Stays Without Borders in Chapter 15?
"Maybe" Says a New York Bankruptcy Court

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October 17, 2010, marked the five-year anniversary of the effective date of chapter 15 of the Bankruptcy Code, which was enacted as part of the comprehensive bankruptcy reforms implemented under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005. Governing cross-border bankruptcy and insolvency cases, chapter 15 is patterned after the Model Law on Cross-Border Insolvency (the "Model Law"), a framework of legal principles formulated by the United Nations Commission on International Trade Law in 1997 to deal with the rapidly expanding volume of international insolvency cases. The Model Law has now been adopted in one form or another by 19 nations or territories.

The jurisprudence of chapter 15 has evolved consistently since 2005, as courts have transitioned from considering the theoretical implications of a new legislative regime governing cross-border bankruptcy and insolvency cases to confronting the new law's real-world applications. An important step in that evolution was the subject of a ruling recently handed down by the U.S. Bankruptcy Court for the Southern District of New York. In *In re JSC BTA Bank*, the court, addressing a matter of apparent first impression, ruled that the automatic stay triggered when a U.S. court issues an order recognizing a foreign main proceeding under chapter 15 does not prevent non-U.S. creditors from continuing to prosecute a foreign arbitration proceeding that does not involve the foreign debtor's U.S. assets.

Procedures and Relief Under Chapter 15

Under chapter 15, a duly accredited representative of a foreign debtor may file a petition in a U.S. bankruptcy court seeking "recognition" of a "foreign proceeding." "Foreign proceeding" is defined as:

> a collective judicial or administrative proceeding in a foreign country, including an interim proceeding, under a law relating to insolvency or adjustment of debt in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation.

Because more than one bankruptcy or insolvency proceeding may be pending against the same foreign debtor in different countries, chapter 15 contemplates recognition in the U.S. of both a "main" proceeding—a case pending in the country that contains the debtor's "center of main interests"—and "nonmain" proceedings, which may have been commenced in countries where the debtor merely has an "establishment."

Upon recognition of a foreign "main" proceeding, certain provisions of the Bankruptcy Code automatically come into force, while others may be deployed in the bankruptcy court's discretion by way of "additional assistance" to the foreign representative. Pursuant to section 1520(a)(1), provisions that automatically apply upon recognition include the automatic stay in section 362 and the right to "adequate protection" in section 361 "with respect to the debtor and the property of the debtor that is within the territorial jurisdiction of the United States."

By contrast, if the foreign proceeding is recognized as a "nonmain" proceeding, the bankruptcy court may, but is not required to, grant a broad range of provisional and other relief designed to

preserve the foreign debtor's assets or otherwise provide assistance to a main proceeding pending elsewhere.

Notably, chapter 15, unlike the other chapters of the Bankruptcy Code, does not incorporate the concept of a bankruptcy estate consisting of the foreign debtor's property as of the bankruptcy filing date.

Scope of the Automatic Stay

Section 362(a) of the Bankruptcy Code provides that the filing of a bankruptcy petition under section 301, 302, or 303 operates as a stay, "applicable to all entities" of, among other things: (i) the commencement or continuation of any judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced prior to the petition date; and (ii) any act to obtain possession of property of the debtor's bankruptcy estate or to exercise control over property of the estate.

Section 541 of the Bankruptcy Code defines "estate property" to include a broad range of property belonging to the debtor as of the petition date, "wherever located and by whomever held." Similarly, the general jurisdictional mandate statutorily conferred upon U.S. district courts (of which bankruptcy courts are units) extends to "all of the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate" pursuant to 28 U.S.C. § 1334(e)(1).

On the basis of these provisions, some courts have ruled that the scope of the automatic stay extends beyond the territorial boundaries of the U.S. in "plenary" bankruptcy cases (*i.e.*, "full-

fledged" cases filed under chapter 7, 9, 11, 12, or 13). Whether the stay operates extraterritorially in a chapter 15 case was the subject of the court's ruling in *JSC BTA Bank*.

JSC BTA Bank

JSC BTA Bank ("BTA Bank"), one of the largest banks in the Republic of Kazakhstan, borrowed $20 million in 2008 from a Swiss bank to finance the construction of an entertainment complex in Moscow. The loan agreement is governed by Swiss law and obligates the parties to submit any disputes arising from the agreement to arbitration in Switzerland. BTA Bank defaulted on its obligations under the loan agreement in August 2009.

On October 16, 2009, BTA Bank commenced a reorganization proceeding in Kazakhstan. That proceeding was recognized as a "foreign main proceeding" in December 2009 in Great Britain and in February 2010 in Ukraine (both of which have adopted the Model Law). The U.S. Bankruptcy Court for the Southern District of New York issued an order recognizing the Kazakh reorganization as a foreign main proceeding under chapter 15 on March 2, 2010. The recognition order, which was issued after an uncontested hearing, granted BTA Bank:

> all of the relief set forth in section 1520 of the Bankruptcy Code including, without limitation, the application of the protection afforded by the automatic stay under section 362(a) of the Bankruptcy Code to the Bank worldwide and to the Bank's property that is within the territorial jurisdiction of the United States.

In the meantime, however, BTA Bank's Swiss lender had commenced an arbitration proceeding on October 29, 2009, against BTA Bank in Switzerland seeking a determination that BTA Bank had breached the loan agreement and was liable for the amount of the loan, including damages and interest. BTA Bank filed a statement of defense in the arbitration proceeding on June 21,

2010, claiming that continuation of the arbitration violated the U.S. recognition order because "the U.S. Recognition Order grants a worldwide stay of court and arbitration proceedings."

The arbitrator, taking the position that the U.S. recognition order did not stay the arbitration, issued an award in the proceeding in the Swiss bank's favor on July 19, 2010. Shortly thereafter, BTA Bank's foreign representative filed a motion in the U.S. bankruptcy court seeking an order confirming that the U.S. recognition order stayed the arbitration proceeding and sanctioning the Swiss bank for willfully violating the stay.

The Bankruptcy Court's Ruling

Bankruptcy judge James M. Peck denied the motion. On the basis of the plain meaning of section 1520(a)(1), Judge Peck determined that the provision stays actions against a foreign debtor within the U.S., but applies outside the U.S. only to the extent that such actions affect property of the debtor that is "within the territorial jurisdiction of the United States." In keeping with chapter 15's "international origins" and the explicit instruction in section 1508 to consider those origins in construing the meaning of specific provisions, Judge Peck stated, chapter 15 cases are different from plenary bankruptcy cases in certain key respects. These differences, he explained, include a more restrictive definition of the term "debtor" in chapter 15 and the absence of a bankruptcy estate created upon the "commencement" of a chapter 15 case.

Judge Peck rejected the foreign representative's argument that the language of section 1520(a)(1)—applying the stay "to the debtor and the property of the debtor that is within the territorial jurisdiction of the United States"—must be interpreted to distinguish between the debtor, on the one hand, and its property, on the other:

> This interpretation . . . is focused too narrowly on scanning the words and ignores the ancillary nature of chapter 15, the specialized definition of the word "debtor," and the interpretive mandate of section 1508. It would be contrary to the essential purposes and structure of a chapter 15 case for recognition of a foreign main proceeding to stay a commercial arbitration proceeding as remote as this one—a proceeding in Switzerland between two foreign banks relating to a loan transaction that has no connection to the United States or to any property of the chapter 15 debtor "that is within the territorial jurisdiction of the United States."
>
> This concept of territorial jurisdiction is an essential aspect of promoting cooperation and greater legal certainty in cross-border cases. The phrase "within the territorial jurisdiction of the United States," as defined in section 1502(8), highlights the *in rem* nature of jurisdiction in a chapter 15 case and refers to tangible property within the territory of the United States and intangible property deemed under applicable nonbankruptcy law to be located within this country. . . . The definition is a source of clarity with respect to the intended scope of the automatic stay in a chapter 15 case—it applies only to property within the United States. As such, this territorial delineation serves to eliminate any doubt as to the extent of the authority of the bankruptcy court over property of a foreign debtor.

On the basis of his analysis, Judge Peck ruled that the stay arising in a chapter 15 case upon recognition of a foreign main proceeding "applies to the debtor within the United States for all purposes *and may extend to the debtor as to proceedings in other jurisdictions for purposes of protecting property of the debtor that is within the territorial jurisdiction of the United States*" (emphasis added).

Because the Swiss arbitration proceeding had "no connection to the United States and no conceivable impact on debtor property in this country," Judge Peck concluded, the arbitration was not stayed upon recognition in the U.S. of BTA Bank's Kazakh reorganization proceeding under chapter 15. However, in dicta, the judge wrote, "[r]egardless of its venue in another country," an arbitration proceeding with different facts that might involve a determination of the rights of a third party in property of a foreign debtor that is within the territorial jurisdiction of

the U.S. “would be subject to the automatic stay under the interpretation of section 1520(a)(1) articulated in this ruling.”

Acknowledging the absence of any precedent under chapter 15 applying (or refusing to apply) the automatic stay on a worldwide basis, Judge Peck found the rulings relied on by the foreign administrator to be inapposite because they involved plenary bankruptcy cases. According to the judge, “The global reach described in these chapter 11 cases has no relation to the shared jurisdictional model of a chapter 15 case that is an adjunct to a foreign proceeding.” Unlike the “worldwide estate” created in a plenary bankruptcy case, Judge Peck wrote, there is no bankruptcy estate in a chapter 15 case, and “a bankruptcy court’s jurisdiction over property of the debtor is expressly limited to property located ‘within the territorial jurisdiction of the United States.’ ”

Judge Peck concluded that the foreign representative’s position on this issue would convert recognition of a foreign main proceeding under chapter 15 into the “granting, by operation of law, of a worldwide anti-suit injunction as to any proceeding against the debtor, regardless of subject matter, that may be pending or threatened against the foreign debtor in any country around the globe.” “The absurdity of such a far reaching result,” he wrote, “is obvious”—and clearly at odds with the intent of lawmakers in enacting chapter 15.

Finally, Judge Peck explained, his ruling is supported by both “equitable and practical concerns.” Principles of judicial restraint warranted by the absence of any contacts between the U.S. and the dispute subject to arbitration, he emphasized, militate against any “needless intervention by the

bankruptcy court." Equitable concerns also counsel restraint, he wrote, because "[t]he effort comes too late to affect the outcome of the Arbitration Proceeding."

Given his conclusions regarding the inapplicability of the automatic stay, Judge Peck ruled that the Swiss bank should not be sanctioned for its conduct with regard to the arbitration proceeding.

Outlook

JSC BTA Bank is consistent with the purpose of chapter 15 as a mechanism to provide assistance in the U.S. to qualifying foreign bankruptcy and insolvency proceedings involving debtors with assets located in the U.S. Like its predecessor—section 304 of the Bankruptcy Code—chapter 15 was designed to provide for a limited "ancillary" proceeding acting in concert and cooperation with main proceedings pending in a foreign jurisdiction. Judge Peck's ruling in *JSC BTA Bank* underscores some of chapter 15's significant limitations in keeping with its international origins and goals.

The ruling also fits neatly within the infrastructure erected around the Model Law, at least in countries where some version of the Model Law has been adopted. Under the Model Law, if a debtor's assets are threatened by creditor collection efforts in a jurisdiction other than the nation where a main bankruptcy or insolvency proceeding is pending, a representative of the debtor can seek injunctive relief from the courts of the nation in question by seeking recognition of the host nation's proceeding. As such, an injunction with extraterritorial reach is unnecessary in Model Law countries. This construct breaks down, however, if the situs of assets or creditor collection initiatives aimed at either the debtor or its property is a non-Model Law country. In such cases, a debtor or its representative would most likely be forced to rely upon principles of comity under

international law or other less wieldy remedies than the Model Law to prevent piecemeal dismantling of assets by local creditors.

A version of the Model Law has now been enacted in Australia (2008); the British Virgin Islands, an overseas territory of the United Kingdom of Great Britain and Northern Ireland (2003); Canada (2009); Colombia (2006); Eritrea (1998); Great Britain (2006); Greece (2010); Japan (2000); Mauritius (2009); Mexico (2000); Montenegro (2002); New Zealand (2006); Poland (2003); the Republic of Korea (2006); Romania (2003); Serbia (2004); Slovenia (2007); South Africa (2000); and the United States (2005). In the U.S., the volume of chapter 15 filings has generally expanded since 2005. Calendar years 2006, 2007, 2008, and 2009 saw 74, 42, 76, and 131 chapter 15 filings, respectively. 135 chapter 15 cases were filed in the U.S. in 2010.

In re JSC BTA Bank, 434 B.R. 334 (Bankr. S.D.N.Y. 2010).

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