INSOL INTERNATIONAL
NEWS UPDATE

February 2015 **Issue No. 02**

Contents at a glance...

Promoting comity and yet grounded in the distinct jurisdictional reality of global insolvency regimes, INSOL's relevance is abundantly apparent in this month's ENL. Our highlight article analyzes a decision from the U.S. Second Circuit Court of Appeals that takes a whack at judicial comity in cross-border cases, providing an opportunity for U.S. courts to revisit decisions by foreign insolvency forums where U.S. assets are at issue.

Further clouding the pursuit of comity are developments in China where the Supreme People's Court acknowledged the authority of foreign insolvency appointees to act on behalf of the companies of Chinese subsidiaries for which they are appointed – clearly a positive development. And yet China's civil law system makes this decision persuasive authority rather than binding on its courts. Without legislative support, it is unclear whether this decision will have a pervasive impact on nurturing cross-border values.

This month's ENL also is replete with summaries of legislative developments from the corners of the globe, tweaking country specific insolvency regimes and reinforcing the axiomatic reality that insolvency, like real estate, is location, location, location.

Fifteen years since its adoption in 1997, the UNCITRAL Model law on Cross-Border Insolvency continues to provide a strong framework for fostering the predictability that is critical to efficient corporate rescue and redeployment of human and economic capital. For all that it has accomplished, work remains to secure its broader implementation and to take the next developmental steps. What form that takes is the subject of much debate, the friendliest of which occur within INSOL.

Our annual regional conference is right around the corner – March 22-24 in San Francisco. We will spend quite a bit of time talking about these issues. But equally valuable is the time spent investing in friends and relationships, new and old, from across the globe so that the next time an insolvency practitioner from Mexico has a client issue in Japan, she will know who to call.

All the best,

J.R. Smith
Partner
Hunton & Williams LLP

Seller's Remorse? U.S. Second Circuit Opens Door to Voiding BVI Liquidator's Sale of $230 Million Madoff Claim

A recent decision by the U.S. Court of Appeals for the Second Circuit opened the door for a New York bankruptcy court to void the sale of a bankruptcy claim by a foreign liquidator, potentially representing a significant expansion of chapter 15 (and possibly section 363) of the U.S. Bankruptcy Code. Despite the British Virgin Islands court's approval of the sale, which court oversaw the foreign main proceeding, the Second Circuit determined that the BVI liquidator's sale fell within the "territorial jurisdiction" of the United States. The Second Circuit's decision remands the matter to the U.S. bankruptcy court to determine whether the sale of the claim satisfies requirements under section 363 of the U.S. Bankruptcy Code. The decision is noteworthy because the Second Circuit held that the bankruptcy court erred by deferring to the BVI court's decision. The stage is now set for a U.S. bankruptcy court in a chapter 15 case essentially to act as an appellate court conducting a plenary review of a matter previously adjudicated in the "foreign main proceeding."

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Legislation

Cayman Islands

Cayman Islands Portfolio Insurance Companies

The long awaited portfolio insurance company legislation is now in force. Those familiar with the Cayman Islands segregated portfolio company will note that an SPC is one legal entity irrespective of the number of segregated portfolios created. This means that segregated portfolios forming part of the SPC cannot contract together. Many offshore jurisdictions have sought to overcome this obstacle by introducing legislation to specifically provide that segregated portfolios within the same segregated portfolio company can contract together. Through the portfolio insurance company legislation, the Cayman Islands offers its own solution to the perceived limitations of the traditional SPC structure.

Articles

USA

(i) Review of Chapter 15 Cases in 2014: Relief Available to a Foreign Representative

Chapter 15 of the Bankruptcy Code provides a mechanism for a foreign insolvency, liquidation, or debt restructuring to obtain recognition in the United States. With the continued globalisation of the world's economies, it should come as no surprise that foreign debtors and their trustees, liquidators and administrators, acting as "foreign representatives", continue to file Chapter 15 cases to enjoin litigation against the debtor, preserve a debtor's assets, and pursue claims in the United States. In 2014, more than sixty-five Chapter 15 cases were filed in more than a dozen different judicial districts.

The Southern District of New York was the preferred Chapter 15 venue with twenty-one of the cases filed there, followed by Delaware with twelve. The Chapter 15 cases filed in 2014 were ancillary to foreign proceedings from fourteen different jurisdictions: Australia, Brazil, British Virgin Islands, Canada, Cayman Islands, China, Germany, Hong Kong, Israel, Japan, Kazakhstan, Korea, Singapore, and the United Kingdom. During 2014, several courts highlighted the relief available to a foreign representative in the United States. The correlation between the relief granted by the United States court and the relief granted in the foreign proceeding is the focus of this article.

(ii) Virtual Currency, Real Risks - CSBS publishes Draft Model Regulatory Framework

In March 2014, "Mt. Gox," one of the largest and best-known virtual currency exchanges, announced that bitcoins (a prominent virtual currency) worth $409 million had been hacked and stolen. Mt. Gox subsequently declared bankruptcy, leaving more than one million people unable to recover their funds. Earlier this month, one of the active, operational bitcoin storage wallets of European bitcoin exchange Bitstamp was hacked, with approximately 19,000 bitcoins stolen, representing a market value of approximately $5 million.

On December 16, 2014, the Conference of State Bank Supervisors published a Draft Model Regulatory Framework for state virtual currency regulatory regimes. The CSBS, a national organisation dedicated to advancing the state banking system, believes that, once adopted, the Framework will support the CSBS's policy on state regulation of virtual currency, will promote consistent state regulation of virtual currency activities and will provide for greater consumer protection. The Framework is an initiative of the CSBS's Emerging Payments Task Force, which was formed in February 2014 to take a comprehensive look at the changing payments landscape.

Cases

New Zealand

Parent Company Made to Pay its Subsidiary's Debts

Lewis Holdings Ltd v Steel & Tube Holdings Ltd [2014] NZHC 3311

When Stube Industries Ltd was put into liquidation, Lewis Holdings Ltd filed a proof of debt as the unpaid landlord. The liquidators of Stube then sought an order under section 271 of the Companies Act 1993 that Steel & Tube Holdings Ltd be required to pay the whole of the claim on the basis that:

- Lewis Holdings leased a property to Stube, a wholly owned subsidiary of Steel & Tube;
- the rent and rates under the lease were invoiced to and paid by Steel & Tube; and
- decisions for Stube, including a decision to renew the lease for a further 21 year term, were made on the advice of Steel & Tube's legal counsel, without Stube obtaining independent legal advice.

The liquidators were successful and the Court ordered the parent company to pay the debt of its subsidiary company. The Court acknowledged that it is common practice for a parent company to be involved in the management of its subsidiary, including appointing high-level managers to the subsidiary's board. However, in this case, the level of involvement had been so large as to compromise the subsidiary's independence.

This decision highlights the need for directors to ensure that a subsidiary's interests are kept distinct and that appropriate legal and financial arrangements are made if there is to be a sharing of liabilities between companies within a group.

Legislation

China

China Plans to Reshuffle Foreign Investment Regulation

After a long wait, on 19 January 2015, China's Ministry of Commerce released the draft Foreign Investment Law for public comment. The draft Foreign Investment Law represents a significant step forward in China's continuing reform and opening-up. Upon effectiveness, the Foreign Investment Law will replace the current three main laws on foreign-investment enterprises (the Law on Wholly Foreign Owned Enterprises, the Law on Equity Joint Ventures, and the Law on Cooperative Joint Ventures), and introduce various other changes.

The draft Foreign Investment Law is a big step forward for foreign investment regulation in China. There remain, however, lots of issues that will still need to be addressed. For example, the draft does not give the details of how the new negative list review system will work. The draft also still appears, in practice, to leave governmental authorities with significant discretionary power to review foreign investment. Various aspects of the existing M&A rules are inconsistent with the draft law, and it is likely that the M&A rules will be revised for compliance with the Foreign Investment Law. While this might introduce greater flexibility, the revision might also introduce more reporting requirements. Finally, it is noted that the draft Foreign Investment Law only sets out the general regulatory framework and certain principles. A lot more legislative work will be required before the full details of the system emerge. Comments on the draft Foreign Investment Law will be accepted until 17 February 2015. It is unclear, however, when the Foreign Investment Law will be finalised and issued.

Articles

China

Will the Chinese Courts Grant "Back Door Recognition" to Overseas Insolvency Practitioners?

On 11 June 2014, the Supreme People's Court of the People's Republic of China handed down its ruling in

the case of Sino-environment Technology Group Limited v Thumb Env-Tech Group (Fujian) Co., Ltd. The Court found in favour of the liquidators of Sino-environment, a Singapore incorporated company, against its wholly-owned subsidiary, Thumb, represented in the action by a legal representative that the liquidators of Sino-environment had sought to replace. In making its judgment, the Court gave its view on two issues with potentially far-reaching implications for offshore creditors and investors seeking to enforce their rights in the PRC by:

- recognising the authority of foreign insolvency appointees to act on behalf of the company to which they are appointed; and
- confirming that the sole shareholder of a wholly foreign owned enterprise has the power to remove and replace the legal representative of the WFOE and that from an internal perspective, such appointment should be seen as effective from the date of the resolution, even if the changes have yet to be registered with the company registration authority, the Administration of Industry and Commerce.

However, these key decisions may not be as helpful or far-reaching as they might appear at first glance, on account of certain legal and practical limitations. This article outlines the principles and substance of the judgment and its implication in both the short term and the longer term.

Legislation

UK

Changing the Priority of Claimants: New Depositor Preference Legislation

On 1 January 2015, the Banks and Building Societies (Depositor Preference and Priorities) Order 2014 (SI 2014/3486) came into force. The Order implements the requirements contained in Article 108 of the Bank Recovery and Resolution Directive (2014/59/EU) to ensure that both deposits that are eligible for compensation under the UK Financial Services Compensation Scheme, and other deposits that would be eligible deposits but for the fact that they are made in branches of UK banks outside the EEA, are treated as preferential debts. The Order also ensures that eligible deposits are given a higher priority within the class of preferential debts than other deposits.

The Order, therefore, creates a new class of preferential debt and amends the law on preferential debts to ensure that this new preferential debt is treated as a “secondary preferential debt”, ranking after all other “ordinary preferential debts” (which include deposits covered by the FSCS). The Insolvency Act 1986, the Insolvency (Northern Ireland) Order 1989, the Bankruptcy (Scotland) Act 1985 and related primary and secondary legislation have been amended to reflect this change on preferential debts. In particular, the Order builds on the changes to Schedule 6 (categories of preferential debts) to the IA 1986 that came into effect on 31 December 2014, and which converted bank and building society deposits covered by the FSCS into preferential debts (paragraph 15B, Schedule 6).

South Africa

Does the Section 155 Compromise Further the Objectives of Business Rescue?

The South African Companies Act 2008 provides in sections 128-155 (Chapter 6) for ‘business rescue and compromise with creditors’, which deals primarily with the ‘business rescue’ of companies. The compromise mechanism, contained in section 155, is distinct from the sections dealing with business rescue, which provide for a fairly comprehensive procedure for ultimately developing and implementing a plan to rescue the company from its financial distress under the supervision of a business rescue practitioner. Section 155, on the other hand, provides for the restructuring of the financial affairs of a company without the involvement of a business rescue practitioner, allowing a company to propose a compromise or arrangement to its creditors in

a form that is almost identical to a business rescue plan.

This article examines the pros and cons of the section 155 compromise mechanism envisaged and concludes that whilst it shows promise in principle, it lacks in certain material respects. In particular, section 155 does not provide for a moratorium to protect the company from claims of creditors during the period of renegotiation and is not available to a company under liquidation.

Articles

United Arab Emirates

Abu Dhabi Global Market

Abu Dhabi, the largest emirate in the United Arab Emirates, has established the Abu Dhabi Global Market as a new international financial free trade zone to connect the economies of the Middle East, Africa and South Asia with world markets. On 7 January 2015, ADGM released six consultation papers on the proposed legal regime to apply within the free zone, following consultation with a panel of leading international financial institutions. Ranging from Company Regulations to Insolvency Regulations, the consultations are the first step in what will be an extensive and ongoing consultation process with the aim of ensuring that all activities in the free zone are regulated to the highest international standards.

This article examines some of the key features of the proposed legal and regulatory environment in ADGM and compares these with the Dubai International Financial Centre in Dubai.

Bermuda One Day Seminar - Thursday 4 June 2015

Fairmont Hamilton Princess, Hamilton, Bermuda

CPE/CLE Points: 6 hours

Registrations are now open! The full programme for the day including on line registration can be found on our website at https://www.insol.org/page/458/bermuda-one-day-seminar

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Final Booking Deadline 21 February 2015

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In 2015 INSOL's Annual Conference will be held in the Americas in the beautiful city of San Francisco and we look forward to seeing you there.

You will see that we have an interesting program covering issues affecting the Americas and the worldwide profession. We will cover a variety of subjects through plenary and breakout sessions. Topics will include intellectual property; tax havens; restructuring of corporate groups; the independent directors role; insolvency law reform in the EU and many more diverse and interesting subjects. We have a first class line up of speakers from around the world representing the different interest groups of INSOL. We look forward to seeing you in San Francisco where you will be able to renew friendships and make new acquaintances with colleagues from over forty countries who are the key members of the international insolvency profession.

We would like to thank our main sponsors BMC Group, Borrelli Walsh, Hilco Global and Skadden, Arps, Slate, Meagher & Flom LLP for supporting this conference.

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