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Fifth Circuit Holds Foreign Representatives May Bring Foreign Law Avoidance Actions Under Chapter 15 of the Bankruptcy Code

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The United States Court of Appeals for the Fifth Circuit recently held that foreign representatives appointed in a foreign insolvency proceeding have the authority to bring a foreign law based avoidance action in an ancillary bankruptcy proceeding commenced under Chapter 15 of the Bankruptcy Code, reversing the lower court opinions. The authors of this article explain this decision and its implications.

The United States Court of Appeals for the Fifth Circuit has ruled that foreign representatives appointed in a foreign insolvency proceeding have the authority to bring a foreign law based avoidance action in an ancillary bankruptcy proceeding commenced under Chapter 15 of the Bankruptcy Code, reversing the lower court opinions. This opinion is significant because it is the first published circuit court decision on this discrete issue and overrules the apparent understanding that foreign representatives may not pursue avoidance actions in Chapter 15 cases.

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BACKGROUND

Condor Insurance, Limited ("CIL") is a Nevis corporation that operated an insurance and surety bond business. In November 2006, one of CIL's creditors initiated a winding up proceeding, (the equivalent of a Chapter 7 bankruptcy proceeding under the Bankruptcy Code), against CIL. In May 2007, Richard Fogerty and William Tacon were appointed as the Joint Official Liquidators of CIL (hereinafter, the "Foreign Representatives").

The Foreign Representatives filed a Chapter 15 bankruptcy proceeding in the United States Bankruptcy Court for the Southern District of Mississippi. Chapter 15 of the Bankruptcy Code permits foreign representatives to seek assistance from United States' courts in an ancillary proceeding once the foreign proceeding is "recognized" by the bankruptcy court. The bankruptcy court recognized the Nevis winding up proceeding as a foreign main proceeding, which is a foreign proceeding pending in the country where the debtor has the center of its main interests. Thereafter, the Foreign Representatives initiated an adversary proceeding against Condor Guaranty, Inc. and several other companies (collectively, "CGI"), seeking to avoid, under Nevis law, over $313 million in assets that were fraudulently transferred by CIL to CGI. CGI filed a motion to dismiss the Foreign Representatives' adversary proceeding, and the bankruptcy court granted the motion on the basis of lack of subject matter jurisdiction, reasoning that a foreign representative is not authorized to bring an avoidance action to set aside prepetition transfers in a Chapter 15 case. The Foreign Representatives appealed and the district court affirmed.

THE RELEVANT CODE PROVISIONS

The two sections of Chapter 15 at issue are §§ 1521 and 1523 of the Bankruptcy Code. Section 1521 provides courts the discretion to grant any appropriate relief that is necessary to effectuate the purpose of Chapter 15 and to protect the assets of the debtor or the interest of creditors, with the exception of avoidance powers that are available under certain provisions of the Bankruptcy Code. Specifically, the provision states that a bankruptcy court may grant "any appropriate relief," including staying various aspects

of the proceedings, suspending the right to transfer assets of the debtor, providing for discovery, granting the foreign representative administrative powers and "granting any additional relief that may be available to a trustee, except for relief available under sections 522, 544, 545, 547, 548, 550 and 724(a)."[1] Nevertheless, § 1523 permits a foreign representative to initiate these excluded avoidance actions in a full Chapter 7 or 11 case. Here, however, the Foreign Representatives did not have the option of filing a Chapter 7 or 11 case in the United States because foreign insurance companies that have not conducted business in the United States, such as CIL, may not be debtors in a case under Chapter 7 or 11 of the Bankruptcy Code.

Thus, the core issue before the district court was whether §§ 1521(a)(7) and 1523 restrict a foreign representative from commencing an avoidance action under the Bankruptcy Code only, or also under foreign law. The Foreign Representatives asserted that they were seeking relief under Nevis law, not United States law, such that the plain language of the statute merely prohibits them from using certain sections of the Bankruptcy Code when seeking avoidance and accordingly, they are not prohibited from relying on the avoidance actions available under the applicable foreign law. The parties did not disagree, however, over the fact that the plain language of §§ 1521(a)(7) and 1523 does not expressly address the use of avoidance powers under foreign law, and that no applicable case-law authority exists on this specific disputed issue. The district court held that Congress intended §§ 1521(a)(7) and 1523 to relegate avoidance actions, *under both United States and foreign law*, to a full Chapter 7 or 11 bankruptcy case.[2] The district court's conclusion, however, was not supported by anything specifically in the legislative history on which it based its decision.[3]

THE CIRCUIT COURT OPINION

On March 17, 2010, Judge Higginbotham of the circuit court reversed the decision of the district court, holding that bankruptcy courts do indeed have jurisdiction and authority to offer avoidance relief under foreign law in a Chapter 15 bankruptcy proceeding.[4] The circuit court commenced its decision by explaining that Chapter 15 implements the United Nations Commission on International Trade Law Model Law on Cross-Border In-

solvency (the "UNCITRAL Model Law"), which represents a culmination of a long-standing effort by almost 40 countries to develop a uniform system guiding needed cooperation. The UNCITRAL Model Law was intended to be integrated into local insolvency law and it was expected that any departures therefrom were to be as narrow and limited as possible in an effort to harmonize international bankruptcy proceedings.

Next, the circuit court addressed the list of excluded avoidance actions from § 1521(a)(7) of the Bankruptcy Code. This list of exclusions does not exist in the Model Law, and Chapter 15 is silent regarding proceedings that apply foreign law, including any rights of avoidance such law may offer. The circuit court reasoned that "where there are enumerated exceptions additional exceptions are not to be implied, in the absence of a contrary legislative intent."[5] Judge Higginbotham opined that if Congress wished to bar all avoidance actions, including under foreign law, it could have and should have explicitly so stated.[6]

The circuit court's rationale was based largely on its interpretation of the purpose of Chapter 15, which includes furthering cooperation between U.S. courts, parties in U.S. bankruptcy proceedings and insolvency courts and authorities, as well as promoting greater legal certainty, and fair and efficient administration of cross-border insolvencies.[7] Judge Higginbotham stated that the "silence [of the statute] is loud," given the history of the United States to rescue financially troubled transnational businesses and the structure of Chapter 15 that suggests an expansive reading of the powers granted to courts in order to advance the goals of comity to foreign jurisdictions.[8]

The circuit court also rationalized that because foreign insurance companies may not bring a Chapter 7 or 11 proceeding in the United States, precluding foreign representatives from initiating an ancillary fraudulent conveyance action might induce debtors to hide assets in the United States outside of the reach of the foreign jurisdiction. The last basis of support for the circuit court's decision is that pursuant to case-law under § 304 of the Bankruptcy Code, the predecessor to Chapter 15 which was repealed by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), avoidance actions under foreign law were permitted when foreign law applied. Congress is presumed not to have overturned precedent when amending the Bankruptcy Code and it intended for courts to consider § 304 case-law in interpreting the scope of Chapter 15.[9]

IMPLICATIONS AND CONCLUSION

One potential concern, which was raised by CGI, of allowing foreign representatives to use foreign avoidance law is that it might encourage "section shopping" (or Chapter shopping) by giving to foreign representatives the option to bring a Chapter 15 ancillary proceeding when using foreign law would be more favorable and a Chapter 7 or 11 proceeding when U.S. law would be more beneficial. As the circuit court noted, however, by allowing foreign representatives to pursue avoidance actions available under foreign law, Chapter 15 does not provide foreign representatives with any powers they do not already have under foreign law.

Although the statute may not be unambiguous on this point, prior to the circuit court's decision it was generally presumed that § 1521(a) authorizes any additional relief that may be available to a trustee with the *exception of* the exercise of avoidance powers, and avoidance powers were generally understood to only be available to foreign representatives in a full case under another chapter of Title 11, such as Chapter 7 or 11.[10] Accordingly, the circuit court decision clearly departs from the restriction that BAPCPA was understood to place on foreign representatives who seek to bring avoidance actions in the United States.

NOTES

[1] 11 U.S.C. § 1521(a)(7).
[2] *In re Condor Ins. Ltd.*, 411 B.R. 314 (S.D. Miss. 2009).
[3] *See In re Atlas Shipping*, 404 B.R. 726, 744 (Bankr. S.D.N.Y. April 27, 2009) (questioning the reasoning of the district court in the *Condor* case).
[4] *In re Tacon v. Petroquest Res. Inc. (In re Condor Ins. Ltd.)*, 2010 U.S. App. LEXIS 5635 (5th Cir. 2010).
[5] *Id.* at *11.
[6] *Id*.
[7] *Id*. at *12-13.
[8] *Id*. at *13-15.
[9] *Id*. at * 23-26.
[10] *See* Collier on Bankruptcy ¶ 1521.02 (2009).