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District Court Enforces German Stay, Ignoring Bankruptcy Code's Chapter 15

Michael B. Schaedle and Evan J. Zucker*

The authors explain that a recent decision by a New York bankruptcy court treated Chapter 15 of the U.S. Bankruptcy Code and the relief it offers as a kind of discretionary alternative to general comity—despite the intent for Chapter 15 to be the "exclusive door to ancillary assistance to foreign proceedings."

In *David Moyal v. Münsterland Gruppe GmbH & Co. KG* (the "New York Action"),[1] the U.S. District Court of the Southern District of New York (the "U.S. District Court" or the "*Moyal* Court") dismissed a lawsuit suit filed by a contract counterparty, seeking damages for a breach of a contract, because Münsterland Gruppe GmbH & Co. KG ("MGKG") had commenced a German insolvency proceeding.

Specifically, the U.S. District Court recognized MGKG's German insolvency proceeding and the relief accorded to a debtor under German insolvency law under principles of comity, including a moratorium barring all litigations against a German debtor and a German law requirement that all claims against a German debtor must be adjudicated in a central German forum.

In so ruling, the U.S. District Court summarily rejected as "absurd" the need for recognition under Chapter 15 of the U.S. Bankruptcy Code of MGKG's German insolvency proceeding. And so, by implication, the *Moyal* Court treated Chapter 15 and the relief it offers as a kind of discretionary alternative to general comity—despite the explicit intent behind the UNCITRAL Model Law on Insolvency, as enacted in Chapter 15, to be the "exclusive door to ancillary assistance to foreign proceedings."[2]

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[1] *Moyal v. Münsterland Gruppe GmbH & Co. KG*, 2021 U.S. Dist. LEXIS 93398.

[2] Collier on Bankruptcy ¶ 1509.03 (16th ed. 2018) (quoting H.R. Rep. No. 109031(I), 110 (2005) ("This section concentrates the recognition and deference process in one United States court."); UNCITRAL Model Law on Cross-Border Insolvency with Guide to Enactment and Interpretation, January 2014 (the "Guide to Enactment"), at 21 (https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/1997-model-law-insol-2013-guide-enactment-e.pdf).

MOYAL'S CLAIM AGAINST MGKG

On February 1, 2019, Moyal commenced the New York Action in the New York County Supreme Court seeking damages from MGKG for breach of a distribution agreement. The New York Action was subsequently removed to the U.S. District Court. Due to a lack of financial resources to defend itself, MGKG did not answer the complaint and conceded liability. Moyal, therefore, moved for entry of a default judgment and an inquest was commenced on the appropriate amount of damages.

Prior to the entry of final judgment on the amount of MGKG's damages, on March 11, 2021, MGKG commenced an insolvency proceeding under the German Insolvency Act in the District Court of Münster, Germany. Pursuant to Section 240 of the German Code of Civil Procedure, the commencement of the bankruptcy proceeding automatically stayed all previously filed actions against MGKG—at least in Germany. As a result, MGKG's U.S. counsel, filed a notice of the insolvency proceeding and a motion seeking to dismiss or stay the New York Action.

Thereafter, MGKG's insolvency administrator informed MGKG's U.S. counsel that by operation of German law, the U.S. counsel's mandate to represent MGKG was terminated upon the commencement of the insolvency proceeding. MGKG's U.S. counsel subsequently moved to withdraw as counsel.

Unsurprisingly, Moyal opposed the termination of the New York Action. Among other arguments, in his opposition, Moyal argues that Chapter 15 of the U.S. Bankruptcy Code provides the exclusive means to recognize a foreign insolvency proceeding and stay actions within the United States.

Specifically, Moyal relied upon the express language of Section 1509(a) of the Bankruptcy Code, which provides "[a] foreign representative may commence a case under section 1504 by filing directly with the court a petition for recognition of a foreign proceeding under section 1515." And, without recognition, a foreign representative does not have the capacity to sue and be sued in the United States.[3]

In response, MGKG first argued that Chapter 15 is only a remedy available to a foreign representative in the United States and because MGKG's insolvency administrator was not a party to the New York Action, recognition was irrelevant.[4]

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[3] *See* 11 U.S.C. § 1509(b) ("if the court grants recognition . . . the foreign representative has the capacity to sue and be sued in a court in the United States").

[4] *See* Defendant's Reply in Further Support of its Motion to Dismiss or Stay this Action, Case

Second, MGKG argued Chapter 15 relief was unnecessary because MGKG had no known assets in the United States and any judgment for damages by Moyal would still be subject to a proceeding in Germany to enforce the judgment.[5]

Third, MGKG argued that Chapter 15 does not preempt common law principles of comity.[6]

On May 17, 2021, the U.S. District Court entered its opinion and order dismissing the New York Action (the "Opinion").

In the Opinion, the U.S. District Court found comity requires the dismissal of the New York Action. Specifically, "[d]eference to a foreign bankruptcy proceeding is appropriate where 'the foreign proceedings are procedurally fair and . . . do not contravene the laws or public policy of the United States.'"[7] And, in the New York Action, the U.S. District Court found that MGKG had shown that the German insolvency proceeding was procedurally fair, providing for an equitable distribution of assets and making no distinction between foreign and domestic creditors. The U.S. District Court rejected the notion that a Chapter 15 proceeding is required to stay or cause the dismissal of the New York Action, finding such argument to be "absurd and would fly in the face of comity principles because courts regularly grant comity on the request of a party other than a foreign representative."[8]

CHAPTER 15 REPLACED AN AD HOC COMITY ANALYSIS FOR RECOGNITION OF A FOREIGN INSOLVENCY PROCEEDING

In coming to its conclusion, the U.S. District Court rests its Opinion on theories that appear to conflict with the intent and mandate of Chapter 15.

First, its reliance on the notion that courts regularly provide comity to foreign insolvency proceedings without Chapter 15 recognition seems to conflate recognition of a foreign insolvency-related judgment with recognition

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No. 19-cv-04946, Doc No. 114, at 6 (Apr. 27, 2021, S.D.N.Y.) (citing *Trikona Advisers, Ltd. v. Chugh*, 846 F.3d 22, 31 (2d Cir. 2017) ("11 U.S.C. § 1515 does not apply generally to parties, but, by its terms, requires only 'foreign representatives' to apply for recognition of a foreign judgment in bankruptcy.")).

[5] *Id.* at 7 (citing *JP Morgan Chase Bank v. Altos Hornos de Mex., S.A. de C.V.*, 412 F.3d 418, 424 (2d Cir. 2005) (Second Circuit has "repeatedly held that U.S. courts should ordinarily decline to adjudicate creditor claims that are the subject of a foreign bankruptcy proceeding.")).

[6] *Id.* at 6.

[7] *Moyal v. Münsterland Gruppe GmbH & Co. KG*, 2021 U.S. Dist. LEXIS 93398.

[8] Opinion at 6 n.1.

of a foreign insolvency proceeding. Courts that have provided assistance in aid of a foreign insolvency, without Chapter 15 recognition, usually have done so when enforcing an insolvency-related judgment.

Essentially, in such a context, the U.S. court is simply giving preclusive effect to a specific factual and legal finding made by a foreign court.[9] For example, in *EMA GARP Fund v. Banro Corporation*,[10] the U.S. District Court dismissed an action, on comity grounds, based on a foreign insolvency judgment that released all claims asserted in the action pending in the U.S. District Court.[11] On the other hand, where a party is seeking "assistance of the district court in enforcing or administering a foreign liquidation proceeding," Chapter 15 recognition is required.[12]

In the New York Action, MGKG's motion to dismiss was akin to seeking recognition and assistance in administering the Germany insolvency proceeding.

Specifically, MGKG sought assistance of a U.S. court with the claims administration process by asserting that Moyal's damage claim should be dismissed because of the existence of a German insolvency moratorium on actions against MGKG as a debtor and the German law requirement that claims be adjusted in a central forum governed by German law. The German moratorium is akin to the U.S. automatic stay under the U.S. Bankruptcy Code, which is a key tool and feature of American bankruptcy and collective remedies thereunder.[13] As a result of the moratorium, MGKG argued that the

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[9] 8 Collier on Bankruptcy ¶ 1509.02 (16th ed. 2021).

[10] *EMA GARP Fund v. Banro Corporation*, No. 18 CIV. 1986 (KPF) (S.D.N.Y. Feb. 21, 2019).

[11] *See* Michael B. Schaedle and Evan J. Zucker, *Enforcement of an Insolvency-Related Judgment Does Not Require Recognition under Chapter 15*, Pratt's Journal of Bankruptcy Law (Vol. 16, Feb./Mar. 2020).

[12] *Id.*

[13] *Compare* Section 240 of the German Code of Civil Procedure ("[i]n the event of insolvency proceedings being opened against a party, [all other] proceedings shall be interrupted to the extent they concern the insolvent estate until they can be resumed in accordance with the rules applying to the insolvency proceedings, or until the insolvency proceedings are terminated.") *with* 11 U.S.C. 362(a) ("[a] petition filed . . . operates as a stay, applicable to all entities, of—(1)the commencement or continuation, . . . , of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case. . . ."); *see generally, In re Onouli-Kona Land Co.*, 846 F.2d 1170, 1174 (9th Cir. 1988) ("The automatic stay is at the essence of bankruptcy as a procedural forum; the automatic stay makes possible the collective proceeding which sorts out non-bankruptcy entitlement")

merits of Moyal's stayed claim should then be adjudicated fully in Germany, where collective claims reconciliation was taking place.[14]

Second, the Opinion impliedly rested upon a distinction between the foreign representative and the Debtor, in finding that the foreign representative was not requesting comity, and therefore Chapter 15 recognition was not required.[15] But this argument and reasoning does not take into account how a Chapter 15 case protects foreign debtors, entities who are under the control of foreign representatives for the purpose of Chapter 15 commencement. No Chapter 15 case can be commenced by a representative that does not have control over a foreign debtor for such purposes—either by easily ascertainable statutory law or by a specific order of a foreign court naming the representative.[16]

While it is true that MGKG's insolvency administrator was not literally substituted as a named party for MGKG in the New York Action, under German insolvency law, the insolvency administrator was in charge of MGKG's assets and the administration of claims against MGKG. The U.S. District Court did not address the key question—whether the insolvency administrator needed to act as the foreign representative and commence a Chapter 15 to obtain enforcement of key aspects of the German insolvency law in the United States; to wit, the German moratorium and claims reconciliation process.

Here, in effect, the German insolvency administrator, a person appointed to liquidate the debtor's assets or affairs (i.e., the eligible MGKG foreign representative under 11 U.S.C. § 101(24)), through the Debtor's U.S. counsel and the formal vehicle of the German debtor's appearance in the *Moyal* litigation, sought the assistance of a foreign court to protect and maximize the value of a German debtor's assets for the benefit of all creditors in a German insolvency proceeding.[17] This is the precise business of Chapter 15 and the Model Law—a law designed to precisely identify when courts should apply comity to a foreign insolvency proceeding and the collective remedy sought in that proceeding pursuant to a clear, simple, statutory "recognition" standard.[18]

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[14] It should be noted that had MGKG first obtained an order of the German court enjoining the New York Action or finding that its continuation violated the German moratorium then, MGKG might be said to be seeking the enforcement of an insolvency related judgment consistent with Chapter 15.

[15] *See* Opinion at 6 n.1.

[16] *See* 11 U.S.C. § 1515.

[17] *See* 11 U.S.C. § 1501(a)(3)–(4).

[18] Guide to Enactment, at 28 ("One of the key objectives of the Model Law is to establish simplified procedures for recognition of qualifying foreign proceedings that would avoid

The fact that, in extending comity, the U.S. District Court considered many of the same factors as a bankruptcy court can in ordering specific additional relief for a foreign debtor under Section 1507 of the Bankruptcy Code, including whether the German insolvency proceeding provided "protection of claim holders in the United States against prejudice and inconvenience in the processing of claim in such foreign proceeding," did not obviate the need for prior Chapter 15 recognition. Recognition is the finding that comity should be done to a foreign collective remedy. It is the key predicate to a U.S. federal court acting as an ancillary to a foreign court in bankruptcy.

The Opinion's application of comity rested primarily on cases decided prior to the enactment of Chapter 15 under repealed Bankruptcy Code Section 304, which vested substantial discretion in bankruptcy courts to determine when to support a foreign insolvency process. Congress enacted Chapter 15 to expressly avoid the results of the Opinion—that is, recognition of a foreign insolvency proceeding by a court other than the bankruptcy court and outside of the clear, almost mechanistic governors of recognition under Chapter 15.

Chapter 15's legislative history confirms that Chapter 15 "is intended to be the exclusive door to ancillary assistance to foreign proceedings" and that "[t]he goal [of Section 1509] is to concentrate control of these questions in one court. That goal is important in a Federal system like that of the United States with many different courts, state and federal, that may have pending actions involving the debtor or the debtor's property."[19] The House Report goes on to note that under prior law, some courts had:

> granted comity suspension or dismissal of cases involving foreign proceedings without requiring a[ ] petition or even referring to the requirements of that section. Even if the result is correct in a particular case, the procedure is undesirable, because there is room for abuse of comity. Parties would be free to avoid the requirements of this chapter and the expert scrutiny of the bankruptcy court by applying directly to a state or Federal court unfamiliar with the statutory requirements.[20]

Accordingly, even though the result in MGKG's case was correct—the dismissal of the New York Action—the Opinion directly conflicts with

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time-consuming legalization or other processes and provide certainty with respect to the decision to recognize.").

[19] H.R.Rep. No. 109-31, at 110–11 (2005).

[20] *Id.*; *see also* Guide to Enactment at 21 ("[a]pproaches based purely on the doctrine of comity or on exequatur do not provide the same degree of predictability and reliability" as the Model Law).

legislative history for Chapter 15 and "is undesirable" because of the precedent it sets (i.e., that "parties would be free to avoid the requirements" of Chapter 15 relief).[21]

IMPLICATIONS

The *Moyal* case is likely to be an outlier given the clear and mandatory requirements of Chapter 15. Further, *Moyal* will be of little use to complex foreign debtors who need to control multiple stakeholder interests and subject a large U.S. collective of claims and rights to a foreign collective remedy. Ad hoc informal comity in multiple U.S. courts is an inefficient way to bind creditors to a liquidation or restructuring of assets.

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[21] H.R.Rep. No. 109-31, at 110–11 (2005).