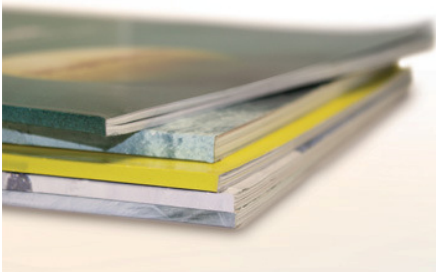


## Chapter 15 Update: All Change or No Change?

*As originally appeared in Resolution – Offshore, Winter 2010/11*



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**A recent decision by the Bankruptcy Court for the district of Delaware, to recognise the liquidation of a Cayman Islands company and grant relief to its liquidators, has been hailed by some commentators as a milestone in the development of Chapter 15 jurisprudence. However, a closer review of the case, *In Re Saad Investments Financing Company (No 5) Limited* (“SIFCO”), reveals that the decision was little more than a triumph of pragmatism over principle.**

SIFCO was a privately-owned investment company incorporated in the Cayman Islands, and a wholly-owned subsidiary of Saad Investments Company Limited (“SICL”), another Cayman company formed to hold investment assets on behalf of its beneficial owner, a Saudi national and chairman of the Saudi-based Saad Group of companies. SIFCO’s principal assets were “a portfolio of 57 private equity vehicles and one hedge fund (*“the Funds”*)”. The Funds were registered in several jurisdictions around the world,

with some 38.7% in value being registered in the Cayman Islands and 28.5% in Delaware. As part of a financing agreement between SICL and Barclays Bank PLC, SICL had transferred its interest in the Funds to SIFCO as in-specie contributions for the issue of Class B shares to Barclays.

The Grand Court of the Cayman Islands ordered SIFCO to be wound up on the petition of Barclays and appointed official liquidators over it. Two months later, the liquidators filed a petition in the US Bankruptcy Court for the District of Delaware, seeking recognition of the Cayman liquidation under Chapter 15 of the Bankruptcy Code. This was to protect SIFCO’s assets in the USA from potential seizure, by third parties in connection with a mass of litigation involving the beneficial owner and his group of companies.

The petition for recognition was unopposed, and no reasoned decision was delivered by the court. However, it was apparent from the transcript of

proceedings that the court relied heavily on the petitioners' written submissions. One of their key arguments was that the relevant time for determining a debtor's centre of main interest ("COMI") is the time that the Chapter 15 case is commenced, that "*the court is to examine the COMI factors at they existed at the time of the filing the Chapter 15 petition, without reference to SIFCO's operational history*". This argument enabled the Petitioners to rely on the following activities by the Cayman liquidators themselves in establishing that the company's COMI was the Cayman Islands: "*The management and administration of the Debtor is being conducted entirely by the Petitioners from the Petitioners' headquarters in the Cayman Islands*"; "*No activity being conducted in respect of the management, administration or operations of the Debtor anywhere apart from the activities of the Petitioners in the Cayman Islands*"; "*The Petitioners have obtained or are in the process of obtaining, electronic versions of all of the Debtor's financial records from SFS*" [a Swiss company that provided investment management services to SIFCO].

### **Adverse Facts Downplayed**

At the same time, the Petitioners downplayed these adverse facts which militated against COMI being established in the Cayman Islands: SIFCO was an investment vehicle set up by a Saudi national; its directors were resident in the middle east; its investment management services were provided by a Swiss company, which was subcontracted by its parent (whose board was composed of Saudi or Bahraini residents). Over 60% in value and 70% in number of SIFCO's assets comprised shares in

private equity vehicles and hedge funds registered in countries other than the Cayman Islands.

The Delaware Court, in an *ex tempore* oral decision, concluded that SIFCO's COMI was in the Cayman Islands, and that its liquidation should be recognised as a foreign main proceeding. This in itself should not be great news, since such orders have been made since the launch of the Chapter 15 regime. Perhaps its newsworthiness is a reflection of the fear cast into practitioners' minds by the New York court's decisions in 2008 regarding the **Bear Stearns and Basis Yield Alpha** cases, although those related to a particular species of company, a hedge fund.

### **Rigorous Examination**

Nevertheless, the facts of this case had characteristics which, if presented differently and/or to a different court, may well have led to a different result. The Delaware court declined to undertake a rigorous examination of the facts or legal arguments, unlike the New York court in the **Bear Stearns and Basis Yield Alpha** cases. The result may be said to demonstrate a pragmatic and commercial approach by the Delaware court – supportive of that state's leading role in the offshore funds industry.

However, it is hard to overlook the analytical flaw in the Delaware court's decision, which pointed to the activities of foreign representatives in order to establish the COMI of companies which they are in the process of winding up. Taken to its logical conclusion, that reasoning would entitle every foreign representative who carries out his statutory

functions in liquidating a company to obtain recognition as a foreign main proceeding, irrespective of what that company's COMI relevant activities may have been prior to the liquidator's appointment. This would effectively do away with the COMI test altogether.

The Petitioners' argument was itself grounded on a slender line of authorities which addressed arguments about how much weight should be given to changes in COMI during the operational lifetime of a company. Those cases hold that *"the centre of main interests is to be determined in the light of the facts as they are at the relevant time for determination [i.e. the time of opening recognition proceedings]. But those facts include historical facts which have led to the position as it is at the time for determination"*. At the same time, the court must guard against abuse, so that a debtor cannot not rely on acts it might take unilaterally to change its COMI between the date of the original winding up petition and the date when the liquidators' recognition application is heard, which may be a period of many months. There should be

no distinction in principle between such manipulation by a debtor or by its liquidators.

### **Working Against Commended**

Against this background, the work of the US delegation to the UNCITRAL Working Group is to be commended: they are seeking to promote consistency of treatment and certainty of outcome in Chapter 15 cases by proposing legislative amendments to the Bankruptcy Code, which give clearer guidance to the courts when addressing the difficulties identified in recent recognition cases. The most obvious of these is the current absence of any definition of COMI in the **Model Law**.

What Chapter 15 (and all cross-border insolvency legislation) needs is to strike an appropriate balance between vesting courts with gatekeeper powers and discretion to do justice in individual cases, whilst creating a predictable statutory regime for office holders.

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December 2010

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