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### Why Chinese Companies File Chapter 15 Cases in US Bankruptcy Courts



Reward Science and Technology Industry Group Co., Ltd. (Reward) joins a growing list of Chinese companies which have chosen to file a case in U.S. Bankruptcy Court in connection with their restructuring efforts under the People's Republic of China's Enterprise Bankruptcy Law (EBL). These U.S. cases are known as "Chapter 15" cases, as they are commenced under Chapter 15 of the U.S. Bankruptcy Code.[\[1\]](#)

## **Reward Reorganization**

### **Background**

Through its EBL case, Reward seeks to facilitate its ongoing reorganization under the EBL and safeguard the rights and interests of Reward and its creditors. With the EBL case pending, Reward's Chapter 15 "foreign representative"[\[2\]](#) commenced the Reward Chapter 15 case[\[3\]](#) on September 9, 2019. Simultaneously, the foreign representative asked the U.S. Bankruptcy Court to recognize the EBL case as Reward's "foreign main proceeding," to provisionally enjoin the prosecution of lawsuits filed against Reward in U.S. courts, to prevent the transfer of Reward's U.S. assets located within the United States outside of the territorial jurisdiction of the United States, and to grant related relief. The pending litigation was described as "disruptions that could otherwise derail" Reward's case under the EBL. One lawsuit was filed by Hong Kong-based BFAM Partners Ltd. and seeks \$83 million due under a promissory note. The other lawsuit was filed by three investment funds and sought nearly \$77 million more in damages.[\[4\]](#) Much of the provisional relief sought was granted on the Chapter 15 petition date, and additional provisional relief was granted three days later.[\[5\]](#)

Weeks later, the U.S. Bankruptcy Court issued an order granting recognition of the EBL case as Reward's foreign main proceeding. With that came a stay of all efforts by Reward's U.S. creditors to continue litigation and to commence any new lawsuits or other efforts to collect on claims in the United States. Additionally, the Reward foreign representative was granted the power to administer Reward's U.S.-based assets for the benefit of its creditors and to gather evidence within the United States concerning Reward's liabilities, assets, business affairs, and operations, including through examining witnesses under oath and issuing subpoenas to obtain documents. Though such relief is often granted in a Chapter 15 case, Reward also succeeded in obtaining additional relief. Specifically, the recognition order requires the parties that sued Reward in the United States to provide the Foreign Representative with 10 days' notice of any action they intend to take against Reward or its assets outside China or the United States. This notice provision enables the foreign representative to notify Reward and its representatives in China and to seek relief from a U.S. bankruptcy court if any party seeks to take control of Reward assets located outside of China and the United States. At the same time, the Foreign Representative must give those plaintiffs three days' notice of any information she obtains regarding any action by creditors to enforce claims against Reward or its assets outside of China or the United States.<sup>[6]</sup>

## **Commencing a Chapter 15 Case**

In a Chapter 15 case, the foreign representative files a petition in a U.S. bankruptcy court seeking "recognition" of a foreign proceeding.<sup>[7]</sup> A foreign representative is a party authorized in a foreign proceeding to act as its representative in the Chapter 15 case in the United States. To be eligible to be a Chapter 15 debtor, the foreign entity must: (1) be the subject of a foreign bankruptcy or similar proceeding, and (2) have a domicile, residence, place of business, or property in the United States. Courts have held that having minimal property in the United States will satisfy this requirement. For example, having money on deposit in a bank account has been held by some judges to be sufficient property in the U.S..<sup>[8]</sup> Some other courts have held that an entity's lack of domicile, place of business, or property in the U.S. alone does not preclude seeking relief under Chapter 15 in the U.S. Bankruptcy Court.<sup>[9]</sup> Given that U.S. courts repeatedly have recognized EBL cases as foreign main proceedings, it is unlikely this would serve as an obstacle for a foreign representative appointed by a Chinese court.

It should be noted that the Bankruptcy Code provides that U.S. bankruptcy courts should not grant relief under Chapter 15 if doing so "would be manifestly contrary to the public policy of the United States."<sup>[10]</sup> To determine whether the "public policy exception" applies, courts have considered, for example, whether: (1) the foreign proceeding was procedurally unfair, and (2) whether the application of foreign law or the recognition of the foreign main proceeding under Chapter 15 would "severely impinge the value and import of a U.S. statutory or constitutional right."<sup>[11]</sup> Courts construe this "public policy exception" very narrowly, and Chapter 15 petitions are infrequently denied on this basis.<sup>[12]</sup>

## **Remedies Available Through Chapter 15**

Typically, as in the Reward case, a U.S. bankruptcy court will rule on whether to grant a petition for recognition and recognize the foreign proceeding as the main proceeding within a month or so of the filing of the petition. If

recognition is granted, all collection actions, all lawsuits, and certain other actions against the Chapter 15 debtor and its assets are stayed. In other words, they are frozen subject to the court granting a creditor the right to proceed against assets on the creditor's motion for good cause shown.<sup>[13]</sup> Appreciating that many restructurings require fast action, U.S. bankruptcy courts often grant interim or temporary relief within a few days of the filing of a Chapter 15 petition and grant permanent relief once the petition is recognized.<sup>[14]</sup> As noted, such relief was granted in the Reward Chapter 15 case.

Once a petition is granted, the foreign representative can conduct any U.S.-based operations of the foreign entity, unless the U.S. court expressly orders otherwise.<sup>[15]</sup> Nonetheless, court approval is needed to sell assets in the United States and to transfer the proceeds of a sale or other assets out of the United States.<sup>[16]</sup> So too, a U.S. bankruptcy court may fashion other broad relief for the benefit of the foreign entity.<sup>[17]</sup> For example, U.S. courts have prevented U.S.-based parties from enforcing contract provisions which would otherwise enable the U.S.-based party to terminate a contract with the foreign debtor due to its financial problems or pending bankruptcy case.<sup>[18]</sup> Courts also have issued orders enforcing a debt adjustment or restructuring plan approved by a foreign tribunal and issued injunctions to prevent any interference by U.S.-based creditors with such a plan, including prohibiting creditors from trying to collect on their claims other than through the terms of the plan approved by the foreign court.<sup>[19]</sup>

## Implications

Reward's Chapter 15 case demonstrates that companies that are the subject of EBL cases or are considering whether they could benefit from filing an EBL case may also be able to obtain protections from creditor action in the United States by commencing a Chapter 15 case. As part of a Chapter 15 case, U.S. bankruptcy courts may halt litigation and other collection efforts against the Chinese business (temporarily or permanently), limit the enforceability of certain contract provisions, and simultaneously facilitate the Chinese's business' efforts to reorganize or liquidate.

This update was also published in *Harvard Law School Bankruptcy Roundtable*, titled "[Why Chinese Companies File Chapter 15 Cases in US Bankruptcy Courts](#)," on 02.25.2020.

## ENDNOTES

[1] 11 U.S.C. § 1501 *et seq.*

[2] Reward's Foreign Representative is Dr. Yin Zhengyou, of the Beijing Wei Heng law firm.

[3] *In re Reward Science and Tech. Industry Grp. Co, Ltd.*, Case No. 19-12908 (MEW) (Bankr. S.D.N.Y. September 9, 2019) [Dkt. 1].

[4] *Id.* at [Dkt. 5].

[5] *Id.* at [Dkt. 7].

[6] *Id.* at [Dkt. 26].

[7] 11 U.S.C. §§ 1504, 1509, 1511, 1515.

[8] 11 U.S.C. § 109(a); *In re Berau Capital Res. Pte Ltd*, 540 B.R. 80, 82 (Bankr. S.D.N.Y. 2015) (citing *In re Octaviar Admin. Pty Ltd*, 511 B.R. 361, 369–74 (Bankr. S.D.N.Y. 2014)).

[9] *See, e.g., In re Toft*, 453 B.R. 186, 193 (Bankr. S.D.N.Y. 2011).

[10] 11 U.S.C. § 1506.

[11] *In re British Am. Isle of Venice (BVI), Ltd.*, 441 B.R. 713, 717 (Bankr. S.D. Fla. 2010).

[12] *See In re Rede Energia S.A.*, 515 B.R. 69, 92 (Bankr. S.D.N.Y. 2014) (noting that "public policy exception" is to be applied "sparingly").

[13] 11 U.S.C. §§ 1517, 1520.

[14] 11 U.S.C. §§ 105(a), 1509, 1519-1521.

[15] 11 U.S.C. § 1520(a)(3).

[16] 11 U.S.C. § 1520.

[17] 11 U.S.C. § 1521.

[18] *E.g. In re BuildDirect.com Techs. Inc.*, Case No. 17-23522 (Bankr. C.D. Cal. November 3, 2017) [Dkt. 14]; *In re Nortel Networks Corp.*, 2013 U.S. Dist. LEXIS 162887 (D. Del. November 15, 2013); *In re W.C. Wood Corp. Ltd.*, Case No. 09-11893 (Bankr. D. Del. June 1, 2009); *In re Gandi Innovations Holdings LLC*, Case No. 09-51782 (Bankr. W.D. Tex. June 5, 2009). *But see In re SunEdison, Inc.*, 577 B.R. 120 (Bankr. S.D.N.Y. 2017) (upholding enforcement of *ipso facto* clause against foreign debtor, thereby allowing termination of license essential to foreign debtor's business).

[19] *See, e.g., BuildDirect; In re CGG S.A.*, 579 B.R. 716 (Bankr. S.D.N.Y. 2017); *In re Energy Coal S.P.A.*, 582 B.R. 619 (Bankr. D. Del. 2018); *In re Avanti Commc'ns Grp. PLC*, 582 B.R. 603 (Bankr. S.D.N.Y. 2018) (enforcing third-party, non-debtor guarantor releases included in scheme of arrangement and approved by British court).

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