Chapter Three

Relief Available in the Pre-Recognition "Gap" Period

Chapter 15 provides that a foreign representative may request "relief of a provisional nature" from the filing of the petition for recognition until the court rules on the petition.[135] To obtain provisional relief, the foreign representative must demonstrate that the relief is "urgently needed" to protect the assets of the debtor or the interests of creditors.[136] The temporary remedies, which may ultimately be made permanent upon recognition, may include staying execution against the debtor's assets, entrusting the administration of the debtor's assets to a foreign representative or other authorized person, suspending the right to transfer, encumber or otherwise dispose of assets, or providing for the examination of witnesses, the taking of evidence or the delivery of information concerning the debtor's assets, affairs, rights, obligations or liabilities.[137] Additionally, the court may grant the foreign representative other relief that the Bankruptcy Code may provide to a trustee, except for relief available for the avoidance of transactions under and in accordance with §§ 522, 544, 545, 547, 548, 550 and 724(a) of the Bankruptcy Code.[138]

One aspect of provisional relief that has caused confusion in the courts is the proper procedure to obtain provisional relief. This is so because § 1519(e) provides that the "standards, procedures, and limitations applicable to an injunction shall apply to relief" sought under § 1519 of the Bankruptcy Code. Under Bankruptcy Rule 7001(7), a request for injunctive relief must be commenced by a separate lawsuit called an adversary proceeding, which may take more time and delay recognition significantly;[139] however, Bankruptcy Rule 1018 provides that only certain

135 *See* 11 U.S.C. § 1519(a).
136 *Id.*
137 *Id.*
138 *See* Chapter 6 of this manual for a discussion of the availability of avoidance actions under chapter 15 of the Bankruptcy Code.
139 For those foreign readers not familiar with procedural issues in bankruptcy, it is necessary to understand the difference between a "contested matter" and an "adversary proceeding," and to understand why the latter is often not preferred. In general, a "contested matter" is a matter with some protections of regular litigation, but not others, to ensure prompt and efficient resolution. *See generally* Fed. R. Bankr. P. 9014. An "adversary proceeding" is regular litigation regarding a discrete dispute that is subject to more formal pleading rules and more strict procedural protections. *See generally id.* 7001-7087. The significance of whether an issue is a contested matter or an adversary proceeding is that a contested matter is less formal than an adversary proceeding. Generally, the parties submit argument in writing, and a hearing is scheduled within 14 to 30 days. At the hearing, the parties appear before the court and argue for a ruling or propose a shortened process for the exchange of documents and other necessary discovery before scheduling a final hearing on the contested matter, which discovery may be similar to that as in an adversary proceeding, but it is often on a truncated basis. An adversary proceeding, on the other hand, starts when the party objecting to the claim files a complaint in which it alleges facts and states the relief it seeks (*i.e.*, money damages or claim disallowance or subordination). *See id.* at 7003. The party filing the complaint would have to serve it in accordance with the normal rules of service of process, which, with respect to a foreign party, may require service in accordance with the Hague Convention on the Service Abroad of Judicial and Extrajudicial Documents. *See id.* at 7004(a)(1) (incorporating Rule 4(f) of the Federal Rules of Civil Procedure). Once the service is effected, the defendant must either answer the complaint by admitting, denying or stating insufficient knowledge to either admit or deny the allegations in the complaint or move to dismiss the complaint. The purpose of a motion to dismiss is to test the factual sufficiency of

of the Bankruptcy Rules apply with respect to a contested petition for recognition of a foreign proceeding, and that those Rules that require commencement of a separate action by adversary proceeding do not apply. Courts have construed these provisions differently and have created some procedural confusion.[140] As we will see below, different courts take different approaches to these issues.

I. The Not-So-Automatic Stay

The most frequently litigated aspect of 11 U.S.C. § 1519 arises in the context of a request by a foreign representative for the court's imposition of the automatic stay on a provisional basis pending the entry of an order for recognition.[141] The plain language of 11 U.S.C. § 1519(a) explains that a stay of execution against the assets of a foreign debtor may only be granted upon the foreign representative's showing that such relief is "urgently needed" to protect the debtor's estate. This highlights that, unlike petitions filed under other chapters of the Bankruptcy Code that benefit from an "automatic stay," the petition for recognition under chapter 15 does not give rise to an automatic stay of execution upon which the foreign representative may immediately rely. Indeed, during the "gap period" between the filing of the petition for recognition and the court's ruling on the recognition request (which may last up to several weeks or months in a contested litigation setting), the automatic stay will not take effect absent affirmative and justified action on behalf of the foreign representative.[142]

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the factual allegations, which are accepted as true and in the light most favorable to the plaintiff, and to determine whether there are enough facts to raise a reasonable expectation that discovery will reveal evidence of the necessary elements of the claims asserted. In other words, the court presumes all of the facts plead by a plaintiff in a complaint are true and determines whether the plaintiff asserted a claim on which legal relief can be granted. If so, the defendant must answer the complaint, and the parties will pursue discovery. If not, then the court will dismiss the complaint. Discovery generally consists of written questions (called "interrogatories"), requests for production of documents, requests for admissions of facts, and oral depositions. Additionally, during this discovery period, there will be time committed to discovery of any expert testimony necessary to the litigation, including expert testimony on any relevant provisions of foreign law. When discovery ends, if there are no disagreements on material facts, then either party may move for summary judgment and ask for a judgment from the court without the need for a trial. If material facts remain disputed after the completion of the discovery, then the court will have a trial with live testimony, submission of evidence and formal legal argument. The time between when a complaint is filed and the trial can be anywhere from six to 12 months to two years or more, depending on the facts and circumstances. Litigation involving foreign parties tends to take longer than that between domestic parties. A contested matter, on the other hand, can usually be completed in less than 45 to 60 days.

140 *See* Hon. Louise De Carl Adler, *Managing the Chapter 15 Cross-Border Insolvency Case: A Pocket Guide for Judges* (Fed. Jud. Center 2014) at 5 ("Arguably, this language could be interpreted to require the foreign representative to proceed as though the representative were obtaining a Fed. R. Civ. P. 65 temporary restraining order or preliminary injunction in order to obtain *any* § 1519 interim relief. This would require a foreign representative to file an adversary proceeding.").

141 *See* De Carl Adler, *Managing the Chapter 15 Cross-Border Insolvency Case,* at 4.

142 If the foreign proceeding is recognized as a foreign main proceeding, the automatic stay under 11 U.S.C.

Courts disagree as to the procedure to be used to obtain this relief and what the foreign representative must demonstrate in order to obtain a stay during the pre-recognition gap period. One requirement, however, is that the foreign representative must identify against whom it seeks provisional relief.[143] While Bankruptcy Rule 2002(q) contemplates 21 days' notice for a hearing on a recognition petition, when it comes to provisional relief, the courts will "likely grant immediate relief if the affidavit in support of the motion adequately satisfies the standards for entering such an order, setting a hearing on notice for a later time to give an opportunity for notice to affected parties and the possibility of a hearing."[144] Nonetheless, as will be shown by the following discussion of some of the relevant cases, not all U.S. courts approach the procedural aspects of a case in the same fashion. Thus, the key takeaway for a foreign representative is to know what procedural preferences the relevant court prefers and to follow that procedural approach.

A. The *Pro-Fit* Approach

In *In re Pro-Fit International Ltd.*,[145] the foreign representatives of three affiliated debtors whose insolvency proceedings were pending in the U.K. sought provisional relief from the bankruptcy court during the gap period in the form of a stay of execution by a judgment creditor against the debtors' assets located in the U.S. The debtors' judgment creditor objected to the requested provisional relief, arguing that the foreign representative's motion failed to follow the "standards, procedures and limitations applicable to an injunction," as required by § 1519(e) of the Bankruptcy Code. The court rejected such a broad reading of the statute, finding it to be inconsistent with bankruptcy jurisprudence generally, and the legislative history of § 1519(e) specifically. "[S]uch a reading," the court reasoned, "would impose procedural barriers that are unknown in the bankruptcy law to the availability of at least some section 1519 remedies."[146]

The court also referenced the legislative history of § 1519, which reveals that subsection (e) "contemplates injunctive relief and that such relief is subject to specific rules and a body of jurisprudence. According to this legislative comment, the

§ 362 will automatically apply to stay actions against the debtor's assets located in the U.S. *See* 11 U.S.C. § 1520(a).

143 *See* Bankruptcy Rule 1007.

144 Hon. Leif M. Clark, *Ancillary and Other Cross-Border Insolvency Cases Under Chapter 15 of the Bankruptcy Code: A Collier Monograph* (LexisNexis, 2008; Daniel M. Glosband, consulting ed.).

145 *In re Pro-Fit International Ltd.,* 391 B.R. 850 (Bankr. C.D. Cal. 2008).

146 *In re Pro-Fit International Ltd.*, 391 B.R. 850, at 860.

rules and jurisprudence for an injunction apply ... only where a foreign representative seeks an injunction under § 1519, and not where the relief sought is not an injunction."[147]

The *Pro-Fit* court was careful to explain why, in its view, the automatic stay requested by the foreign representative in that case was not an injunction within the meaning of 11 U.S.C. § 1519(a):

> The stay under § 362 is fundamentally different in several respects from an injunction. Perhaps the most important difference is that the stay is *in rem*: its purpose is to protect property that is in *custodia legis* in consequence of the bankruptcy filing. Accordingly, it is not directed to a party in litigation, or even to any particular person. Instead, it is directed to the world at large, including all individuals and corporate entities.... Furthermore, the fact that § 362 takes effect automatically in all bankruptcy cases, except those filed under chapter 15, without the limitations or procedural safeguards of an injunction, supports the inference that these limitations and procedural safeguards are not needed when a court imposes § 362 in a chapter 15 case on an interim basis.[148]

The *Pro-Fit* court went on to suggest that, had the foreign representative pursued the relief it originally sought in its filings with the court (which were "in the nature of a temporary restraining order and preliminary injunction") without amending its position to request the court's imposition of the automatic stay, its grant of the requested provisional relief might not have been forthcoming.[149] Thus, the court determined that an adversary proceeding was not required to seek to have the automatic stay extended, but for nonautomatic stay relief under § 1519 of the Bankruptcy Code that is injunctive in nature, the analysis could differ.[150]

At least one court has held that an adversary proceeding was not necessary under § 304 of the Bankruptcy Code and that one should not be required in a chapter 15 case in which a foreign representative seeks injunctive relief.[151] In the *Ho Seok Lee* case, the foreign representative sought to close its case and to have a permanent

147 *Id.*
148 *Id.* at 864-65.
149 *Id.* at 866.
150 *See* De Carl Adler, *Managing the Chapter 15 Cross-Border Insolvency Cases,* at 6.
151 *See In re Ho Seok Lee*, 348 B.R. 799 (Bankr. W.D. Wash. 2006).

injunction imposed on a creditor from seeking any recovery from any assets in the U.S. in excess of what was going to be distributed to creditors under a Korean plan.[152] The foreign representative sought this relief under § 1521 of the Bankruptcy Code, which contains the same provisions that § 1519 of the Bankruptcy Code does, conditioning relief under that section on the "standards, procedures, and limitations applicable to an injunction."[153] The court disagreed that an adversary proceeding was required because it was not required under § 304, the legislative history of chapter 15 did not indicate a change was intended, and requiring foreign representatives to file an adversary proceeding "would result in an unintended change in procedure for seeking an injunction in foreign ancillary proceedings."[154]

B. The *Worldwide Education Services* Approach

Not all courts have followed *Pro-Fit*. On June 17, 2013, the U.S. Bankruptcy Court for the Central District of California rejected the *Pro-Fit* reasoning on the standard of proof for preliminary relief during the gap period.[155] In *Worldwide Education Services*, the debtor was a former Wyoming limited liability company that was redomiciled as a British Virgin Islands corporation. The debtor ceased operations in 2010, but maintained its corporate form with the hopeful intent of reopening at some point in the future. After the debtor began its insolvency proceedings in the British Virgin Islands, the foreign representative petitioned for relief under chapter 15 and requested provisional relief in the form of the automatic stay. In doing so, the foreign representative admitted in papers filed with the court that the debtor had no operations and no significant assets.

Notwithstanding its lack of assets, the debtor remained a defendant in several lawsuits at the time that the chapter 15 petition was filed, at least one of which was scheduled for trial on the following day. In his motion for provisional relief, the foreign representative asked the court to "enter an order staying all pending litigation against the Debtor or the seizure of the Debtor's assets in the United States

152 *Id*. at 801.
153 *Id*.
154 *Id*.
155 *In re Worldwide Education Services Inc*., 494 B.R. 494 (Bankr. C.D. Cal. June 17, 2013). This exacting standard has been applied by other courts. *See, e.g., In re Innua Canada Ltd*., 2009 WL 1025088 (Bankr. D.N.J. Mar. 25, 2009) (foreign representative won imposition of the automatic stay during the gap period by showing that the Third Circuit's standards for injunction had been met); *In re Qimonda AG*, 2009 WL 2210771 (Bankr. E.D. Va. July 16, 2009) (same result, applying Fourth Circuit standards).

pending the outcome of the hearing on the petition for recognition."[156] Two creditors with pending litigation against the debtor opposed the foreign representative's request. Citing the bankruptcy court's prior decision addressing provisional relief in *Pro-Fit*, the foreign representative argued that "a temporary application of the automatic stay under Section 1519(a) does not even need to meet the requirements for injunctive relief, either procedural or substantive."[157]

The *Worldwide Education Services* court rejected the *Pro-Fit* court's analysis of the foreign representative's burden in requesting imposition of the automatic stay during the gap period, stating that the analysis "is flatly inconsistent with the plain and unambiguous language of Section 1519(e).... The court in *Pro-Fit* ... concluded that Section 1519(e) was limited to motions that only requested injunctive relief, but this court notes that the express language of the statute does not contain such a limitation and generally applies to all relief sought pursuant to Section 1519, including imposition of the automatic stay."[158] Thus, the court held that a foreign representative seeking provisional relief under any subsection of § 1519 must meet the standard of proof for a preliminary injunction, establishing that (1) the foreign representative is likely to succeed on the merits, (2) the foreign representative is likely to suffer irreparable harm in the absence of preliminary relief, (3) the balance of equities tips in the foreign representative's favor, and (4) an injunction is in the public interest.[159]

Applying the standard of proof for preliminary injunction to the facts before it, the court found that an injunction was not warranted, explaining:

> There is no showing that not granting provisional relief to stay the pending federal district court trial by the creditors would give them more favorable treatment. The creditors are merely seeking to determine the liability of debtor and the other defendants. No explanation is given [as to] how this gives them an unfair or inequitable advantage over other creditors, and there is no showing that there would be an unfair or inequitable advantage to them through a "race to the courthouse," that is, to collect or seize assets of the debtor before other creditors. There is no showing by the liquidator that the creditors are undertaking any collection activity

156 *Id*. at 497.
157 *Id*. at 498.
158 *Id*.
159 *Id*. at 499.

> against the debtor; rather, they are only seeking to determine liability in the federal court action.[160]

In the view of the court in *Worldwide Education Services*, "granting the motion for stay of litigation proceedings on the eve of trial in a case that has been pending for about two years would unduly prejudice creditors because they are ready to go to trial after extensive pretrial litigation and discovery."[161] The court concluded that a preliminary stay during the gap period was not "urgently needed to protect the assets of the debtor or the interests of the creditors."

Significantly, the *Worldwide Educational Services* court did agree that in order to seek provisional relief, no adversary proceeding was required, choosing instead to apply the standards for injunctive relief in the context of a contested matter on motion.[162]

C. Conclusion

It should not be ignored that the legislative history of 11 U.S.C. § 362 explains that "[t]he court has ample other powers to stay actions not covered by the automatic stay.... Stays or injunctions issued under these other sections will not be automatic upon the commencement of the case, but will be granted or issued under the usual rules for the issuance of injunctions."[163] This, together with the fact that 11 U.S.C. § 1519(a) sets forth a nonexclusive list of relief available to a foreign representative upon filing a chapter 15 petition, leaves room for the possibility that the *Pro-Fit* court was correct in its characterization of the automatic stay as something outside the scope of 11 U.S.C. § 1519(a).

However, given the split of authority on the specific point of the appropriate standard applicable to a foreign representative's request for imposition of the automatic stay on a provisional basis during the gap period, a foreign representative pursuing such relief may be best served to include, within its papers, an explanation of why the circumstances warrant the desired relief according to the governing

160 *Id.* at 501.
161 *Id.*
162 *See id.* at 499 n.1 ("The purpose of provisional relief under Section 1519 is to provide remedial relief to preserve the status quo in the gap period between the filing of the petition and the time the court rules upon the petition for recognition, and in this court's view, it does not make sense to require an adversary proceeding for provisional, or preliminary, relief where the underlying action for recognition does not require one.").
163 124 Cong. Rec. H 11092, H 11093 (Sept. 28, 1978).

standard for the issuance of an injunction, typically a showing that requires the foreign representative to demonstrate (1) the likelihood of success on the merits of recognition, (2) that there would be irreparable harm in the absence of preliminary relief, (3) that the balance of equities tips in the foreign representative's favor, and (4) that an injunction is in the public interest. There is little doubt that such a showing will be necessary if the foreign representative seeks relief other than the automatic stay and that for which 11 U.S.C. § 1519 makes specific provision.

Although the issue of whether specific matters should be filed as adversary proceedings or contested matters is likely to continue to be litigated, it would seem that most courts will not require an adversary proceeding to seek injunction relief. However, different courts apply different standards, so a foreign representative would be well advised to address these issues with U.S. counsel to ensure that they are not delayed by procedural shortcomings.