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## Getting More out of Your “Stay” in the United States: *Brazilian Insolvency and the Investigative Powers of Chapter 15*

### David L. Lawton & David K. Shim, Morgan, Lewis & Bockius LLP

Cross-border insolvency practitioners the world over may know that chapter 15 of the U.S. Bankruptcy Code allows a foreign representative to seek recognition of a non-U.S. insolvency proceeding and, upon recognition, to benefit from an automatic stay of execution against the debtor’s assets “within the territorial jurisdiction of the United States.”<sup>1</sup> The court may implement additional measures to protect such assets, including:

- Entrusting a foreign representative with the administration of some or all of the debtor’s assets;<sup>2</sup>
- Suspending the right to transfer, encumber, or otherwise dispose of any of the debtor’s assets;<sup>3</sup> and
- Granting additional relief available to a trustee, apart from avoidance powers.<sup>4</sup>

However, some insolvency practitioners may not realize the full scope of additional tools available not only to protect the debtor’s identifiable U.S. assets—but also to trace and recover additional assets in the United States through the investigative powers of 11 U.S.C. § 1521(a)(4). Several recent cases highlight the potential value of obtaining broad discovery powers in the United States through chapter 15 recognition.

### Protecting Property in the United States

During the last six months, there has been an increase in the number of petitions for recognition of Brazilian insolvency proceedings under chapter 15. Among these and other cases, the foreign representative often seeks the most common relief: a stay of any action or proceeding against the debtors’ assets—no matter how briefly such property remains in the United States. For example, the UST Group, one of the largest sugar and ethanol producers in Brazil, suffered in recent years from sugar price volatility, price controls on retail fuel sales, and the depreciation of the Brazilian real. In *Usina De Açúcar Santa Terezinha Ltda.*,<sup>5</sup> after failed attempts to restructure its debts out of court, the UST Group commenced *recuperação* judicial proceedings in Brazil and filed a chapter 15 petition seeking recognition of the proceedings in the United States. Specifically, the foreign administrator sought to protect payments from export contracts that passed through deposit accounts in the United States en route to Brazil. The foreign representative moved for—and the bankruptcy court granted—a pre-recognition stay of enforcement on the debtor’s assets in the United States, including such deposits held temporarily in U.S. bank accounts.

### Recovering Assets in the United States – Investigative Powers

Whereas *Usina De Açúcar* likely represents the more common use of chapter 15—to protect identifiable assets in the United States, section 1521(a)(4) of the Bankruptcy Code entitles the foreign representative

to request authority to compel broad discovery from any person “concerning the debtor’s assets, affairs, rights, obligations or liabilities.” The following three recent Brazilian cases demonstrate the utility of such broad investigative powers—not merely for protecting assets—but for tracing and recovering potential assets in the United States and abroad.

In *Schahin Holdings SA et al.*,<sup>6</sup> the foreign representative used the discovery powers of section 1521(a)(4) to expand the scope of investigations already underway in Brazil. Schahin and its affiliates had collaborated with Petrobras, a Brazilian state-controlled oil company and the subject of much controversy. Largely driven by economic and political uncertainty, the Schahin group struggled to remain current on \$1.8 billion of debt and subsequently commenced a *recuperação judicial* proceeding in Brazil. Moreover, like other companies conducting business with Petrobras, the Federal Police of Brazil targeted the Schahin group in its ongoing anti-corruption investigation, *Operação Lava Jato* (Operation Car Wash). Based on records implicating Schahin and its controlling stakeholders with the Petrobras scandal (including fraud, bribery, and the use of U.S., Austrian, Bahamian and other offshore companies to conceal assets), Schahin’s foreign representative sought and obtained chapter 15 recognition to expand investigations of the debtors’ affairs in the United States as part of its efforts to recover concealed assets.

In *Knijnik Participações S.A.*,<sup>7</sup> the foreign representative from Brazil likewise sought recognition under chapter 15 for access to the broad investigative powers available under section 1521(a)(4). Knijnik and its affiliates provide engineering services and project management for major architectural and construction projects in Brazil. After commencing *recuperação judicial* proceedings, the administrator asserted that the debtors’ controlling shareholders had mismanaged the debtors’ finances and may have misappropriated the debtors’ assets. By obtaining recognition of the Brazilian proceedings, the foreign representative was able to commence broad discovery in an attempt to uncover additional assets transferred to the debtors’ former shareholders and their affiliates in the United States.

In *São Fernando Açúcar e Álcool Ltda.*,<sup>8</sup> the foreign representative used section 1521(a)(4) in an attempt to expand investigations in a Brazilian fraud action to recover property that may have been illegally diverted to the United States. São Fernando and its affiliates operated an industrial ethanol plant in Brazil. Attempts to restructure the group’s debt in a court-supervised reorganization proceeding failed, and the Brazilian court ordered liquidation of the group and seizure of the two shareholders’ assets as a precautionary measure based on allegations that the shareholders had engaged in fraudulent activity. At the same time, Brazilian authorities took action against the São Fernando shareholders for fraud, which resulted in a second seizure order against the shareholders. Based on those records, the foreign representative obtained recognition of the liquidation proceedings under chapter 15 to investigate the debtors’ affairs in the United States, asserting that the shareholders may have diverted debtor moneys to U.S. entities.

In all three cases, pursuant to section 1521(a)(4), the recognition orders authorized the foreign representatives to examine witnesses under oath and obtain documents and other information in the United States regarding the foreign debtors’ and their stakeholders’ affairs, assets and liabilities.

The scope of 1521(a)(4) investigative powers is broad—potentially offering much broader powers than an administrator or liquidator might obtain through Brazilian or other foreign proceedings. Indeed, while at least one U.S. bankruptcy court has narrowly interpreted section 1521(a)(4) as the limit for discovery under chapter 15,<sup>9</sup> other courts have held that the “additional assistance” available to foreign representatives under section 1507(a) authorizes the court to further expand investigative powers beyond section 1521(a)(4) and to offer discovery powers akin to those of a Rule 2004 examination.<sup>10</sup> The scope of discovery permitted under Federal Rule of Bankruptcy Procedure 2004 has been described as “unfettered and broad” and permitting “fishing expeditions.”<sup>11</sup> Rule 2004 permits the examination of third

parties relating to, inter alia, “any matter which may affect the administration of the debtor’s estate.”<sup>12</sup> Rule 2004 examinations therefore provide one of the broadest discovery powers available in insolvency proceedings—and therefore the potential to obtain discovery of persons suspected of concealing assets or having information about the debtor’s affairs, to obtain transaction and financial documents necessary to locate assets that have been concealed by insiders or are otherwise undocumented by the debtor in its center of main interests. While such investigations may prove expensive, the ability to examine transactions and expose wrongdoing that may result in judgments for the benefit of creditors is often worthwhile.<sup>13</sup>

## **Conclusion: Chapter 15 Offers a Shield *and* a Sword**

Recognition of a foreign proceeding under chapter 15 of the U.S. Bankruptcy Code provides a stay of execution on the debtor’s assets within the territorial jurisdiction of the United States—without a doubt an invaluable shield. Moreover, section 1521(a)(4)—as may be further expanded pursuant to Rule 2004—enables administrators and other foreign representatives to proactively uncover additional information and assets in the U.S. and abroad. Recent Brazilian proceedings recognized under chapter 15 serve as a timely reminder of these broad discovery and investigative powers available to a foreign representative in the U.S. under section 1521(a)(4). Where such representatives serve in a fiduciary capacity, they may do well to consider the benefits of using chapter 15 as a cross-border investigative tool—even if the debtor has few identifiable assets in the United States.

### About the Authors:



David L. Lawton is Of Counsel with Morgan, Lewis & Bockius LLP. He represents private and public bondholders, banks, hedge funds, and other institutional lenders and equity groups in complex workouts, insolvency proceedings, and related litigation in domestic and international corporate financial restructurings.



David K. Shim is an Associate with Morgan, Lewis & Bockius LLP. He focuses his practice on financial insolvency matters in the United States, as well as international financial restructurings.

<sup>1</sup> 11 U.S.C. §§ 1502(8), 1521(a)(2).

<sup>2</sup> *Id.* § 1521(a)(5).

<sup>3</sup> *Id.* § 1521(a)(3).

<sup>4</sup> *Id.* § 1521(a)(7).

<sup>5</sup> *Usina de Açúcar Santa Terezinha Ltda.*, Case No. 19-11199 (Bankr. S.D.N.Y. Apr. 18, 2019); *USACIGA – Açúcar, Álcool e Energia Elétrica Ltda.*, Case No. 19-11200 (Bankr. S.D.N.Y. Apr. 18, 2019) (procedurally consolidated as Case No. 19-11199).

<sup>6</sup> Case No. 19-19932 (S.D. Fla. July 26, 2019).

<sup>7</sup> Case No. 19-19817 (S.D. Fla. July 24, 2019).

<sup>8</sup> Case No. 19-21256 (S.D. Fla. Aug. 22, 2019).

<sup>9</sup> See *In re Glitnir Banki hf.*, 08-14757, 2011 WL 3652764, at \*6 n.15 (Bankr. S.D.N.Y. Aug. 19, 2011) (observing that "§ 1521(a)(4) may not authorize the 'fishing expeditions' associated with Rule 2004").

<sup>10</sup> *E.g.*, see *Millennium Glob. Emerging Credit Master Fund Ltd.*, 471 B.R. 342, 347 (Bankr. S.D.N.Y. 2012) (stating that "one of the main purposes of chapter 15 is to assist a foreign representative in the administration of the foreign estate, which would militate in favor of granting a foreign representative broad discovery rights using the full scope of Rule 2004.").

<sup>11</sup> *In re Bennett Funding Grp., Inc.*, 203 B.R. 24, 28 (Bankr. N.D.N.Y. 1996).

<sup>12</sup> Fed. R. Bankr. P. 2004(b).

<sup>13</sup> See *In re Wash. Mut., Inc.*, 408 B.R. 45, 50 (Bankr. D. Del. 2009) (citing *In re Enron Corp.*, 281 B.R. 836, 840 (Bankr. S.D.N.Y. 2002)).

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