

Global *Erie* and its Limits: Channeling Jurisdictional Competition for Procedure in Cross-Border Bankruptcies

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Forthcoming, Texas Journal of International Law

Draft as of: July 11, 2021

The subject of this symposium is the competition among jurisdictions to serve as hosts for global bankruptcy cases. The stakes in such a competition are high for judges, lawyers, bankers, and debtors themselves. Status as a destination jurisdiction for large scale bankruptcies can bring legal business and can help cement a jurisdiction as a full-service financial center.¹ New York, London, Hong Kong, and increasingly Singapore have established themselves as choice venues for filing global bankruptcies.² This competition for cases poses a challenge to modified universalism -- the dominant modern approach for administering cross-border bankruptcies -- and its two principal pillars: center of main interest (“COMI”); and comity (recognition).

The question is timely. There are forces in play now that could affect the future of that competition as well as the shape of global bankruptcy practice. These include the fact that: (1) Brexit may affect the way in which UK restructurings are recognized in Europe;³ (2) the advent of

¹ Lynn M. LoPucki, *Courting Failure: How Competition for Big Cases is Corrupting the Bankruptcy Courts* (2005).

² John A. E. Pottow, *The Myth (and Realities) of Forum Shopping in Transnational Insolvency*, 32 *Brook. J. Int'l L.* 32 785 (2007); Gerard McCormack, *Bankruptcy Forum Shopping: The UK and US As Venues Of Choice For Foreign Companies*, *The International and Comparative Law Quarterly* 63, no. 4 (2014): 815-42. (available at: <http://www.jstor.org/stable/43301639>). Within the United States, large company cases tend to be filed in the District of Delaware, the Southern District of New York, and a few other courts. https://lopucki.law.ucla.edu/design_a_study.php?OutputVariable=DistFiled.

³ (<https://www.mondaq.com/uk/insolvencybankruptcy/1074176/a-parting-of-the-ways-the-recent-decision-in-gategroup-puts-schemes-and-restructuring-plans-on-different-roads-to-recognition>). See also, Adam J. Levitin, *Purdue's Poison Pill: The Breakdown of Chapter*

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modern Chapter 11 like regimes throughout the EU may lead to harmonization of rules regarding cross-class cramdown among other things;⁴ and (3) proliferation of new UNCITRAL instruments such as the Model Law on Insolvency Related Judgments (MLJ) and the Model Law on the Insolvency of Enterprise Groups (MLEG), as well as the Legislative Guide on Insolvency may lead to harmonization of substantive law and procedural rules globally.⁵ How these various pieces fit together will have a profound impact, on the effectiveness of bankruptcy law as a tool for preserving enterprise value and on whether that value is distributed fairly.

Modified universalism is the animating principle behind the two major existing international instruments for coordinating cross-border bankruptcies -- the EU Insolvency Regulation (the “EUIR”) and the UNCITRAL Model Law on Cross-Border Insolvencies (Chapter 15 in the United States) (the “MLCBI”). Both instruments are designed to facilitate the reorganization of an enterprise by facilitating the recognition of relief issued by the courts and under the law of the jurisdiction that is the enterprise’s center of main interest (COMI).

This first pillar -- administration of the restructuring at the debtor’s COMI -- is driven by several articles of faith. First, that the claims of creditors and the fate of the debtor ought to be decided in the jurisdiction expected by creditors. Second, that the centralization of the case in or at the direction of one jurisdiction will facilitate an orderly disposition of the debtor’s assets or a coordinated rescue of the business enterprise through recapitalization or a going concern sale. Third, that by limiting jurisdiction to the debtor’s COMI, the debtor will not be able to strategically shift fora to frustrate the legitimate expectations of creditors.⁶ In sum, centralization is desirable because it increases the power of the forum

11's Checks and Balances, 100 *Texas Law Review* __ (forthcoming 2021)(Available at SSRN: <https://ssrn.com/abstract=3851339> or <http://dx.doi.org/10.2139/ssrn.3851339>).

⁴ [EU Directive on Preventive Restructuring Frameworks \(June 2019\) paragraphs 49-58.](#)

⁵ [UNCITRAL Model Law on Recognition and Enforcement of Insolvency Related Judgments \(2018\)](#); [UNCITRAL Model Law on Enterprise Group Insolvency \(2019\)](#); [UNCITRAL Legislative Guide on Insolvency \(2004-2019\)](#).

⁶ Jay L. Westbrook, *A Global Solution to Multinational Default*, 98 *Mich. L. Rev.* 2276 (2000). Available at: <https://repository.law.umich.edu/mlr/vol98/iss7/5>; Irit Mevorach, *The Future of Cross-Border Insolvency: Overcoming Biases and Closing Gaps* (2018).

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court to coordinate the case, and COMI protects creditor expectations by ensuring that the forum will be predictable and related to the operations of the business and its debts.⁷

However, a single coordinated global bankruptcy case is not feasible as a practical matter. So, the second pillar of modified universalism is a recognition regime based on a strong norm of comity. To accomplish this recognition regime, both the EUIR and the MLCBI contemplate that the debtor will open a “main” proceeding at its COMI and will open “secondary” or “ancillary” proceedings where necessary to obtain recognition of relief and/or to seek assistance for and cooperation with the main case.

There is, unfortunately, a central paradox within modified universalism, laid bare by competition among jurisdictions for cases and forum shopping by parties. Coordination through centralization -- essential to value maximization -- is in tension with the due process values associated with participation, equitable treatment, and creditor expectations (reasonable or not) about governing law. This wedge between coordination and due process is driven home by the practical dynamics of jurisdictional competition. Debtors, or debtors in league with certain key creditors, may choose to locate their case in a particular jurisdiction for strategic reasons, distinct from the best interests of the enterprise; the jurisdiction may be chosen with the precise goal of undercutting equitable distribution to stakeholders or frustrating creditor participation.⁸ Because of the centralizing focus of the EUIR and MLCBI, the COMI choice can carry with it favorable treatment for particular stakeholders, or the ability to preserve private benefits for management. These benefits may be in the form of express distributional priorities, but they can also manifest in the form of procedural shortcuts that serve to lock-in or lock-up a desired result.⁹ For example, such procedural shortcuts were criticized in

⁷ As will be discussed below, the case law around COMI has not fulfilled this promise. Case law in the EU has focused on jurisdiction of registration, while in the US courts permit a wide variety of bases for exercising jurisdiction. See text at note ____.

⁸ John A.E. Pottow, *The Myth (and Realities) of Forum Shopping in Transnational Insolvency*, 32 *Brook. J. Int'l L.* 785 (2007).

⁹ The dangers of procedural shortcuts are discussed in Janger and Levitin, *Badges of Opportunism*, and Jacoby and Janger, *Ice Cube Bonds*. Of course, strategic behavior can also be used by holdouts to shift value distribution or just to disrupt. Janger and Levitin, *One Dollar, One Vote*.

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connection with the Chrysler and GM bankruptcies, where the deal to sell the companies specified distributions to secured creditors, and to trade unions that would have required additional procedural steps to implement under a plan of reorganization.¹⁰ The Supreme Court, in the US, expressed concern about such “end runs” around the procedural protections of the plan process in *Czyzanski v. Jevic Holding Corp.*¹¹ So, the centralization and consolidation of control envisioned by modified universalism can exacerbate the effects of jurisdictional competition, be they good, bad, or neutral.

For close to a decade, I have been promoting choice of law as a possible solution to this contradiction within modified universalism, both at the firm and at the group level.¹² I have called my approach “virtual territoriality” under which choice of forum should not affect distributional entitlements. Under virtual territoriality, the COMI court should apply ordinary choice of law principles to resolve disputes that affect a creditor’s substantial rights. A related term that has caught on is “synthetic treatment” under which distributional entitlements are calculated “as if” a local proceeding had been opened.¹³ The two are not identical, but they are linked. One cannot give meaning to the term “synthetic treatment” without calculating an entitlement baseline. This, in turn, requires a determination of law governing the claim, as well as the realizable value of the claim under “virtual territorial” treatment.

In the first part of this essay, I will explain how virtual territoriality limits the benefits of forum shopping, and thereby can work as a complement to COMI and comity. The key intuition of virtual territoriality is that there is an important distinction between forum shopping for procedure (including judicial and institutional capacity) which can be good, and

¹⁰ Mark J. Roe and David A. Skeel Jr., *Assessing the Chrysler Bankruptcy*, 108 Mich. L. Rev. 727 (2010)(available at: https://scholarship.law.upenn.edu/faculty_scholarship/685).

¹¹ 137 S.Ct. 973, 986 (2017)(“ The consequences are potentially serious. They include departure from the protections Congress granted particular classes of creditors.”). *See also, id.* at 985 (“Desire to make an end run around a statute,” does not constitute “cause.”)(quoting, *In re Sadler*, 935 F.2d 918, 921 (C.A.7 1991)).

¹² Edward J. Janger, *Virtual Territoriality*, 48 Colum. J. Transnat’l L. 401 (2010) [hereinafter Janger, *Virtual Territoriality*].

¹³ John A. E. Pottow, *A New Role for Secondary Proceedings in International Bankruptcies*, 46 Tex. Int’l L. J. 579 (2011).

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forum shopping for distributional advantage, which is bad. By neutralizing the substantive effect of a forum shop, virtual territoriality limits forum shopping and jurisdictional competition to matters of procedure.

For the US lawyer, I am advocating a global version of the framework articulated by Justice Brandeis in *Erie R.R. v. Tompkins*, under which federal courts apply their own procedural law, but defer to the common (and other substantive) law of the state where they sit (including choice of law). For the private international lawyer, I am suggesting that *Lex Fori* should be limited to the procedural aspects of bankruptcy law, and questions of substance (especially baseline distribution) should be governed by *Lex Situs*.

In the second part of this paper, however, I will give myself a black eye. It has always been obvious that the line between procedure and substance is not a clean one. But recent cases, both in the US and globally, have made it clear that there is a category of behavior that I cannot, in good faith, ignore: pernicious procedural competition. Both “modified,” and my proposed version of “modified modified” universalism need to address this concern, and neither COMI nor governing law is a sufficient solution.

The tentative solution I propose focuses on the discretionary aspect of cooperation—what I will call “recognition pushback.” Much of the framework of modified universalism, and of current law reform instruments has been to smooth the path toward recognition – limiting the bases for objection to recognition of proceedings and judgments. The UNCITRAL Model Law on Enterprise Groups, the EU Insolvency Regulation as recently recast, and the UNCITRAL Model Law on Insolvency Related Judgments all push in this direction. Jurisdictional competition for cases, in both its substantive and procedural form, creates the need for a more developed understanding of the appropriate reasons for a jurisdiction to push back by denying recognition.

Very tentatively, the principle that I suggest should guide the recognition inquiry is externality – be it jurisdictional, distributional, or both. Globally, a jurisdiction should not compete by extending the reach of its local

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distributional rules (or procedural rules with distributional implications), and, within the firm, a debtor should not be able to shift risk, costs, or distributional entitlements among claimants in a way that is inequitable. Jurisdictional externality creates an incentive for opportunistic case placing and distributional externality, when linked to control, can similarly be held out as a carrot to attract cross-border cases. Each can be viewed as a “badge of opportunism.”¹⁴ In short, a rule that creates interjurisdictional or intrafirm externality should be scrutinized to determine whether it serves an important value preserving bankruptcy purpose, or merely redistributes. This principle must focus on procedures as well as entitlements – policing the ability of claimants to participate in the case and obtain adequate information.

To be clear, the goal here is not to be “more territorial,” or “less universal,” but to ensure that the cross-border bankruptcy architecture has the tools to facilitate coordinated realization of enterprise value in a manner that assures both adequate process and equitable treatment.

This essay will proceed in four steps. First, it will explain and build a case for “Global *Erie*”: a cross border insolvency architecture that respects realizable territorial priority as an entitlement baseline but facilitates a procedurally universal global administration of the debtor. This section largely recaps previous work. Second, it will develop and explore the related problems of pernicious procedural competition, by looking at two U.S. examples: (1) *Purdue Pharma*; and (2) more generally the problem of third-party releases and quick sales. Third, it will develop the concept of recognition push-back and explore both the substantive and procedural reasons that might justify withholding recognition. The focus will be rules that create jurisdictional externality or undercut equitable allocation of value. Fourth, and finally, it will examine the MLEG and MLJ in this regard and identify a number of key features and a few bugs.

¹⁴ Edward J. Janger & Adam J. Levitin, *Badges of Opportunism: Principles for Policing Restructuring Support Agreements*, 13 Brook. J. Corp. Fin. & Com. L. (2018) (available at: <https://brooklynworks.brooklaw.edu/bjcfcl/vol13/iss1/8>). See also, Edward J. Janger & Adam Levitin, *The Proceduralist Inversion: A Response to Skeel*, 130 Yale L.J. Forum 335 (2020) (available at: https://www.yalelawjournal.org/pdf/JangerLevitinEssay_gmur71w9.pdf).

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I. *Global Erie*: A Governing Law Solution to Jurisdictional Competition?

A. Modified Universalism and the Market for Bankruptcy Cases

1. COMI and its limits.

Jurisdictional competition presents both a promise and a challenge for corporate and transactional law.¹⁵ In the market, jurisdictions seek to attract businesses to invest in local operations. In corporate law, jurisdictions compete for incorporations and the financial and legal business that they bring. Jurisdictional competition also influences state transactional law, most recently, for example, Wyoming seeking to become the venue of choice for “locating” digital assets.¹⁶ Finally, in bankruptcy, jurisdictions compete to be the forum of choice for global restructurings. The phenomena are interrelated, but the legal and institutional levers used by jurisdictions to compete in each of these areas are distinct. The common theme is that the jurisdiction seeks to appeal to the person or entity that controls the decision where to locate the business, transaction or case. Further, whether that competition is efficient and value creating or simply redistributive and even destructive is an empirical question. Corporate scholars have argued *ad infinitum* about whether Delaware’s aggressive pursuit of corporate registrations is a bug or a feature. The same is true in bankruptcy, where LoPucki has claimed that bankruptcy judges choose rules favored by the lawyers who control the decision to file. These include, for example, paying critical vendors, key employee “retention” plans, and debtor in possession financing orders that allow senior incumbent lenders to increase their recovery and maintain control of the case. Rasmussen, Skeel and others have debated LoPucki on whether this market for bankruptcy cases is beneficial or harmful, but all agree that the market exists.¹⁷

¹⁵ Corporate (Race to the Top/Bottom); LoPucki, *Courting Failure* (____)(bankruptcy); Janger, *Predicting When the Uniform Law Process Will Fail*, __ Iowa L. Rev. __ (1998)(commercial transactions)

¹⁶ <https://www.marketwatch.com/story/how-wyoming-became-the-promised-land-for-bitcoin-investors-11619201182>

¹⁷ Cites

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In cross-border bankruptcy cases, COMI is part of the solution to problematic forum shopping; but COMI is also part of the problem. The COMI concept seeks to regulate the market directly by limiting the debtor's choice of main forum to jurisdictions that could be characterized as the debtor's "home." The EUIR limits jurisdiction for the opening of a main case to the debtor's COMI. The MLCBI gives privileged status and commands deference to a main case pending at the debtor's COMI. But centralization, particularly when linked to a broad scope for *Lex Fori* increases the stakes associated with a COMI shop, and places pressure on the method of determining COMI.

To the extent that a debtor can choose or manipulate its COMI, centralization of the case increases the "advantage" a particular COMI can offer. So, the more power handed over to the forum, the more important it is that the COMI concept be robust, to ensure that the chosen forum is predictable, transparent, and related to the facts on the ground. The degree of tension between the power to coordinate the case and the danger of opportunistic case placement, thus depends, in large measure, on how COMI is determined: is it merely a formal designation, determined by jurisdiction of incorporation; or do courts require a more robust assessment of the debtor's operations, assets and nerve-center?

Under current law and practice, COMI has proven to be highly manipulable, while the EU and US have taken different approaches, debtors will generally have some flexibility in choosing the forum for their bankruptcy. In the EU, there is a strong presumption in favor of jurisdiction of registration as the basis for COMI,¹⁸ and this has led to the widespread practice of COMI shifting.¹⁹ To facilitate access to a common law jurisdiction, many EU debtors incorporate all of their subsidiary entities in the UK, regardless of the location of their operations, assets or nerve center.²⁰ US Courts, by contrast, have been somewhat more focused on the location of operations and decision making, at least where offshore letterbox registration is involved.²¹ However, within the US

¹⁸ Eurofood

¹⁹ [Anna Kaczor, Moving a company's COMI to achieve a restructuring: factors for consideration, 83 Amicus Curiae \(Autumn 2010\) at 13.](#)

²⁰ The future of this practice is uncertain after Brexit.

²¹ Baer Stearns, Sphinx, etc.

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itself, court shopping is virtually unfettered,²² and jurisdictions compete for large cases. So, at least where large global enterprises are involved, COMI appears to do little to limit a multinational debtor's ability to participate in the market for bankruptcy cases.

2. Corporate groups and the problem of multiple COMIs

Cases involving enterprise groups present an additional challenge to the concept of COMI as a safeguard against opportunistic jurisdictional competition. Corporate groups may be polycentric, or they may be operated as a consolidated enterprise. Entities, creditors, and operations may be centralized or scattered across the globe. Centralizing control of a global bankruptcy case in a single jurisdiction may be consistent with the expectations of some creditors (who dealt with the global enterprise), but it may defeat the expectations of creditors who dealt with a local entity. Further, governance of a global restructuring from a single jurisdiction may pose a threat to sovereignty.

Early cases under the EUIR sought to resolve this problem through the concept of a group COMI (sometimes called "enterprise COMI" or "e-COMI") located in the UK, but Continental jurisdictions rebelled.²³ Consequently, none of the current instruments recognize the concept of "group" or "enterprise" COMI. This creates a practical problem. Where enterprises are structured as groups, the subsidiaries are often structured along jurisdictional lines. Each member may have a different COMI. When this happens, the centralizing force of the MLCBI can turn centrifugal. The COMI of the group member may be in a different place than the gravitational center of the group, and local courts and local creditors may disagree about how to administer the case. Worse yet, group structure can lead to jurisdictional strategy and local creditor obstruction. Where subsidiaries have disparate COMIs, creditors of a group member can seek strategic advantage by threatening to open a costly and disruptive involuntary main proceeding for the subsidiary.

²² 28 U.S.C. 1408.

²³ Edward Klempka, *The Center of Main Interest and the Administration of *Daisytek**, 2004 *International Corporate Rescue* _____ (available at: <http://www.chasecambria.com/site/journal/article.php?id=77>).

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COMI, thus, does less under current law than it could to limit the market for bankruptcy cases, and, in group cases may operate as a barrier to rather than a tool of coordination. So the question is raised, should COMI be strengthened, relaxed, or abandoned. The answer depends on one's view of this particular market.

B. *Erie*: Substance/Procedure, Jurisdictional Externality, and Choice of Law.

Markets are not necessarily bad; indeed, they are generally thought to be good. They are also inevitable. So, in considering the market for bankruptcy cases, one must start by asking what we want that market to look like? What behaviors do we want the law to encourage and discourage? The market we are looking at is global, but the US experience within a federal system can be instructive. While global and federal jurisdictional competition are not identical, considering them together offers some important lessons.

In the US corporate law literature, Lucian Bebchuk has offered an insight that bears repeating (since he originally said it in 1992!). Bebchuk focuses on jurisdictional externality, asking: when does Delaware corporate law impose costs on the rest of the country? He then identifies two sources of externality one positive and one negative: legal rules that facilitate the allocation of private benefits to those with control over incorporation (substance), and laws that enhance market transparency (process). In the first group, he hypothesizes, a race to the bottom is likely. In the second, he argues, competition is more likely to lead to a race to the top.²⁴ Thus in the market for incorporations, the effect of the competition depends on the type of rule at stake.

This interrelationship between substance, process, jurisdictional externalization, and forum shopping has deep historical roots in the US

²⁴ Lucian Arye Bebchuk, *Federalism and the Corporation: The Desirable Limits on State Competition in Corporate Law*, 105 Harv. L. Rev. 1435 (1992). This is similar to the point made, even more forcefully, and pessimistically, by LoPucki in his book "Courting Failure" both about Delaware, and, for the purpose of this discussion, about modified universalism. Any local practice that benefits the "case placer" at the expense of other stakeholders, creates a risk of pernicious substantive jurisdictional competition. Lynn Lopucki, *Courting Failure* (2005). LoPucki does not see a beneficial side to competition.

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Federal Courts jurisprudence, where jurisdiction and venue must be allocated between local and national courts. Indeed, recognition of jurisdictional competition can be traced back at least to Justice Brandeis's opinion in *Erie Railroad v. Tompkins*, where he bemoaned forum shopping between state and federal courts based on differences between state and federal common law:

[T]he mischievous results of the doctrine [in *Swift v. Tyson*] had become apparent. Diversity of citizenship jurisdiction was conferred in order to prevent apprehended discrimination in state courts against those not citizens of the State. *Swift v. Tyson* introduced grave discrimination by noncitizens against citizens. It made rights enjoyed under the unwritten "general law" vary according to whether enforcement was sought in the state or in the federal court, and the privilege of selecting the court in which the right should be determined was conferred upon the noncitizen. Thus, the doctrine rendered impossible equal protection of the law.²⁵

By eliminating uniform federal common law as an option, state/federal forum shopping was substantially reduced.

But *Erie* was not just about litigation strategy. It was also intended to preserve the ability of states to regulate within their borders. Brandeis's jurisprudence had a powerful sense of the local, and the need for states to be able to experiment with their own policies on their own citizens. It was not lost on Brandeis that the states could only be the laboratories of democracy if local regulation could be kept local.²⁶

It is one of the happy incidents of the federal system that a single courageous state may, if its citizens choose, serve as a laboratory;

²⁵ *Erie Railroad Co. v. Tompkins*, 304 U.S. 64, 74-75 (1938). Cf. Edward J. Janger, Predicting When the Uniform Law Process Will Fail: Article 9, Capture and the Race to the Bottom, 83 Iowa Law Review 569 (1998) (Available at SSRN: <https://ssrn.com/abstract=158269>) (considering the effect of jurisdictional and intrafirm externality in connection with the drafting of the Uniform Commercial Code).

²⁶ *New State Ice Co. v. Liebmann*, 285 U.S. 262 (1932) (Brandeis J., dissenting).

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and try novel social and economic experiments *without risk to the rest of the country.*²⁷

The purpose of diversity jurisdiction was to protect against local bias in the forum, and *Erie* protected the states from federal overreach.

The benefit of the *Erie* framework was twofold. It preserved a policy space for the states and limited the geographic scope of those policies. States could continue to have jurisdiction and control over their own citizens, but should not be allowed to impose the costs of those choices on other states. Thus, the *Erie* vision had a second dimension, not just state/federal, but also state/state. The *Erie* case itself regulated the scope of *Lex Fori*, the effect of the choice of a federal forum, but this was just part of Brandeis's vision of federalism. State/federal forum shopping was one piece of the puzzle, but so was state/state externality, as businesses do not stay neatly within state (or national) borders.

This second piece of the *Erie* framework, the part that regulated state/state externality, was not implemented by the Supreme Court until 1941, shortly after Brandeis retired in 1939. In *Klaxon v. Stentor*,²⁸ the Supreme Court held that a federal court in Delaware, when exercising its diversity jurisdiction, should apply Delaware's choice of law rules in addition to its rules of substantive law. The court said:

We are of opinion that the prohibition declared in *Erie R. Co. v. Tompkins* ... against such independent determinations [of common law] by the federal courts, extends to the field of conflict of laws. The conflict of laws rules to be applied by the federal court in Delaware must conform to those prevailing in Delaware's state courts. Otherwise, the accident of diversity of citizenship would constantly disturb equal administration of justice in coordinate state and federal courts sitting side by side. See *Erie R. Co. v. Tompkins*, supra, at 74-77. Any other ruling would do violence to the principle of uniformity within a state, upon which the *Tompkins* decision is based. Whatever lack of uniformity this may produce between federal courts in different states is attributable to our federal

²⁷ *Id.* at 311 (emphasis added).

²⁸ *Klaxon Co. v. Stentor Elec. Mfg. Co.*, 313 U.S. 487 (1941).

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system, which leaves to a state, within the limits permitted by the Constitution, the right to pursue local policies diverging from those of its neighbors. It is not for the federal courts to thwart such local policies by enforcing an independent "general law" of conflict of laws. Subject only to review by this Court on any federal question that may arise, Delaware is free to determine whether a given matter is to be governed by the law of the forum or some other law. . . .²⁹

Thus, the *Erie* framework for determining applicable law within a federal system has two choice of law components: (1) *Lex Fori*; and (2) *Lex Situs*. The forum court applies its procedural law (*Lex Fori* governs) but applies the applicable state substantive law to the dispute, as determined using choice of law principles (*Lex Situs* governs). This framework has the dual effect of preventing federal judges from imposing federal common law on the states, but it also prevents states from utilizing the federal forum to export local law, which is what would have happened if choice of law had been excluded from the *Erie* framework.

C. Global *Erie*: “Virtual Territoriality”

Modified universalism and cross-border bankruptcy recapitulate the problem faced by Brandeis in *Erie*, on a global scale. For national or transnational enterprises, the power of a single jurisdiction to regulate and/or administer is essential, but it may carry with it the power to externalize favorable local rules.

This is the puzzle presented by modified universalism. Modified universalists seek to create a global architecture for the coordinated restructuring of cross-border enterprises, against the crazy quilt of local debt collection and insolvency laws. To the extent that a forum is exporting its local distributional or governance principles, it is imposing them on citizens of other jurisdictions. To the extent that a global bankruptcy architecture facilitates that export, it facilitates externalization and creates an incentive for jurisdictions to compete, and for debtors to shop. The *Erie* framework, however, suggests that choice of law can play a role in moderating the stakes and effect of jurisdictional competition.

²⁹ *Id.* at 496-97.

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Thus, one possible solution to externalization in cross-border bankruptcy cases is to globalize *Erie* as a choice of law framework.

In prior work, I have called this strategy “virtual territoriality.” Under virtual territoriality the procedural law of the bankruptcy forum governs, but not necessarily the substantive aspects of bankruptcy law. Virtual territoriality seeks to limit the scope of *lex fori* in in cross border bankruptcy cases to rules that facilitate coordination, enhance transparency, and limit the effect of territorial strategy. Governing law, for other issues, should be determined by ordinary choice of law principles – *lex situs*. As in *Klaxon v. Stentor*, the forum court should apply its own governing law principles of general application. The delegation to the private international law is, of course, not complete. As will be discussed below, the choice of governing law must be sufficiently plausible that it will not interfere with recognition. In this regard, the conflict of law rules will, and should generally be driven by the conflict of law principle, articulated by Brainerd Currie -- that a forum court should apply the substantive law of the jurisdiction with the greatest interest in the transaction.³⁰ To the extent that this principle is honored, choice of law will naturally operate to limit the extent of jurisdictional externality.

D. Virtual Territoriality v. Modified Universalism

Virtual territoriality relies on the substance/procedure distinction to determine governing law. *Lex Fori* governs procedures and leaves to ordinary choice of law principles (interest analysis and *lex situs*) the substantive and distributional principles that apply. This approach is not consistent with modified universalism, as defined and advocated by Westbrook.³¹ For Jay, choice of forum carries with it the forum jurisdiction’s entire bankruptcy law. As he puts it:

³⁰ Brainerd Currie, *Methods and Objectives in the Conflict of Laws*, in Brainerd Currie, *Selected Essays on Conflict of Laws* (1963).

³¹ Compare Edward J. Janger, *Silos: Establishing the Distributional Baseline In Cross-Border Bankruptcies*, 9 *Brook. J. Corp. Fin. & Com. L.* 180, 182–83 (2014) [hereinafter Janger, *Silos*]; See Also Edward J. Janger, *Universal Proceduralism*, 32 *Brook. J. Int’l L.* 819 (2007); Edward J. Janger, *Virtual Territoriality*, 48 *Colum. J. Transnat’l L.* 401 (2010) [hereinafter Janger, *Virtual Territoriality*]; Edward J. Janger, *Reciprocal Comity*, 46 *Tex. Int’l L.J.* 441 (2011) [Hereinafter Janger, *Reciprocal Comity*] with Jay Lawrence Westbrook, *A Comment on Universal Proceduralism*, 48 *Colum. J. Transnat’l L.* 503, 504 n.2 (2010) [hereinafter Westbrook, *A Comment*].

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The close integration among bankruptcy rules and policies in each jurisdiction applies to the big four of bankruptcy policy: control, priority, avoidance, and reorganization policy. In a system of universalism each of these four elements should be governed by the law of the main proceeding. Under modified universalism, such centralization should be the goal . . . ³²

By contrast, under the *Global Erie* approach, *lex fori* should be limited to the procedural elements of bankruptcy law, at least to the extent that such a distinction can be drawn. In other words, bankruptcy law should be divided for choice of law purposes between those rules that are procedural, and those that are distributive. Broadly speaking, this would place priority and avoidance on one side of the line, and reorganization and (possibly) governance on the other. As I will discuss below, however, the line may not be a straight one.

Westbrook's concerns with virtual territoriality are twofold. He argues, first, that the line between substance and process is not a meaningful one; and second, that seeking to locate claims and assets is a fool's errand.³³

On the first point, our disagreement is a matter of degree. There are certainly procedural rules that have substantive impact. However, there are a significant number of rules, regarding participation, notice, communication and decisionmaking that can be characterized as procedural, and are properly determined by the forum. There are also a number of rules that are clearly allocative – local priorities are certainly on this side of the line, avoidance as well.

Westbrook's second objection goes to priority. He argues that locating claims and assets is likely to be impossible. Here is where our disagreement is both fundamental (to us) but may be little practical importance. In most cases, the choice between modified universalism and virtual territoriality will make little difference. First, to the extent that the basic goals of private international law follow the principles of "interest" analysis, both

³² Jay Lawrence Westbrook, *Locating the Eye of the Financial Storm*, 32 *Brook. J. Int'l L.* 1019, 1021 (2007) (available at: <https://brooklynworks.brooklaw.edu/bjil/vol32/iss3/11>)

³³ Westbrook, *A Comment on Universal Proceduralism*.

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lex situs and *lex fori* will often point toward the forum court. This is particularly true if one follows Currie’s approach, where in cases of overlapping interest, or equal interest, the law chosen will be that of the forum.³⁴ Further, ordinary private international law, or *lex situs* already governs the enforceability and allowance of claims. This is the approach followed by both the EUIR and the UNCITRAL Legislative Guide on Insolvency.³⁵

Second, territorial entitlements can be respected without creating either inequity or opportunities for strategic behavior. The key is that the creditors entitlement baseline is established based on the realizable value of its priority claim.

Stephan Madaus and I have argued that in a case involving a single entity, the creditor who asserts a claim to priority based on the law of a foreign (non-forum) jurisdiction has the burden of establishing that the claim would be enforceable and could be satisfied in a proceeding opened in the relevant jurisdiction, using assets available for distribution in that proceeding.³⁶ The same principle applies when a subsidiary is involved, except that the priority is further limited by the assets that would be available to that group member. Stated in one sentence, we argue that *a stakeholder who claims priority should have the burden of establishing the realizable value of that claim in the absence of the global proceeding, otherwise it shares pro rata with other general claims.*³⁷

³⁴ Kermit Roosevelt III, Brainerd Currie’s Contribution to Choice-of-Law: Looking Back, Looking Forward, 65 Mercer L. Rev. 501 (2015); Currie, Methods and Objectives, *supra* note

³⁵ EUIR, Art. 7, UNCITRAL Legislative Guide on Insolvency, recommendations 30-34.

³⁶ Edward J. Janger and Stephan Madaus, *Value Tracing and Priority in Cross-Border Group Bankruptcies: Solving the Nortel Problem from the Bottom Up*, 27 U. Miami Int’l & Comp. L. Rev. 331 (2020).

³⁷ This principle is well stated in Principle 35 of [the ALI/III Principles of the Law: Transnational Insolvency](#): “A claim that is governed by the law of a state other than that in which insolvency proceedings are taking place should in principle have only the priority it would have in a strictly territorial process conducted in the state whose law governs the insolvency proceedings, and restricted to assets located in that state.” There are two important interpretive caveats here, however. Principle 35 can be read as setting the entitlement baseline at “the liquidation value” of the assets located in the secondary jurisdiction. It is possible that a territorial proceeding could realize going concern value, even in the absence of a global solution. Also, as discussed below, it is important to recognize that the burden of establishing a claim to realizable priority is on the claimant.

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The first implication of this principle is that any reorganization or coordination surplus created by the global proceeding is allocated to the general creditors. No extraordinary remedy, like substantive consolidation is required to accomplish this. While this approach may limit the procedural rights of some creditors to obstruct a coordinated solution, the approach still belongs on the procedural side of the ledger, as it gives the creditor at least what they would have received had they opened a territorial proceeding.³⁸ As such, the practical difference between modified universalism and modified universalism plus virtual territoriality ends up being relatively small, at least where claims of priority are involved.

The comparison case is *Nortel*.³⁹ In that case, Jay thinks that the court reached the appropriate result because there was a showing that the enterprise was highly integrated, and the subsidiaries were unable to prove ownership.⁴⁰ Madaus and I agree with Westbrook that the court reached the right result, but we think that the same conclusion could have been reached, with considerably less expense and drama if the allocation had started from the bottom up, requiring the claimants to prove a realizable entitlement, rather than requiring a threshold determination that the enterprise was operated on an integrated basis. In other words, placing the burden of going forward on the claimant, rather than the estate would have emphasized the failure of proof, rather than the need for a showing of integration. Taken together, *Global Erie* and realizable priority both respect local priorities, ownership and the corporate form, but limit their strategic use.

The idea of global *Erie* has been catching on. In the *Collins and Aikman* bankruptcy, UK courts had found a way to torture the EUIR to allow a UK court to recognize local priorities, without requiring the foreign creditors to open secondary proceedings.⁴¹ *Collins and Aikman* gave rise to the idea that a bankruptcy administrator might commit to recognize

³⁸ Edward J. Janger and Stephan Madaus, *Value Tracing and Priority in Cross-Border Group Bankruptcies: Solving the Nortel Problem from the Bottom Up*, 27 U. Miami Int'l & Comp. L. Rev. 331 (2020).

³⁹ *In re Nortel Networks, Inc.*, 532 B.R. 494 (Bankr. D. Del. 2015).

⁴⁰ See Jay Lawrence Westbrook, *Corporate Formalism in a Global Economy*, in Janis Sarra, Annual Survey of Insolvency Law 311 (Vancouver 2015).

⁴¹ *In re Collins & Aikman Eur. S.A.*, [2006] EWHC (Ch) 1343 (Eng.).

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local priorities to prevent the opening of a costly and disruptive secondary proceeding. This has been called “synthetic” or “as if” treatment, and it has been ratified EUIR as recently recast. The EUIR now expressly authorizes the insolvency administrator to grant an undertaking to recognize local priorities.⁴² Most recently, UNCITRAL has promulgated a Model Law for the Insolvency of Enterprise Groups, which provides for the recognizing of local priorities to avoid the necessity of opening a non-main proceeding.⁴³

Unfortunately, it is too early to proclaim the success of the “Global *Erie*” approach. Jurisdictional competition continues apace, and there are some potential problems with the practice of “undertaking” to respect local priority. These issues will be discussed below.

II. The Market for Control: Pernicious Procedural Competition

In this section, I give myself a black eye. As mentioned above, Westbrook has criticized virtual territoriality based on the inability to distinguish substance from process. While the distinction has meaning, I must concede that, at the margin, it breaks down, and perhaps catastrophically so.

The goal of virtual territoriality and “Global *Erie*,” was not to completely eliminate forum shopping, but instead to limit its scope to shopping on the “procedural” side of the ledger. Complemented by COMI, the assumption was that jurisdictions would compete to provide “better” procedures, that enhanced the ability of firms to maximize their value for the benefit of stakeholders. It is not hard to identify examples of procedural forum shopping and many of them do seem beneficial. For example, common law jurisdictions, such as the US, the UK and other Commonwealth countries have become the restructuring destinations of choice. Indeed, it is generally assumed that only a common law court and common law judges will have the flexibility accomplish a complex

⁴² EUIR Articles 35 and 36 (<https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:32015R0848&rid=7#d1e1963-19-1>).

⁴³ UNCITRAL Model Law on Enterprise Group Insolvency, Articles 28-32 (https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/19-11346_mloegi.pdf).

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restructuring. *Collins and Aikman* mentioned above, is often flagged as a triumph of English pragmatism.⁴⁴

Unfortunately, this pragmatism and flexibility has a dark side as well. The assumption that procedural forum shopping is benign did not consider procedures that could be used to drive a wedge between value maximization and equitable distribution of that value. As LoPucki points out in *Courting Failure*, the willingness of Delaware bankruptcy courts to accommodate prepackaged bankruptcies through accelerated timelines and other shortcuts, drew cases, but also may have meant that the firms did not shed sufficient debt and were left with a greater probability of refiling.⁴⁵

Worse yet, the flexibility of common law courts in the US frequently manifests as a willingness to accept procedural shortcuts in the ostensible service of value maximization. This often manifests as the debtor and a dominant creditor or creditors joining together to strong-arm a particular outcome.⁴⁶ Indeed, procedural competition often appears to be largely about maintaining debtor control at the expense of participation, transparency and equitable distribution of value. Here are some examples.

All-asset going concern sales outside the context of a plan of reorganization provide one example. They have become a relatively common feature of US Chapter 11 practice, in both US and global cases.⁴⁷ The speed is a feature that may, in appropriate cases, minimize disruption to the business. Unfortunately, the speed also shortcuts the negotiation, disclosure and voting process that Chapter 11 envisions. This can have significant distributional impact, either allocating all the enterprise value to secured creditors, or even, as in cases like Chrysler, dictating particular

⁴⁴ Gabriel Moss QC, *Group Insolvency - Choice of Forum and Law: The European Experience Under the Influence of English Pragmatism*, 32 Brook. J. Int'l L. (2007) (Available at: <https://brooklynworks.brooklaw.edu/bjil/vol32/iss3/10>).

⁴⁵ LoPucki, Recidivism; LoPucki and Doherty, Fire Sales; [Edward I. Altman, Revisiting the Recidivism – Chapter 22 Phenomenon in the US Bankruptcy System](#), 8 Brook. J. Corp. Fin. & Com. L. (2014).

⁴⁶ Adam J. Levitin, *Purdue's Poison Pill: The Breakdown of Chapter 11's Checks and Balances* 100 Texas Law Review __ (forthcoming, 2021)(Available at SSRN: <https://ssrn.com/abstract=3851339> or <http://dx.doi.org/10.2139/ssrn.3851339>).

⁴⁷ Melissa B. Jacoby and Edward J. Janger, *Ice Cube Bonds: Allocating the Price of Process in Chapter 11 Bankruptcy*, 123 YALE L.J. 862 (2014).

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distributions without subjecting them to the protections of the plan process.⁴⁸

Indeed, the most egregious recent example of a procedural forum shop may be *Purdue Pharma*.⁴⁹ Purdue manufactured opiates, and a significant element of the case involves determining the liability of the Sackler family that owned the company. They are reported to have received billions of dollars in dividends, and the Purdue estate had large potential claims against them. Accordingly, third party releases were obviously going to be an important feature of the case. For example, the willingness of courts to grant non-consensual third-party releases has been controversial, and courts in the US are divided. Several circuits prohibit them outright.⁵⁰ The majority permits them under limited circumstances, and the tests vary widely.⁵¹ Indeed, even within the SDNY, the level of receptiveness appears to vary amongst the bankruptcy judges.

Meanwhile, the company was headquartered in Stamford Connecticut with offices in Manhattan. Curiously it filed in White Plains, using leased office space as its address for service. The reason for this was not a secret. Under the local rules of the Southern District, this meant that the case would go to Judge Bob Drain, who was known to be receptive to the grant of non-consensual third-party releases.⁵² The case is ongoing, and the price of releasing the Sacklers remains front and center.⁵³

⁴⁸ *Id.* See also, Mark J. Roe and David A. Skeel Jr., Assessing the Chrysler Bankruptcy, 108 Mich. L. Rev. 727 (2010)(available at: https://scholarship.law.upenn.edu/faculty_scholarship/685).

⁴⁹ Adam J. Levitin, *Purdue's Poison Pill: The Breakdown of Chapter 11's Checks and Balances*, 100 TEXAS L. REV. __ (forthcoming 2021).

⁵⁰ See *Bank of N.Y. Trust Co. v. Official Unsecured Creditors' Comm. (In re Pac. Lumber Co.)*, 584 F.3d 229 (5th Cir. 2009); *In re Lowenschuss*, 67 F.3d 1394 (9th Cir. 1995); *In re W. Real Estate Fund, Inc.*, 922 F.2d 592 (10th Cir. 1990); see also *Zacarias v. Stanford International Bank Ltd.*, 945 F.3d 883 (5th Cir. 2019) (third parties making substantial contributions to the receiver in the R. Allen Stanford Ponzi scheme are entitled to an order barring creditors from suing on the creditors' claims), *petition for rehearing en banc denied*, No. 17-11073 (5th Cir. Jan. 21, 2020).

⁵¹ See *In re Drexel Burnham Lambert Grp., Inc.*, 960 F.2d 285 (2d Cir. 1992); *In re A.H. Robins Co., Inc.*, 880 F.2d 694 (4th Cir. 1989); *In re Dow Corning Corp.*, 280 F.3d 648 (6th Cir. 2002); *In re Airadigm Commc'ns, Inc.*, 519 F.3d 640 (7th Cir. 2008); *SE Prop. Holdings, LLC v. Seaside Eng'g & Surveying, Inc. (In re Seaside Eng'g & Surveying, Inc.)*, 780 F.3d 1070 (11th Cir. 2015).

⁵² Lindsey Simon, Bankruptcy Grifters, __ Yale L.J. __ (forthcoming 2021)(https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3817530).

⁵³ <https://twitter.com/melissabjacoby/status/1400465224017203210?s=20>

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Another example of procedural forum shopping is global, but also involves third-party releases. Both UK and Canadian courts grant non-consensual third-party releases of officers and directors as a routine matter. Recent cases out of the SDNY have reflected a willingness to enforce these non-consensual third-party releases, even where they might not have been granted under US law. Judge Glenn has granted comity to third party releases granted in Canadian cases⁵⁴ and UK schemes of arrangement.⁵⁵ This creates the possibility, in an international case for a debtor to shop abroad for relief, and then bring it home in the hope that the US Court will extend comity to the foreign judgment. Cases like these suggest that the principles of *Global Erie* may not go far enough. Local courts may need to pay close attention to the procedural aspects of the case to ensure that procedural shortcuts do not become substantive levers in the market for bankruptcy.

The UK has taken a more restrictive approach to procedural arbitration than the US. In *Singularis*, the Privy Council took the view that a Bermuda court could not grant assistance that would not have been available in the jurisdiction where the case was opened, in this case the Cayman Islands.⁵⁶ This means that a debtor cannot open a case, and then travel abroad in seek of broader relief. This is the opposite of the US, which would grant assistance and extend comity to a foreign case in forms potentially unavailable in the US. The Privy Council has, thus, through *Singularis* apparently erected a barrier to procedural arbitration, limiting the ability of a jurisdiction to export the effects of its procedural rules. Whether this is a good or a bad rule is a difficult question.⁵⁷ UNCITRAL attempted to address the *Singularis* case in the MLJ, and no consensus was reached.⁵⁸

⁵⁴ *In re Metcalfe & Mansfield Alternative Investments*, 421 B.R. 685 (Bankr. S.D.N.Y. 2010); *Sino-Forest Corp.*, 501 B.R. 655 (Bankr. S.D.N.Y. 2013).

⁵⁵ *In re Avanti Commc'ns Grp. PLC*, 582 B.R. 603 (Bankr. S.D.N.Y. 2018).

⁵⁶ <https://www.jcpc.uk/cases/docs/jcpc-2014-0040-judgment.pdf>.

⁵⁷ It is even ambiguous whether this rule will discourage or encourage procedural forum shopping. For complicated reasons, it, along with the rule in *Gibbs, Anthony Gibbs and Sons v La Société Industrielle et Commerciale des Métaux*, (1890) 25 QBD 399, may actually be further evidence of competition, forcing debtors with UK denominated debt to file in the UK.

⁵⁸ Article 15(1) offers alternate language that can be adopted depending on the enacting jurisdiction's view of the *Singularis* rule.

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The lessons of this section are complicated. First, it illustrates the limits of the procedure/substance distinction as a method for sorting between appropriate and inappropriate jurisdictional competition. Jurisdictions will compete on procedure, perhaps even more aggressively than distribution. Or to put it another way, the manner through which distributional distortions are implemented is often through procedural shortcuts, rather than application of foreign distributional law. Second, if procedural competition is part of the problem, then it is essential to develop principles for either identifying problematic practices, or to limit their effects.

III. Recognition Pushback: Limiting Jurisdictional Externality and Distributional Inequity

So, if *Global Erie*, and choice of law, are only imperfect checks on externalization and the other pernicious effects of the market for chapter 11 cases, and if procedural shortcuts that lock in a desired result are a major lever in that competition, the question becomes, how to address this? The answer lies in an important structural feature of modified universalism – recognition itself. The general thrust of the MLCBI, and even more importantly, the MLEG and MLJ is to facilitate cooperation and recognition. But modified universalism is based in comity, rather than *lex fori*. It is axiomatic that the court being asked for recognition and assistance should defer, out of respect, but it is also axiomatic that the receiving court can and should consider whether such deference is appropriate.

A. Comity and its Limits

The common law principle of universalism articulated in *Cambridge Gas*, that, “There should be a single bankruptcy in which all creditors are entitled and required to prove,”⁵⁹ is implemented in the MLCBI through the principle of comity. Comity is based in the mutual respects courts and sovereigns extend to each other.⁶⁰ The classic phrase from *Hilton v. Guyot* bears repeating:

⁵⁹ *Cambridge Gas Transp. Corp. v Official Comm. of Unsecured Creditors of Navigator Holdings PLC*, [2007] 1 A.C. 508, at para. 16.

⁶⁰ MLCBI Arts, 7, 19-21.

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No law has any effect, of its own force, beyond the limits of the sovereignty from which its authority is derived. The extent to which the law of one nation, as put in force within its territory, whether by executive order, by legislative act, or by judicial decree, shall be allowed to operate within the dominion of another nation, depends upon what our greatest jurists have been content to call 'the comity of nations.' Although the phrase has been often criticised, no satisfactory substitute has been suggested. 'Comity,' in the legal sense, is neither a matter of absolute obligation, on the one hand, nor of mere courtesy and good will, upon the other. But it is the recognition which one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citizens, or of other persons who are under the protection of its laws.⁶¹

Comity is, however, subject to limits. The MLCBI focuses on facilitating comity and does everything it can to make recognition of proceedings automatic. It also makes certain basic procedural remedies automatic, where the proceeding being recognized is a main case. In particular, the creation of a territorial estate and stay are automatic.⁶²

However, when the relief is more tailored, such as approving the sale of assets, recognizing an insolvency related judgment, approving a plan of reorganization, or making a distribution, recognition is subject to the requirement of adequate protection.⁶³ Article 22 provides:

In granting or denying relief under article 19 or 21, or in modifying or terminating relief under paragraph 3 of this article, the court must be satisfied that the interests of the creditors and other interested persons, including the debtor, are adequately protected.

Adequate protection carries with it both a procedural and a substantive component. It gives the receiving jurisdiction a second look at the

⁶¹ *Hilton v. Guyot*, 159 U.S. 113, 143 (1895)

⁶² 11 U.S.C. 1520.

⁶³ 15 U.S.C. 1521, 1522.

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requested relief, and an opportunity to consider whether the process has been adequate and whether the treatment satisfies the entitlement baseline.

Crucially, while judges and debtors who are seeking to get a case past the finish line may find it nerve wracking to think that their efforts may be blocked by a jurisdiction whose assistance is needed, in a world where competition may be both procedural and substantive the concept of “adequate protection” provides a necessary check to pernicious competition. The hard question is, how to give appropriate, but not excessive, bite to this second look. What are the appropriate bases for denying or limiting cooperation in a global restructuring case?

The answer is twofold; adequate protection incorporates principles of both due process and distributional equity. As noted above, the receiving court should be permitted to consider whether the procedural rights of local creditors were safeguarded through rights of participation. It might be appropriate to deny recognition if it appears that a jurisdiction being chosen because its procedures facilitate control by a particular creditor constituency, limit transparency, participation, and voice in the formulation of the plan? Finally, if the procedure affects distribution, the court should be permitted to consider whether the proposed distribution exceeds the realizable value of the claim in a purely local proceeding, but also whether it distributes reorganization surplus equitably.

B. The Limits of Control: Jurisdictional Externality, Distributional Equity, and Badges of Procedural Opportunism

Modified universalism seeks to facilitate debtor control of the case from the debtor’s COMI. This presumptive extension of recognition based on comity increases the control available to the debtor and the key proponents of a global insolvency solution. Mostly, this is a good thing, particularly where one is trying to preserve the going concern value of a business enterprise. However, in Chapter 11 practice, control is a double edged sword. In prior work with Melissa Jacoby, I have explored how an all asset going concern sale outside a plan of reorganization can operate as a “lockup” agreement and *sub rosa* plan that allows a stalking horse bidder, the debtor and senior creditors to control the sale process determine

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distributions and short circuit the plan process. Similarly, Adam Levitin and I have explored the use of restructuring support agreements to distort both distributions and the voting process under Chapter 11. In both of these contexts, we pointed out how creditors and the debtor can use “situational leverage” created by the debtor’s financial distress opportunistically to distort the distributional scheme.

The sine qua non of modified universalism is control situated at the COMI. Control of a global case carries with it the ability to expand the scope of relief to other jurisdictions through recognition. The goal of the cross-border insolvency regime is to capture the positive externality of coordinated liquidation or rescue, but as with any rescue regime, this should not come at the expense of jurisdictional inequity or other distributional reallocation. So, the question becomes, when is control being used opportunistically? What are the “badges” of an opportunistic COMI choice. In the MLCBI, the concept of “adequate protection” polices the limits of COMI. So, the question becomes, how does one give meaning to the concept of “adequate protection?”

The answer is twofold, and must have a distributional and a procedural component.

- On the distributional side, adequate protection requires attention to the local distributional scheme and the resulting entitlement baseline. A claimant should have a basis to object to recognition if it can show that the distribution it is receiving is less than the realizable value of its claim using local process. It further requires equitable distribution of the reorganization/coordination surplus through either a pro-rata default, or an adequate process (see next).
- On the procedural side, adequate protection requires that claimants who are bound by the outcome receive (1) an opportunity to prove up their baseline entitlement; (2) that any surplus be distributed through a process that provides adequate information and an opportunity for voice.

In other words, receiving jurisdictions should be able to cross-examine relief that (1) uses situational leverage and control to distort the distributional scheme; and (2) utilizes situational leverage to shortcut

procedural protections. Since comity is the standard rather than strict symmetry with local process, the “adequate protection” inquiry ought to be conducted pragmatically, and with some play in the joints. However, local courts should be alert to what Adam Levitin and I have called “badges of opportunism.”⁶⁴ We explored and identified such badges in the context of restructuring support agreements, but the concerns are similar for recognition of aspects of a global restructuring. The common hallmark is an attempt to use situational leverage (the promise of a global restructuring) as an opportunity to reallocate value or undercut the ability of claimants to participate adequately in the process.

C. A Note on Groups

As noted above, some special rules may be necessary when the debtor is a member of a corporate group. If the COMI of the group member is not the source of the group solution, principles of deference would seem to point in the opposite direction. As such, the presumption of recognition, and hence of “adequate protection,” might be relaxed in these cases. However, the same principles described above apply, and should be applied with the goal of maximizing the value as well as limiting the effect of local/territorial obstruction. This point is discussed below in connection with the MLEG.

D. The Presumption of Recognition

In considering the possibility of recognition pushback, it is crucial that the scrutiny of relief in the receiving jurisdiction not become an obstacle to coordination. Opportunism is a two way street. Debtor control and centralization can be used opportunistically. However, local creditors can also use fights over recognition opportunistically. In this regard, it is crucial to recognize that the principal goal of the MLCBI, MLEG and MLIJ is to encourage comity. As such, the badges of opportunism describe reasons for non-recognition, but they also define its boundaries.

⁶⁴ Edward J. Janger & Adam J. Levitin, *Badges of Opportunism: Principles for Policing Restructuring Support Agreements*, 13 Brook. J. Corp. Fin. & Com. L. (2018) (available at: <https://brooklynworks.brooklaw.edu/bjcfcl/vol13/iss1/8>). See also, Edward J. Janger & Adam Levitin, *The Proceduralist Inversion: A Response to Skeel*, 130 Yale L.J. Forum 335 (2020) (available at: https://www.yalelawjournal.org/pdf/JangerLevitinEssay_gmur71w9.pdf).

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In the absence of badges of opportunism, the receiving jurisdiction should assist in the implementation of the group insolvency solution, and look askance at local creditors, who participated in the formulation of the group solution, and who are seeking a second bite at the apple.

IV. Evaluation of the MLEG and MLJ

The main takeaway from this essay is the somewhat disappointing realization that *Global Erie* is insufficient, in and of itself to check the detrimental effects of jurisdictional competition for bankruptcy cases. It needs the disciplining effect of possible non-recognition. More optimistically, it has sought to articulate the legitimate bases for non-recognition, in the hope that such decisions will be principled, not just pragmatic or localist. The key feature is a robust concept of “adequate protection” that protects due process and equitable allocation by scrutinizing relief that bears the “badges of opportunism”: seeking to reorganize the distributional scheme or shortcut procedural protections. With this insight in mind, we should evaluate the proposed MLEG and MLJ, to consider their effect on this competition.

Both are designed to facilitate the central coordination of bankruptcy cases. The MLEG facilitates the crafting and recognition of a group solution through the creation of a planning proceeding. The MLJ facilitates the recognition of insolvency related judgments. In this regard, they both increase the possible beneficial effects of centralization. The question is whether they adequately address the possibility of opportunism.

A. MLEG

The MLEG addresses the fact that the MLCBI deals only with single companies. Corporate groups require extra tools to achieve a coordinated resolution. The MLEG allows the various members of a corporate group to designate as a “planning proceeding”⁶⁵ and to elect a “group representative”⁶⁶ to act on behalf of the group in proceedings opened for

⁶⁵ MLEG Articles 2(g), 19.

⁶⁶ MLEG Article 19

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the various group members. The planning proceeding may only be opened in a jurisdiction that is the COMI of an essential group member.⁶⁷ The planning proceeding then acts as a forum for formulating a “group insolvency solution” -- a “plan” for the group.⁶⁸ It is then contemplated that the group representative would seek recognition of that solution for the various group members in the relevant jurisdictions.⁶⁹

A central drafting tenet of the MLEG was that it should facilitate “procedural” coordination and should not alter substantive outcomes.⁷⁰ Since it is envisioned that it would accompany the MLCBI, Article 22 remains in place, and the MLEG additionally contains its own Article 27, that further conditions relief to the planning proceeding on adequate protection of group members and their creditors. In all of these respects, the MLEG furthers the principles of recognition described above.

Further, the MLEG contemplates that the group insolvency solution would follow the principles of *Global Erie* – respecting the realizable value of local entitlements. This is implemented through two provisions. First, under Article 26, the receiving jurisdiction has the opportunity to approve the group insolvency solution. Second Article 28 (and its optional sibling Article 30) authorize synthetic (local) treatment of creditors. This expressly authorizes the planning proceeding to implement global *Erie*. Article 28 provides:

a claim that could be brought by a creditor of an enterprise group member in a non-main proceeding in another State may be treated in a main proceeding commenced in this State in accordance with the treatment it would be accorded in the non-main proceeding, provided:

- (a) An undertaking to accord such treatment is given by the insolvency representative appointed in the main proceeding in this State. Where a group representative is appointed, the undertaking should be given jointly by the insolvency representative and the group representative;

⁶⁷ MLEG Article 2(g).

⁶⁸ MLEG Article 2(f).

⁶⁹ MLEG Article 26.

⁷⁰ Cite to discussion in MLEG commentary.

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What is envisioned by this section is that the administrator in the planning proceeding would assure the local creditors of a group member that their claims would receive the same treatment that they would receive if a local proceeding was opened. The hope is that by doing this, the opening of that proceeding will be avoided.

The puzzle lies in how the phrase “treatment it would be accorded” should be interpreted. For example, should a priority wage claim applicable in Jurisdiction X be given that same priority against claims of creditor in Jurisdiction Y, who are given a lower priority in Jurisdiction Y? Or should the priority wage claim be entitled only to the value that would be realizable if a proceeding was opened in Jurisdiction X and the creditor were to seek to realize value locally.

The concept of realizable priority developed above, would suggest that the realizable value, not the formal priority, should be the measure.

A second concern is that the undertaking described in Article 28 will generally be made at an early stage in the restructuring. It may be that, to prevent the opening of a local proceeding, the group representative may be tempted to offer a fixed payment, perhaps even payment in full. This sort of undertaking should be prohibited. Instead, the undertaking should only be a promise of local treatment, with the amount to be determined as part of the group solution. Further, while Article 28 is modeled on the recast EU IR and is intended to implement a version of *Global Erie*, it is important that it be interpreted in the light of realizable priority.

B. MLJ

The Model Law on Insolvency Related Judgments is tremendously important in two regards. Article X of that law operates to reverse the problematic decision in *Rubin v. Eurofinance*⁷¹ and reinstates a discretionary basis for recognizing insolvency related judgments subject to Article 22 of

⁷¹ *Rubin v. Eurofinance SA* [2010] UKSC 46[6]–[10] (Eng.) (holding that avoidance orders made in insolvency proceedings by foreign court will not be enforced in the UK unless the defendant was present in the foreign country when the proceedings were commenced or submitted to the foreign court's jurisdiction)

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the Model Law. Other provisions of the MLJ seek to limit that discretion and may end up in tension with the MLCBI. The key provision in ensuring that this does not happen is Article 14(f), which permits non-recognition if:

- (f) The judgment:
 - (i) Materially affects the rights of creditors generally, such as determining whether a plan of reorganization or liquidation should be confirmed, a discharge of the debtor or of debts should be granted or a voluntary or out-of-court restructuring agreement should be approved; and
 - (ii) The interests of creditors and other interested persons, including the debtor, were not adequately protected in the proceeding in which the judgment was issued;

This provision incorporates the concept of “adequate protection” embodied in Article 22 of the MLCBI and Article 27 of the MLEG. However, its scope is substantially limited by the fact that it does not come into play unless it “materially affects the rights of creditors generally.” How this limitation interacts with Article 22 is unclear, and like any inconsistency may lead creditors or debtors to seek to arbitrage the difference.

Finally, we return to *Singularis*, the MLJ attempts to address *Singularis* in Article 15 (Equivalent Effect) is the result, and it’s a mess. It provides:

1. An insolvency-related judgment recognized or enforceable under this Law shall be given the same effect it [has in the originating State] or [would have had if it had been issued by a court of this State].
2. If the insolvency-related judgment provides for relief that is not available under the law of this State, that relief shall, to the extent

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possible, be adapted to relief that is equivalent to, but does not exceed, its effects under the law of the originating State.

Subsection 1 addresses the *Singularis* problem, and it offers alternative language. One of which reflects the *Singularis* holding, and the other which represents the precise opposite. The problem with this section is that it reflects an insoluble problem. *Singularis* would prevent procedural arbitrage. But as we have discussed above, not all procedural competition and not all procedural arbitrage is bad. The problem is figuring out how to articulate a principle for deciding which is which.

Conclusion

This project – *Global Erie* -- began as an attempt to use governing law and the substance/procedure distinction as a device for curbing the problematic effects of jurisdictional competition. The project ultimately founders on the fact that much of the market for cases appears to turn on and be driven by a market for procedural shortcuts. Governing law is not sufficient to solve this problem, so it is necessary to turn to the disciplining effect of discretionary recognition to allow the overhanging threat of non-recognition to limit the extent to which jurisdictions will be able to engage in opportunistic behavior to attract cases. On the one hand, this has a substantive component – respect of the realizable entitlement baseline, but it also has a procedural component, and this concept requires further development. It is important, however, that the possibility of recognition pushback not unduly hamper the overarching goal of coordination. As such, there should be a strong presumption in favor of recognition, unless the relief sought bears the so-called “badges of opportunism” described above.