CENTRE OF MAIN INTERESTS UNDER THE AUSTRALIAN *CROSS-BORDER INSOLVENCY ACT 2008*: LESSONS FROM THE UNITED STATES

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The recent passage of the *Cross-Border Insolvency Act 2008* (Cth) in Federal Parliament brings Australian domestic law a step closer to the United Nations Commission on International Trade Law (UNCITRAL) Model Law and in line with many of Australia's trading partners. The aim is to allow foreign creditors and foreign insolvency practitioners easier access to Australian assets of debtors. The application of the Model Law is dependent upon the operation of many factors, including the concept of centre of main interests (COMI) which is integral to the recognition procedures in the Model Law. It impacts on the ability of creditors to exercise their rights against the debtor's business and assets. Neither the *Cross-Border Insolvency Act 2008* (Cth) nor the Model Law, however, offer a definition of COMI. The purpose of this article is to explore the meaning and the potential application of COMI in Australia. This article assesses, with reference to recent judicial precedents in the United States, the likely operation of COMI in Australia. An examination of this issue is useful for the potential guidance it can offer to Australian courts when considering the concept of COMI in our jurisdiction.

I. INTRODUCTION

Many complex issues may arise in the context of cross-border insolvency, including the principal issue of identifying and satisfying conditions for recognition of a foreign insolvency proceeding and for granting relief. The location of a debtor's centre of main interests is of great significance in cross-border insolvencies. It impacts on the ability of creditors to exercise their rights against the debtor's business and assets. The *Cross-Border Insolvency Act 2008* (Cth)[1] applies the concept of 'centre of main interests' (COMI) to allow a court to determine whether a proceeding is a 'foreign main proceeding' or a 'foreign non-main proceeding'.

However, neither the *Cross-Border Insolvency Act 2008* (Cth), nor the *UNCITRAL Model Law on Cross-Border Insolvency*[2] on which it is based, offer a definition of COMI. The reason for this deliberate omission is provided in the Explanatory Memorandum to the Bill:[3]

> The Bill does not seek to define COMI as a considerable body of common law exists in overseas jurisdictions in relation to that concept. It is expected that Australian courts will be guided by that body of law in considering the definition of COMI in the context of the Bill. Such an approach will ensure that Australian law is in harmony with that in other jurisdictions.

The purpose of this article is to explore the meaning and the potential application of COMI in Australia as a result of the enactment of the *Cross-Border Insolvency Act 2008* (Cth). This article assesses, with reference to judicial precedents in the United States following a spate of cases arising from the fallout of the subprime crisis and global credit crunch,[4] the likely operation of COMI in Australia. An examination of this issue is useful for the

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1 The *Cross-Border Insolvency Act 2008* (Cth) has now been passed and received royal assent on 26 May 2008. Part 1 of the Act commenced on that date. Parts 2, 3 and 4 of the Act came into effect on 1 July 2008.

2 United Nations Commission on International Trade Law (UNCITRAL), *UNCITRAL Model Law on Cross-Border Insolvency* (1997) <http://www.uncitral.org/pdf/english/texts/insolven/insolvency-e.pdf> at 10 December 2008.

3 Explanatory Memorandum, Cross–Border Insolvency Bill 2008 (Cth).

4 See below Part III.

potential guidance it can offer to Australian courts when considering the concept of COMI in our jurisdiction.

Part II of this article provides an overview of Chapter III of the Model Law which contains key provisions dealing with recognition of a foreign proceeding and relief. The operation of Chapter III of the Model Law is pivotal in cross-border insolvencies as it is concerned with a threshold requirement of recognition that must be met. The incorporation of Chapter III into the *Cross-Border Insolvency Act 2008* (Cth) addresses the fundamental question of whether foreign insolvency proceedings will be recognised in Australia and, if so, the extent to which Australian courts will give effect to those foreign proceedings. Part II of this article focuses attention on the relevant provisions in Chapter III of the Model Law, in particular Articles 15-21, concerned with such issues. Part III of the article provides commentary on the potential application of Articles 15-21 with reference to international jurisprudence that has focused on the Model Law. It surveys the judicial approaches adopted in the United States and highlights the judicial tension and controversy that currently exists in the United States demonstrating the absence of a uniform approach to the threshold requirement of recognition. Notwithstanding the uncertain position in the US to date, there are some interpretational aspects of the decisions that may be instructive for Australian courts. Thus, Part IV draws on the lessons from the US experience and concludes with some observations about the way forward in the interpretation and application of Chapter III of the Model Law.

II. RECOGNITION OF FOREIGN PROCEEDINGS AND RELIEF

One of the main aims of the new *Cross-Border Insolvency Act 2008* (Cth),[5] for the purposes of this article and for practitioners, is to encourage cooperation between courts and insolvency practitioners of different jurisdictions. This is achieved through the key mechanism of recognition, located within Chapter III of the Model Law and incorporated into the *Cross-Border Insolvency Act 2008* (Cth) through operation of s 6 of the Act which confers the force of law onto the Model Law in Australia. The design principles, centred on the recognition of foreign proceedings, form the focus of the discussion below.

Article 17 of the Model Law sets out the criteria affecting the decision to recognise foreign proceedings. Essentially, recognition turns on the satisfaction of the concepts relating to 'foreign main proceeding' and 'foreign non-main proceeding'. In turn, Article 2 of the Model Law defines the former as taking place in the state where the debtor has the centre of its main interests (COMI);[6] in contrast, the latter takes place in a state where the debtor has an establishment.[7] Article 2(f) offers guidance to the meaning of 'establishment' by defining that concept with reference to 'any place of operations where the debtor carries out a non-transitory economic activity with human means and goods or services.' The significance of the distinction in types of recognition ('main' or 'non-main' proceeding) lies in the nature of relief available, discussed below.

Statutory presumptions concerning recognition are available to aid in the decision to recognise a foreign proceeding. Article 16 states, inter alia,[8] that in the absence of proof to the contrary, [9] the debtor's COMI is presumed with reference to the debtor's registered office, or habitual residence in the case of an individual. Insight into the purpose and operation of the presumption can be gained from the UNCITRAL Guide to Enactment of the Model Law on Cross-Border Insolvency which explains that Article 16

5 For broader discussion on the aims of the new legislation, see Anil Hargovan, '*The Cross-Border Insolvency Act 2008* (Cth): Issues and Implications' (2008) *Australian Journal of Corporate Law* (forthcoming).

6 See 11 USC § 1502(4) (2005) of the US Bankruptcy Code for identical provision.

7 See 11 USC § 1502(5) (2005) of the US Bankruptcy Code for identical provision.

8 The other two assumptions concern identity of foreign representatives and authenticity of documents in support of the application for recognition.

9 See 11 USC § 1516 (2005) of the US Bankruptcy Code for a modified provision. Chapter 15 changed the Model Law standard that established the presumption to make it clearer that the ultimate burden is on the foreign representative. To this end, Chapter 15 has substituted the word 'proof' with the word 'evidence' to now read 'in the absence of evidence to the contrary'.

> allow[s] the court to expedite the evidentiary process; at the same time they do not prevent, in accordance with the applicable procedural law, calling for or assessing other evidence if the conclusion suggested by the presumption is called into question by the court or an interested party.

With regard to the recognition of foreign main proceedings, the UNCITRAL Guide to Enactment of the Model Law on Cross-Border Insolvency explicitly warns against consideration of factors other than the location of the debtor's COMI:[10]

> [It] is not advisable to include more than one criterion for qualifying a foreign proceeding as a main proceeding and provide that on the basis of any of those criteria a proceeding could be deemed a main proceeding. An approach involving such a 'multiple criteria' would raise the risk of competing claims from foreign proceedings for recognition as the main proceeding.

Once the definitional aspects under Article 17, discussed above, are met, the decision to recognise a foreign proceeding confers many benefits; in particular, upon recognition as a foreign main proceeding which confers much broader relief.

Upon recognition of a proceeding as a foreign main proceeding, Article 20 allows for the following consequences:

a) commencement or continuation of individual actions or proceedings concerning the debtor's assets, rights, obligations or liabilities is stayed;
b) execution against the debtor's assets is stayed;
c) the right to transfer, encumber or otherwise dispose of any assets of the debtor is suspended.

Significantly, as seen above, recognition of a foreign insolvency proceeding produces an immediate and automatic moratorium which is capable of modification in light of local insolvency laws. Relief in respect of a foreign non-main proceeding is limited to assets that, according to local laws, should be administered in that proceeding or concerns information required in that proceeding.[11] Once a foreign proceeding is recognised by the Court, either as main or non-main proceeding, Article 21 confers discretion on the Court to grant relief as necessary to protect the debtor's assets or the creditors' interests.

The *Cross-Border Insolvency Act 2008* (Cth) tracks the provisions of Chapter III of the Model Law. The key concept of COMI, derived from the European Union Convention on Insolvency Proceedings, in the Model Law, has been adopted into Australian insolvency law; and herein lays the difficulty. Since the adoption of COMI as the gateway to recognition as a main proceeding under the Model Law, it has since remained 'stubbornly undefined'.[12]

The judicial opportunity, however, for further exploration of this concept has recently arisen in the wake of the subprime mortgage crisis in the United States. Divergent judicial approaches to the application of the COMI concept in the United States, in *Re SPhinX*[13] and in *Re Bear Stearns*,[14] arising out of similar facts involving insolvent hedge funds have excited some controversy.[15] Notwithstanding the resultant tension in US law, it is

10 UNCITRAL, 'Guide to Enactment of the Model Law on Cross-Border Insolvency' in *UNCITRAL Model Law on Cross-Border Insolvency* (1997) above n 2, [127].

11 See further, Rosalind Mason, 'Cross-Border Insolvency Law: Where Private International Law and Insolvency Law Meet' in Paul Omar (ed), *International Insolvency Law: Themes and Perspectives* (2008) ch 2, 53-58; Rosalind Mason, 'Cross-Border Insolvency Bill 2007: The UNCITRAL Model Law Enters the Parliamentary Stage Yet Australia Still Awaits the Final Act (2007) 15 *Insolvency Law Journal* 212, 223-225.

12 Judge Leif Clark, '"Center of Main Interests" Finally Becomes the Center of Main Interest in the Case Law' (2008) 43 *Texas International Law Journal Forum* 14, 14.

13 *Re SPhinX, Ltd* (2006) 351 BR 103 (Bankr SDNY); aff'd (2007) 371 BR 10 ('*SPhinX*').

14 *Re Bear Stearns High-Grade Structured Credit Strategies Master Fund Ltd* (2007) 374 BR 122 (Bankr SDNY, 5 September 2007); aff'd (2008) 389 BR 325 by the US District Court (Bankr SDNY, 27 May 2008) ('*Bear Stearns*'). The recent decision in *Re Basis Yield Alpha Fund* (2008) 381 BR 37 followed the judicial approach adopted in *Bear Stearns*.

15 See below n 26-27.

instructive to refer to the experiences in the US jurisdiction for guidance on the potential application of COMI in Australia.

III. UNITED STATES JURISPRUDENCE

It pays to examine in detail the facts and contrasting decisions arising from both *SPhinX* and *Bear Stearns*, decided under Chapter 15 of the Bankruptcy Code which was enacted in 2005 to implement the *Model Law on Cross–Border Insolvency*. Both cases presented opportunities for US bankruptcy courts to consider, in a comprehensive way, the working of the Model Law in the US and are thus considered significant for this reason. Prior to the decision in *SPhinX*, there appears be no published case involving a dispute over COMI under Chapter 15 of the Bankruptcy Code.

Both cases involved a Chapter 15 petition for recognition in the US Bankruptcy Court, preceded by a winding up proceeding in the Grand Court of the Cayman Islands, but with different approaches to the mandatory eligibility test for recognition discussed in Part II of this article.

A. Re SPhinX

The SPhinX Funds ('Funds'), whose business consisted of buying and selling securities, were established as offshore entities to exploit favourable tax benefits and regulations in the Cayman Islands. Although regulated in the Cayman Islands, the Funds did not conduct a trade or business in the Cayman Islands. The Funds were prohibited as 'exempted companies' under Cayman Islands law from engaging in business in the Cayman Islands except in furtherance of their business conducted outside of that jurisdiction.[16]

From the Funds' inception, their hedge fund business was conducted under a fully discretionary investment management contract by another entity, a Delaware corporation located in New York City. Except for the maintenance of corporate books and records required under Cayman Islands law, the Funds had no assets in the Cayman Islands. Substantially, all of the Funds' assets were in the United States — at least 90 percent of the Funds' approximately $500 million of assets were located in accounts in the United States. They had no employees and no physical offices in the Cayman Islands or elsewhere. None of the directors resided in the Cayman Islands, nor were any board meetings held there. Investors, located throughout the world, sent their subscriptions to the Cayman Islands. This review facility was devised, apparently, for purposes of compliance with Cayman Islands anti-money-laundering requirements. Corporate administration of the Funds was conducted primarily in the United States. The Funds' auditors, a major international accounting firm, had a Cayman Islands address in compliance with the requirements of local law. The evidence, however, did not make clear how much work the auditors actually performed in the Cayman Islands.

Voluntary winding up proceedings in the SPhinX Funds were commenced in the Cayman Islands. In conjunction with this event, the insolvency representatives of the SPhinX Funds filed petitions in the US Bankruptcy Court, seeking recognition of the foreign proceedings as foreign main proceedings or, in the alternative, as foreign non-main proceedings under Chapter 15 of the Bankruptcy Code. As noted in Part II of this article, Chapter 15 contains provisions substantially similar to the Australian *Cross-Border Insolvency Act 2008* (Cth).[17]

Of necessity, in determining when the proceeding should be recognised as a 'foreign main proceeding', the judicial inquiry requires an examination of COMI and its operation. The judgment in *Re SPhinX*, for reasons discussed below, has received trenchant criticism for its inadequate attention to the mandatory eligibility test for recognition under Chapter 15.

16 *Companies Law (2004 Revision)* (Cayman Islands) s 193.
17 Note, however, a significance difference discussed in Part II.

The Bankruptcy Court denied recognition of the Cayman Islands proceedings as foreign main proceedings and afforded recognition as foreign non-main proceedings. However, the Court declined relief on the facts due to the improper purpose associated with the Chapter 15 petition.[18]

Controversially,[19] Judge Robert Drain indicated a preparedness to recognise the case as a foreign main proceeding on the basis the funds were registered in the Cayman Islands. In reaching that position, the Court reviewed Chapter 15 and concluded that recognition of foreign proceedings involved a two-step process. Firstly, the Court must determine whether the foreign representatives should be recognised and given access to the local courts. The Court did not anticipate this task to be problematic. Secondly, the Court must determine whether the foreign proceedings can be recognised as main or non-main. Judge Drain noted that the statutory and practical effects of the distinction between foreign main and non-main were 'not as important as the parties may believe.' The Court was influenced by considerations of flexibility inherent in Chapter 15 and by case law which predated Chapter 15.

In determining the debtor's COMI, Judge Drain held that[20]

> [factors influencing COMI] should be viewed in light of Chapter 15's emphasis on protecting the reasonable interests of parties interest pursuant to fair procedures and the maximization of the debtor's value. Because their money is ultimately at stake, one generally should defer, therefore, to the creditors' acquiescence in or support of a proposed COMI …

Although the objective factors pointed to the debtors' COMI being located outside of the Cayman Islands, Judge Drain was prepared to find the debtors' COMI in the Cayman Islands and recognise the proceedings as foreign main proceedings for the following reasons:[21]

> [B]ecause these are liquidation cases in which competent [insolvency representatives] under the supervision of the Cayman Court are the only parties ready to perform the winding up function, and, importantly, the vast majority of the parties in interest tacitly support that approach, normally the Court would recognize the Cayman Islands proceedings as main proceedings …

Notwithstanding that objective facts did not show any establishment in the Cayman Islands, Judge Drain recognised the Cayman proceedings as foreign non-main proceedings.[22] On similar facts, the Bankruptcy Court in *Bear Stearns* adopted a fundamentally different approach to Chapter 15 discussed below. The implications of the conflicting decisions for Australian courts are discussed in Part IV.

B. Re Bear Stearns

Bear Stearns operated open-ended investment companies incorporated in the Cayman Islands,[23] structured as limited liability companies and subject to Cayman Islands tax law. In particular, two of the funds designed to attract sophisticated investors were registered as 'exempted' companies under Cayman Islands law and, similar to the facts *Re SPhinX*, resulted in the same trading restrictions and conditions discussed earlier.[24]

18 A primary basis for the petition, as conceded by the petitioners, was to improperly frustrate a settlement by obtaining an automatic stay to block the appeal.

19 Contra *Bear Stearns* (2007) 374 BR 122; aff'd (2008) 389 BR 325

20 *SPhinX* (2006) 351 BR 103, 117.

21 Ibid 121.

22 The appellate court in *SPhinX* did not address this issue, hence no reference is made to that decision in the article.

23 The investment companies operated funds that invested in a range of financial products and securities including derivatives, swaps, futures, options and, significantly, mortgage-backed securities.

24 Bear Stearns High-Grade Structured Credit Strategies Master Fund Ltd (High Grade Fund) and the Bear Stearns High-Grade Structured Credit Strategies Enhanced Leverage Master Fund Ltd (Enhanced Fund) are collectively referred to as the 'Funds'.

PFPC Inc (Delaware) was the administrator of the Funds. The daily function of the administrator included accounting and clerical functions, maintaining the Funds' principal administrative records as registrar, disbursing payment of expenses of the Funds and responding to inquiries from the general public. The books and records of the Funds were maintained and stored in Delaware. Bear Stearns Asset Management Inc (BSAM), incorporated in New York, was the investment manager for the Funds and the assets managed by BSAM were located within the Southern District of New York. The investor registers were held by a related company in Dublin, Ireland.

As a consequence of the subprime mortgage crisis in the United States in early 2007, the Funds suffered a significant devaluation of their asset portfolios. The financial downturn led to margin calls from the Funds' trading counterparties which the Funds were unable to meet. Default notices were issued by the counterparties who, in turn, elected to exercise their rights as secured creditors and sold off assets over which they held security interests.[25]

On 30 July 30 2007, the Funds' board of directors filed winding-up petitions in the Cayman Islands under local company laws[26] and sought the appointment of foreign representatives to act as joint provisional liquidators of the Funds. The Cayman Court granted such orders the next day, subject to the supervision of the Cayman Grand Court.

Against this factual background, the insolvency representatives of the Funds sought recognition of the Cayman liquidation proceedings in the US Bankruptcy Court under Chapter 15 of the Bankruptcy Code. Thus, in common with *SPhinX*, the Bankruptcy Court had to resolve the central issue of whether the Cayman Islands proceedings were either main or non-main proceedings in accordance with the definitional elements discussed in Part II of this article. The difference, however, lay in the primacy afforded to COMI as the gateway to recognition of foreign proceeding in *Bear Stearns*.

Judge Burton Lifland denied main recognition on the grounds that the Funds' COMI, as defined under Chapter 15, was in the United States and not the Cayman Islands.

Unlike the two-step judicial approach adopted in *SPhinX*, Judge Lifland considered the process of recognition of a foreign proceeding to be single-step process which required the recognition to be coded as either main or non-main. Drawing support from academic commentators (who were also involved in the drafting of the law),[27] the determination of whether the foreign proceedings were main or non-main was held to be a formulaic one requiring compliance with a rigid procedural structure. Judge Lifland endorsed the view that if the foreign proceeding is not pending in a country where the debtor has its COMI or where it has an establishment, then the foreign proceeding is simply not eligible for recognition under Chapter 15.[28]

Turning attention to the definitional test for recognition under Chapter 15, Judge Lifland traced the origins of the COMI concept to the European Convention, and relied on the regulation adopting the European Convention,[29] and also on European case law,[30] to conclude that the concept of COMI generally equates with the concept of a 'principal place of business' in US law.

25 For example, in June 2007, Merrill Lynch exercised its rights as a secured creditor and sold off some of the assets which exacerbated the devaluation of the Funds' asset portfolios.

26 *Companies Law (2004 Revision)* (Cayman Islands).

27 Jay Westbrook, 'Locating the Eye of the Financial Storm' (2007) 32 Brook Journal of International Law 3; Daniel Glosband 'SPhinX Chapter 15 Opinion Misses the Mark' (December 2006) 25(10) *American Bankruptcy Institute Journal* 44. It should be noted that Judge Lifland was among the authors of the Model Law and Chapter 15 of the Bankruptcy Code.

28 Glosband, above n 27.

29 In the regulation adopting the European Convention, the COMI concept is elaborated upon as 'the place where the debtor conducts the administration of its interests on a regular basis and is therefore ascertainable by third parties': EU Council Reg (EC) No 1346/2000.

30 *Re Eurofood IFSC Ltd* (2006) ECR I-3813, 18-19.

The Bankruptcy Code does not state the type of evidence required to rebut the presumption that the COMI is the debtor's place of registration or incorporation. The Court noted, with reliance upon *SPhinX*, the variety of factors that might justify COMI status:[31]

> [T]he location of the debtor's headquarters; the location of those who actually manage the debtor (which, conceivably could be the headquarters of a holding company); the location of the debtor's primary assets; the location of the majority of the debtor's creditors or of a majority of the creditors who would be affected by the case; and/or the jurisdiction whose law would apply to most disputes.

Turning to the facts, Judge Lifland found that the petitioners' own pleadings provided the evidence to establish that the Funds' COMI is in the United States, not the Cayman Islands. The Bankruptcy Court in *Bear Stearns* held:[32]

> The only adhesive connection with the Cayman Islands that the Funds have is the fact that they are registered there. … The only business done in the Cayman Islands apparently was limited to those steps necessary to maintain the Funds in good standing as registered Cayman Islands companies, thus the Funds closely approximate the 'letterbox' companies referred to in the *Eurofoods* decision.

Turning attention to the operation of the presumption under Chapter 15, which presumes that the COMI is the place of the debtor's registered office but only in the absence of evidence to the contrary, Judge Lifland held that the petitioners demonstrated such evidence to the contrary in the following manner:[33]

> [T]here are no employees or managers in the Cayman Islands, the investment manager for the funds is located in New York, the Administrator that runs the back-office operations of the Funds is in the United States along with the Funds' books and records and prior to the commencement of the Foreign Proceeding, all of the Funds' liquid assets were located in the United States … the investor registries are maintained and located in the Republic of Ireland; account receivables are located throughout Europe and the United States; counterparties to master repurchase and swap agreements are based inside and outside the United States but none are claimed to be in the Cayman Islands.

Based on the evidence above, and in reliance upon the European Court,[34] the Bankruptcy Court concluded that each of the Funds' real seat, and therefore their COMI, is the United States — the place where the Funds conduct the administration of their interests on a regular basis and is therefore ascertainable by third parties.

In rejecting recognition of the foreign proceedings as main proceedings, Judge Lifland stressed the need for the Bankruptcy Court to make an independent determination as to whether the foreign proceedings meet the definitional tests under Chapter 15. His Honour noted the departure from the approach adopted in *SPhinX* and held:[35]

> I part with the dicta in the *SPhinX* decision opining that if the parties in interest had not objected to the Cayman Islands proceeding being recognized as main, recognition would have been granted under the sole grounds that no party objected and no other proceeding had been instituted anywhere else … to the extent that non objection would make the recognition process a rubber stamp exercise, this Court disagrees with the dicta in the *SPhinX* decision.

Similarly, Judge Robert Gerber in *Re Basis Yield Alpha Fund* concurred with the observations of Judge Lifland in *Bear Stearns* and held that the determination of recognition is not a rubber stamp exercise.[36] Whilst expressing caution against the

31 *Bear Stearns* (2007) 374 BR 122, 128.
32 Ibid 129.
33 Ibid 130.
34 *Re Eurofood IFSC Ltd* (2006) ECR I-3813, 18-19.
35 *Bear Stearns* (2007) 374 BR 122, 130.
36 (2008) 381 BR 37.

pendulum swinging too far to deprive parties of the use of presumptions, Judge Gerber held:[37]

> But the decision necessarily must remain with the court, which may not be satisfied with reliance on the presumption or not, consistent with its ultimate responsibility, and power, to determine that the requirements of sections 1502 and 1517 [dealing with recognition for a main proceeding] are satisfied.

On appeal to the District Court for the Southern District of New York, in *Bear Stearns*,[38] the central issue that fell for determination centred on whether the Cayman Islands proceedings were either main or non-main proceedings in accordance with the definitional elements discussed in Part II of this article. Judge Robert Sweet of the District Court affirmed Judge Lifland's decision in *Bear Stearns* and, more significantly, the judicial approach adopted in the determination of recognition. In particular, the proposition that principles of comity (based on principles of cooperation with foreign courts) do not figure in the recognition analysis was upheld.[39] Judge Sweet held, contrary to the judicial approach in *Re SPhinX*, that the plain language and history of Chapter 15 requires a factual determination with respect to recognition before principles of comity come into play.

Judge Sweet also affirmed that the appellants in *Bear Stearns* had failed to allege facts establishing non-main recognition. For the latter type of recognition to arise, the debtor must show an establishment as defined under Chapter 15 (i.e. any place of operations where the debtor carries out non-transitory economic activity). This is a factual question, with no presumption in favour. Judge Sweet held that auditing activities and preparation of incorporation papers by a third party in the Cayman Islands did not constitute 'operations' or 'economic activity' by the Funds.[40]

In a powerful endorsement of Judge Lifland's reasoning in *Bear Stearns*, Judge Sweet expressed the hope that the resolution of the issues may provide some aid to navigation in these uncharted waters.[41]

IV. LESSONS FOR AUSTRALIA

The review of the emerging US experience, in Part III of this article, is instructive for Australian courts for its legal reasoning — notwithstanding the factual matrix in the US cases dealing with troubled offshore hedge funds in tax havens. The value lies in the potential guidance it offers to the Australian courts on the competing approaches in the determination of recognition.

The approach adopted to the issue of recognition under Chapter 15, and in particular to COMI, in *Bear Stearns* (by both levels of the judiciary in the Bankruptcy Court) is to be preferred from a construction and policy perspective over the competing decision in *SPhinX* for the following reasons.

The unitary approach to recognition adopted in *Bear Stearns*, discussed in Part III of this article, appears to be more in tune with the Model Law which requires a proceeding to be either a foreign main proceeding or a foreign non-main proceeding as a prerequisite to recognition.[42] If follows from the judicial analysis in *Bear Stearns* that if the proceeding cannot satisfy either criteria, the Court is powerless to grant recognition. That should be the end of the matter. In determining whether the mandatory eligibility test for recognition is satisfied, COMI has a central role to play under the approach in *Bear Stearns*. Judge

37 Ibid 55.

38 *Re Bear Stearns High-Grade Structured Credit Strategies Master Fund Ltd* (2008) 389 BR 325.

39 Ibid 333.

40 Ibid 338.

41 Ibid 327. The amici to the District Court included members of the group that drafted the Model Law (Jay Westbrook and Daniel Glosband) and assisted with the drafting of Chapter 15.

42 See further, Look Chan Ho 'Proving COMI: Seeking Recognition Under Chapter 15 of the US Bankruptcy Code' [2007] *Journal of International Banking Law and Regulation* 636: 'Lifland J's decision in Bear Stearns clearly comports with the intent and structure of Chapter 15 that the determination of the existence of a foreign main or non-main proceeding is a definitional matter, not a discretionary matter.'

Lifland's analysis in *Bear Stearns*, as affirmed by the District Court, appears to be less tolerant in affording recognition to a jurisdiction in which the debtor has little more than a registered name and a letterbox. Judge Leif Clark observes that *Bear Stearns* attends to the structural integrity of Chapter 15, in effect counselling that only in this way can the door be closed on opportunistic filings designed to subvert the cross-border insolvency regime.[43] The denial of access to foreign representatives in such circumstances is not inconsistent with the aims of the Model Law on which Chapter 15 is modelled.

In contrast, the judicial approach adopted in *SPhinX* does not afford the same degree of primacy to considerations based on COMI when determining recognition of foreign proceedings. This result is reached from a broader statutory construction of Chapter 15 which is plainly at odds with *Bear Stearns*.

Judge Drain's analysis of Chapter 15 in *SPhinX* favoured a two-step process in determining recognition of foreign proceedings. Step one was to determine if the foreign representative was to be accorded recognition and access to the local court, based on mechanical considerations in Chapter 15 relating to speed and efficiency. On the premise that recognition is given, step two requires the Court to simply determine whether the foreign proceeding is a main proceeding or a non-main proceeding. This approach clearly illustrates the secondary role accorded to COMI as a determinant to recognition of foreign proceedings.

The judicial approach adopted in *SPhinX* is difficult to reconcile with the central status accorded to COMI under the Model Law and the decision in *Bear Stearns*. The risks in adopting *SPhinX* to develop a standard for recognition of foreign proceedings have been identified by Daniel Glosband: [44]

> [T]he judgment [in *Re SPhinX*] creates a wholly unnecessary, serious and regrettable breach with European case law [*Re Eurofood IFSC Ltd* (2006) E.C.R. I-3813] on the meaning of key concepts taken from a European statute. It threatens to break the very unanimity that is mean to be at the heart of the Model Law and the goal of uniform interpretation throughout the world …

Apart from offering insight into the approach to be adopted in the determination of the threshold question of recognition in Chapter III of the Model Law, incorporated into the *Cross-Border Insolvency Act 2008* (Cth), the US cases also offer valuable guidance on the meaning of COMI. In *Bear Stearns*, discussed in Part III of this article, COMI was described as similar to the concept of principle place of business. Importantly, the Bankruptcy Court in *SPhinX* and *Bear Stearns* were influenced by the regulation adopting the EU Convention on Insolvency Proceedings which explains that COMI means 'the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties.'[45]

Noting that the Bankruptcy Code does not state the type of evidence relevant to the COMI determination, importantly, both US cases adopted a common approach in identifying a list of potentially relevant factors which a court may use in a COMI determination. The array of factors includes: the location of the debtor's headquarters; the location of those who actually manage the debtor; the location of the debtor's primary assets; the location of the majority of the debtor's creditors or a of a majority of creditors who would be affected by the case; and/or the jurisdiction whose law would apply to most disputes. Given that the *Cross-Border Insolvency Act 2008* (Cth) is also deliberately silent on the standard required for the COMI determination, the US precedents (together with the regulations under the EU Convention) are instructive in this regard.

The US precedents discussed in Part III of this article are also potentially helpful in determining the weight to be given to the statutory assumption to determine COMI,

43 Judge Leif Clark, above n 12, 16.
44 Glosband, above n 27.
45 EU Council Reg (EC) No 1346/2000.

notwithstanding divergent judicial approaches and statutory wording.[46] This issue is particularly relevant when there is an absence of objecting parties in a case, as demonstrated in all three cases discussed in Part III.

Unlike the approach in *Bear Stearns* and *Re Basis Yield Alpha Fund* discussed earlier, the Bankruptcy Court in *SPhinX* placed greater weight on the presumption that a debtor's COMI is located at its registered office. In doing so, sight has been lost of the fact that the COMI presumption was designed for speed and convenience of proof, only where there is no serious controversy. The Court in *SPhinX* treated the COMI presumption as having special evidentiary value when such an approach was unsupported by the facts. The courts must remain free to engage in analysis and use judicial discretion to call for evidence, or assess other evidence, as recognised by the Court in *Bear Stearns* and *Re Basis Yield Alpha Fund*. The preferred approach to this issue is captured by Judge Sweet of the District Court in *Bear Stearns*:[47]

> Appellant's emphasis on the fact that their petition was unopposed is unavailing. The lack of objection to the petition may result from any number of considerations, unknown to the court but subject to any assumption. That absence does not relieve the bankruptcy court of its duty to apply the statute as written.

In Australia, the judicial spotlight is yet to fall onto the concept of COMI and its application. Australia will do well to learn from the US experience to date, following the recent passage of the *Cross-Border Insolvency Act 2008* (Cth), when it enters its uncharted waters and forges its own jurisprudence in the development of an effective cross-border insolvency regime.

46 Chapter 15 changed the Model Law wording. See above Part II.
47 (2008) 389 BR 325, 338.