THOMPSON HINE

Business Restructuring, Creditors' Rights & Bankruptcy Update

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Foreign Borrower's Rights in Indenture Ruled Sufficient to Meet Second Circuit's Controversial Chapter 15 Eligibility Requirement

Key Notes:

- Non-U.S. borrowers' access to U.S. Bankruptcy Courts may be eased
- Contractual rights in the U.S. may create property rights for non-U.S. borrowers to meet debtor eligibility requirements

In re Berau Capital Resources Pte Ltd., a recent opinion by Bankruptcy Judge Martin Glenn of the U.S. Bankruptcy Court for the Southern District of New York,[1] may help mitigate a controversial debtor eligibility requirement in effect for courts within the jurisdiction of the U.S. Court of Appeals for the Second Circuit. In *Drawbridge Special Opportunities Fund LP v. Barnet (In re Barnet)*, 737 F. 3rd 238 (2d Cir. 2013), the court held that to obtain recognition of a foreign proceeding under Chapter 15, the foreign entity must not only satisfy the requirements for recognition but must also qualify as a "debtor" under Bankruptcy Code Section 109(a), i.e., the foreign entity must have "a domicile, a place of business, or property in the United States." *Id.* The *Barnet* decision has been criticized for grafting an eligibility requirement applicable to U.S. debtors onto the separate requirements for recognition of a foreign proceeding under Chapter 15, rather than focusing exclusively on the nature of the foreign proceeding and the foreign representative.[2] To date, no other federal circuit court has addressed the issue of whether Code Section 109(a) is applicable in a Chapter 15 case.

In grappling with the necessity of satisfying the eligibility requirement of Code Section 109(a) when considering a petition for recognition, bankruptcy courts in the Southern District of New York (which are bound to apply the law as established in the Second Circuit) have ruled that the foreign representative has met the debtor eligibility requirement by finding *de minimus* property located in the United States. For example, in *In re Suntech Power Holdings,* 520 B.R. 399 (Bankr. S.D.N.Y. 2014), Bankruptcy Judge Stuart Bernstein held that the foreign entity's establishment of a $500,000 bank account in New York, even when the account was titled in the name of an agent, was sufficient "property in the United States" to meet the debtor eligibility requirement of Code Section 109(a). Indeed, the bankruptcy court's decision following the remand ordered in *Barnet* took a similarly liberal view, holding that a retainer paid to the foreign representative's counsel was sufficient "property in the United States." *See In re Octaviar Admin. Pty Ltd.*, 511 B.R. 361, 372-73 (Bankr. S.D.N.Y. 2014).

In *Berau*, Judge Glenn initially ruled that the attorney retainer held by the foreign representative's New York counsel was a sufficient basis for debtor eligibility. However, he then went on to discuss another basis for the foreign entity's eligibility, holding that the foreign entity's contract rights under an indenture agreement were intangible property rights located in the United States and that they satisfied the eligibility requirement of Code Section 109(a). The Bankruptcy Court noted that the indenture was governed by New York law and that it required a number of acts associated with the indenture to occur solely in New York City (such as authentication,

delivery and transfer of notes, maintenance of noteholder registries, note redemption and discharge, covenant defeasance, recovery of cash or securities posted in connection with defeasance, amendments to the indenture, and collateral releases). In finding that the situs of the foreign debtor's intangible property rights was in New York, the Bankruptcy Court looked to New York's General Obligations Law and New York's Civil Practice Laws & Rules, which give effect to choice of law and forum selection clauses under circumstances present in the indenture. According to the *Berau* court, the parties' inclusion of these clauses set New York as the "contract situs," such that the foreign entity can be said to have (intangible) "property in the United States."

The *Berau* decision, as with earlier decisions by other bankruptcy judges in the Southern District of New York, serves to minimize the impact of the Second Circuit's imposition of an eligibility requirement in a Chapter 15 case and potentially establishes the means for divergence from *Barnet's* holding in other jurisdictions. The *Berau* decision should also provide a measure of comfort for foreign borrowers that the New York choice of law and forum selection provisions in their indenture agreements may be sufficient to work around the eligibility requirement, without having to fear accusations of bad faith for suddenly depositing funds into a New York bank account or establishing an attorney retainer account to manufacture eligibility. Finally, it would appear that Judge Glenn's opinion with respect to a foreign entity's rights under an indenture should apply equally in the context of a plenary Chapter 11 case for a non-U.S. debtor as it does in the context of an ancillary Chapter 15 case filed by the foreign representative for a non-U.S. debtor.

FOR MORE INFORMATION

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[1] Case No. 15-11804 (Bankr. S.D.N.Y., October 28, 2015).

[2] *See generally* Daniel M. Glosband and Jay Lawrence Westbrook, "Chapter 15 Recognition in the United States: Is a Debtor 'Presence' Required?", *29 Int'l Insolv. Rev. 28* (2015).