreign main proceedings were limited to: (a) protection from litigation; (b) protection from execution; and (c) suspension of rights to charge or dispose of debtors' assets. It was held that security could still be enforced. Under Article 20, paragraph 6 of the 2006 Regulations the court of its own motion could modify or terminate the stay. The Pan Oceanic decision [14 May 2010 - unreported] also was to the effect that under Article 21 of the

2006 Regulations, the automatic stay could be extended and made available to all recognized foreign proceedings (main or non-main). Furthermore, once a foreign proceeding had gained access to the UK insolvency law through the 2006 Regulations, the extensive powers of the English court included relief under paragraph 43 B1 of the Insolvency Act 1986 (UK Administration Proceedings) and the Court could under that paragraph require a stay on the enforcement of security. In this case, therefore, we see the automatic stay under Article 20 of the 2006 Regulations being supplemented by the English Court ordering a restriction on enforcement of securities in the terms of Paragraph 43 Schedule B1 of the Insolvency Act 1986.

As explained above, the EU Regulation is a pan-European regulation which creates a framework for immediate recognition of orders relating to the opening, conduct and closure of insolvency proceedings within the EU. Its effect is to prevent competition for assets between insolvencies of the same company in different Member States and duplication of costs. Under Article 3 (1) relating to primary proceedings it is stated that "*[t]he courts of the Member State within the territory of which the centre of the debtor's main interests is situated shall have jurisdiction to open insolvency proceedings. In the case of a company or legal person, the place of the registered office shall be presumed to be the centre of its main interests in the absence of proof to the contrary*." Under Article 3 (2), which relates to secondary proceedings, it is stated that the courts of another Member State have jurisdiction to open proceedings only if the debtor has an establishment in that state. These proceedings may only be winding up proceedings and they will be secondary proceedings.

There have been a proliferation of reported cases in the insolvency of *Nortel Networks Corp [2009] EWHC 206 (Ch)*. A significant decision relates to the two roles of Article 3 (1) and Article 3 (2). Nortel SA and eighteen group companies obtained administration orders from the English court on 14 January 2009. They were primary proceedings under Article 3 (1) of the EU Regulation. There were other EU Member States in which secondary proceedings under Article 3 (2) of the EU Regulation could be issued but this would have destroyed the rescue plan. To prevent this from happening the English judge fashioned a creative, "common law" solution by invoking his inherent jurisdiction and applying decisions of other EU Member States in order to achieve a reasonable and workable solution. The English judge directed letters of request to go to the courts in the other EU jurisdictions requesting that: (i) notice to be given to the English administrators of any application for secondary proceedings to be opened; and (ii) the English administrators were to be allowed to put their case in opposition to any such secondary proceedings. The basis of the English judge's authority to order letters of request were as follows: Article 31 of the EU Regulation states that officeholders in any concurrent proceedings have a duty to co-operate. In the European case of *Re Stojevic 2004*, the Vienna Higher Regional Court allowed Article 31 to extend to letters of a request between courts. Finally, in the case of *Rover France SA* it was stated that the opening of secondary proceedings was only to be allowed if they were "purposeful." In the case of Nortel it would be demonstrated by the administrators that the opening of secondary proceedings would hinder the viable rescue plan and would therefore not be purposeful.

VIII. Conclusion

As this article demonstrates, the law of cross-border insolvency proceedings, while being nothing new, has undergone a far-reaching and intense development since the early 1990s, which process has been spurred on by the fast pace of global economic integration. Two supranational organizations, the United Nations and the European Union, have led the way by creating separate, integrated legal mechanisms for coordinating insolvency proceedings of the same entity or related entities pending concurrently in two or more states. While the frameworks of the Model Law and the EU Regulation have established the general superstructure of these two different, but in many ways similar, systems, the task of filling in the gaps remains. As we have seen, national legislatures and courts are performing this task and fashioning solutions to problems not anticipated when the Model Law and the EU Regulation were born. One can only hope that this "policy of letting a hundred flowers blossom and a hundred schools of thought contend"[28], will result in a rich, diverse and creative legal fabric to resolve the multitude of problems arising in insolvency cases involving the legal systems of different lands.

Footnotes:

1. One commentator has described cross-border insolvency cases as involving "either a single case where the debtor's assets are located in multiple jurisdictions or the insolvency of multiple members of a cross-border group resulting in concurrent insolvency proceedings in multiple jurisdictions." Paul H. Zumbro, *Cross-border Insolvencies and International Protocols - an Imperfect but Effective Tool*, 11 Bus. L. Int'l 157, 160 (May 2010).

2. Bob Wessels, et al., *International Cooperation in Bankruptcy and Insolvency Matters*, 72 (Oxford Univ. Press 2009).

3. *Id.* at 74.

4. *Id.* at 159-59. *See also* Kurt H. Nadelmann, *Bankruptcy Treaties*, 93 U. Pa. L. Rev. 58 (1944).

5. COMI is a concept that is used in both the Model Law and

the European Union's Insolvency Regulation, although the term is defined in neither. Article 16(3) of the Model Law provides the presumption that a debtor's "registered office, or habitual residence" in the case of an individual, is the debtor's COMI "in the absence of proof to the contrary." Article 3 of the EU Regulation contains a similar, although not identical, presumption.

6. The Regulation does not define COMI. Therefore, the issue of jurisdiction of where cross-border insolvency cases must be opened as determined by the debtor's COMI has been heavily litigated in the European Union. *See, e.g.*, the Eurofood decision of the European Court of Justice, 2 May 2006 (Case C - 341/04) (*Eurofood*). *See also* Samuel L. Bufford, *Center of Main Interest, International Insolvency Case Venue, and Equality of Arms: The Eurofood Decision of the European Court of Justice*, 27 NW J. Int'l L. & Bus. 351 (Winter 2007).

7. The definition of "establishment" in the Regulation is similar to the definition of that same term as used in the Model Law. Article 2(h) of the Regulation defines "establishment" as "any place of operations where the debtor carries out a non-transitory economic activity with human means and goods."

8. The Regulation also provides for "territorial proceedings," which are essentially secondary proceedings commenced prior to the opening of a main proceeding. Regulation, Article 3(4). As used in this article, the discussion concerning secondary proceedings encompasses territorial proceedings.

9. *See, e.g.*, *Altos Hornos de Mexico, S.A. de C.V.*, a suspension of payments case which was commenced in 1999.

10. Prior to the conciliation phase, companies usually have to undergo an examination phase to see if they are eligible for concurso. This phase lasts, on the average, 45 days. The only exception to this phase is the pre-packaged concurso case which was incorporated into to the Concurso Law at the end of 2007.

11. The full year term requires approval from the majority of creditors.

12. Section 304 of the United States Bankruptcy Code, repealed in 2005, was the precursor of Chapter 15.

13. See footnote 10.

14. Durango's second time was not a pre-negotiated arrangement and in fact the company faced litigation before securing an agreement with creditors.

15. The Insolvency Act of 2000 was a new law replacing older

insolvency laws (*Konkursordnung und Vergleichsordung*). Earlier drafts of the new Insolvency Act of 2000 did include a separate section on cross-border insolvencies (Sec. 379 *et seq.*). However, with a view to ongoing negotiations regarding the European Insolvency Treaty (the predecessor of the European Insolvency Regulation), these sections were stricken from the draft and the new Insolvency Act went into force on January 1, 2000 with just one provision addressing cross-border insolvencies.

16. In this respect also Denmark does not qualify as a Member State, since Denmark is not participating in the adoption of the Regulation. *See* Recital 33 of the Regulation.

17. High Court of Justice Leeds, ZIP 2003, 1362; High Court of Justice Leeds, ZIP 2004, 963; see further Westphal/Goetker/Wilkens, Grenzüberschreitende Insolvenzen (2008), Rn. 124.

18. See Westphal/Goetker/Wilkens, Grenzüberschreitende Insolvenzen (2008), Rn. 124.

19. AG München, ZIP 2004,962; AG Siegen, EWiR 2005, 175; AG Offenburg, EWiR 2005, 73; but see AG Mönchengladbach, ZIP 2004, 1064.

20. European Court of Justice, 2 May 2006 (Case C - 341/04) (*Eurofood*).

21. In both cases, company voluntary arrangements under English law including a debt-equity swap were employed.

22. *E.g.* Hans Brochier GmbH & Co. KG; Local Court (*Amtsgericht*) of Nuremberg, decision (*Beschluss*) of October 1, 2006 - 8034 IN 1326/06 and decision (*Beschluss*) of August 15, 2006 - 8004 IN 1326-1331/06.

23. Similar to the Company Voluntary Arrangements under the English Insolvency Act 1996.

24. *See* Recital 4 of the Regulation.

25. Referentenentwurf des Bundesjustizministeriums für ein Gesetz zur weiteren Erleichterung der Sanierung von Unternehmen (ESUG) of January 25, 2011.

26. The draft act includes further amendments which are not relevant here.

27. A German insolvency plan (*Insolvenzplan*) may currently deal with all issues concerning the satisfaction of creditors' claims, the sale of the debtor's assets and the distribution of sale proceeds as well as the debtor's liability after termination of the

insolvency proceedings, also deviating from the provisions of otherwise applicable law. Section 217, Insolvency Act. Furthermore, the insolvency plan may include provisions impairing security rights of creditors and may contain additional undertakings of single creditors. However, to date an insolvency plan may not include provisions affecting the debtor's shareholders in their capacity as shareholders. All insolvency plans must be submitted to the court for review and approval. If approved by the court, the plan will be submitted to a creditors' meeting for approval. The insolvency plan will be approved if the majority of creditors and the majority of claims of each group of creditors set out in the plan vote to accept the plan. Section 244, Insolvency Act.

28. Mao Zedong, On the Correct Handling of the Contradictions Among the People, February 27, 1957.

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Announcements (Seminar)

The FBA - Bankruptcy Section will hold its annual seminar on July 28 - 30, 2011 at Boyne Mountain Resort, Boyne Falls, Michigan. Registration information can be found at http://www.miwb.uscourts.gov/cms/assets/Home/Court-News/FBA-Seminar.pdf.

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