MLA COMMITTEE ON MARITIME BANKRUPTCY AND INSOLVENCY

CMI CROSS BORDER INSOLVENCY IWG

JOINT MEETING – NEW YORK, NEW YORK

MAY 4, 2016

DISCUSSION TOPICS

Chairs:

John E. Bradley (Chair, MLA Committee on Maritime Bankruptcy and Insolvency)
Christopher O. Davis (Chair, CMI Cross Border Insolvency IWG)

Guests:

Judge Robert Gerber (Retired, SDNY Bankruptcy)
Justice Stephen Rares (Federal District Court Australia)
Professor Martin Davies (Tulane Law School)

PARTIAL LIST OF DISCUSSION TOPICS

ISSUE NO. 1: ABSTENTION IN PLENARY CASES

The U.S. Bankruptcy Courts have attracted the filing of numerous plenary cases (Chapters 7 and 11) by foreign shipping companies having no local creditors or debt, no trading patterns involving the United States, and no offices, personnel, bank accounts or tangible presence in the United States other than a "peppercorn" retainer paid to U.S. bankruptcy counsel. Such cases are often commenced for the purpose of obtaining strategic leverage over foreign lenders and creditors. Given the easily met debtor "eligibility" requirements under Section 109(a) of the Bankruptcy Code (the "**Code**"), what legal standards should govern a bankruptcy court's decision to abstain and dismiss a plenary case under Section 305 of the Code? The National Bankruptcy Conference ("**NBC**") has recommended an amendment to Section 305 which would permit dismissal if "*the debtor's center of main interests is not the United States and the court cannot exercise effective control over either the debtor or the debtor's material assets.*" How would such an amendment affect the ability of foreign shipping companies seeking debt relief in the United States?

ISSUE NO. 2: DEBTOR PRESENCE IN THE U.S.: REQUIRED FOR CHAPTER 15?

Section 109 of the Code states that "only a person that resides or has a domicile, a place of business, or property in the United States … may be a debtor under this title." Does this eligibility requirement apply as a condition to Chapter 15 recognition by a U.S. bankruptcy court? The Second

Circuit in *Drawbridge Special Opportunities Fund, L.P. v. Barnet (In re Barnet)*, 737 F.3d 238 (2d Cir 2013) says yes. The NBC and almost everyone else says no. *See e.g., In re Bemarmara Consulting A.S.*, Case No. 13-13037 (Bankr. D. Del. Dec. 17, 2013) If the answer is yes, how does a foreign representative manufacture eligibility where there the foreign debtor has no U.S. presence?

ISSUE NO. 3: CENTER OF MAIN INTERESTS ("**COMI**"): WHEN MEASURED

To seek U.S. recognition of a foreign insolvency proceeding, a qualified foreign representative appointed in connection with a foreign insolvency proceeding must file a petition for relief under Chapter 15 of the Code. A foreign insolvency proceeding may be a "foreign main proceeding" or a "foreign nonmain proceeding." A foreign proceeding will be recognized in the U.S. as a foreign main proceeding "if it is pending in the country where the debtor has the center of its main interests." A foreign proceeding will be recognized as a foreign nonmain proceeding if it takes place in a jurisdiction where the debtor has an "establishment." The distinction is important because of the benefits automatically obtained under Chapter 15 in circumstances where a foreign insolvency proceeding is recognized as a foreign main proceeding.

When should a debtor's COMI be measured by the court of ancillary jurisdiction? There appears to be a split on this issue. The UNCITRAL Model Law on Cross-Border Insolvency (the "**Model Law**") would measure COMI as of the date that the foreign insolvency proceeding is filed. At least one influential court in the United States has held that COMI should be measured as of the date of a Chapter 15 filing subject to an inquiry into whether the process has been manipulated by the debtor.[1] *See Morning Mist Holdings, Ltd. v. Krys (In re Fairfield Century)*, 714 F.3d 127 (2d Cir. 2013). NBC recommends that Chapter 15 be amended so that it is aligned with the Model Law.

The timing issue is of importance to shipping debtors that are organized (but not doing business) in so-called letterbox jurisdictions such as the Cayman Islands, the British Virgin Islands, etc. The "European Court of Justice used the 'letterbox' appellation to describe a company 'not carrying out any business in the territory of the Member State in which its registered office is situated,' and which thus might present an instance where the presumption that the COMI is the registered place of business could be overcome." *In re Creative Finance Lt. (in Liquidation), et al.*, *Decision and Order on Motion for Recognition and Cross-Motion for Dismissal*, footnote 6 Chapter 15, Case No. 14-10358 (REG) (Bankr. SDNY Jan. 13, 2016) How much of a presence must be established in a letterbox jurisdiction in order for COMI to be fixed there?

ISSUE NO. 4: QUIETING OF MARITIME LIENS BY BANKRUPTCY COURTS

In *Universal Oil Ltd. v. Allfirst Bank,* 419 F.3rd 83 (2d Cir. 2005) (*In re Millenium Seacarriers*), the U.S. Court of Appeals for the Second Circuit observed the complexities of a U.S. bankruptcy court selling a ship free and clear of maritime liens: "When a debtor's estate consists primarily of maritime assets, …, a measure of uncertainty exists the propriety of the bankruptcy court's jurisdiction to sell those assets wholly free of maritime liens." *Id.* at 27-28 The Court further stated: "While bankruptcy courts have adjudicated the validity and priority of maritime liens asserted debtors' maritime assets for nearly a century, the particular question of whether a bankruptcy court may enforce and foreclose maritime liens over a lienor's objections has not been conclusively settled." *Id.*

[1] In order to address manipulation, a court may review the period between the date of filing of the the foreign insolvency and the date of filing of the Chapter 15 proceeding.

at 30-31 (citations omitted) Can a U.S. bankruptcy court extinguish the maritime liens of non-participating foreign maritime lienors (over whom the court has no jurisdiction) through a ship sale authorized under Section 363 of the Code?

ISSUE NO. 5: EU CARVE-OUT FOR IN REM CLAIMS

The EU's Recast Insolvency Regulation[2] and will apply from 26 June 2017. Under Article 8 of the new regulation, the "opening of insolvency proceedings shall not affect the rights of *in rem* creditors or third parties in respect of tangible or intangible, moveable or immovable assets, both specific assets and collections of indefinite assets as a whole which change from time to time, belonging to the debtor which are situated within the territory of another Member State at the time of the opening of the proceedings." The rights preserved by new Article 8 include the right to dispose of assets or have them disposed by virtue of a lien or mortgage. Should a protocol to the Model Law which provides for a similar carve-out be entertained?

ISSUE NO. 6: STATUS OF CHARTER PARTIES IN BANKRUPTCY

Under traditional rules of admiralty, when an owner of a vessel under charter breaches that charter, the charterer possesses a maritime lien enforceable *in rem* against the vessel and that lien traditionally "relates back" to the date of the charter. Conversely, when a charterer of a vessel under charter breaches that charter, the owner of the vessel very often possesses a maritime lien enforceable *in rem* against freights and sub-freights and that lien traditionally relates back to the date of the charter. As recent cases have shown, when that charterer or owner becomes a Chapter 11 debtor, the bankruptcy courts are called upon to balance the debtor's need for relief and the competing lien claims against the vessels, freights or sub-freights belonging to the debtor. Charter parties in effect as of the commencement date of a Chapter 11 case are treated as unexpired leases which are subject to assumption or rejection by the debtor. However, in the absence of Creditor Committee support, how are maritime lien claims protected and preserved in a fast-moving Chapter 11? Does Section 546(b) of the Code provide the best answer?

ISSUE NO. 7: ALTERNATIVE FINANCE: ROLES AND STRATEGIES

Since the 2008 various alternative finance providers, mostly hedge funds and private equity firms, have moved into shipping, providing much-needed capital financing and occupying the investment space abandoned by traditional marine lenders. However, when shipping investments made by alternative finance providers turn sour, what strategies are pursued and how do those strategies differ from those of traditional marine lenders? How well do hedge fund and PE managers understand shipping and how have they influenced the Chapter 11 landscape??

ISSUE NO. 9: RECIPROCAL COMITY ISSUES

The nature and timing of insolvency and ship arrest proceedings has a bearing on comity issues between bankruptcy and admiralty courts. Do the arrest proceedings precede the opening of an insolvency case or do they follow it? Is the insolvency case in the nature of a reorganization or rehabilitation or is it a straight liquidation? And if an ancillary case is filed under the Model Law, do the arrest proceedings precede or follow that filing. As discussed by Professor Martin Davies of

[2] Council Regulation (E.U.) 2015/848 of the European Parliament and Council of 20 May 2015 will repeal EC Regulation No. 1356/2000.

Tulane, the answers to these questions may provide a working framework for the application of comity between bankruptcy and admiralty courts.