

**Protocols as a possible solution to jurisdiction
problems in cross-border insolvencies**

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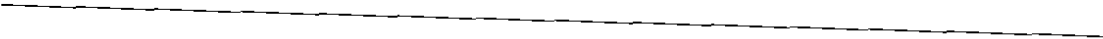
By

**LDM STROEBEL
12433489**

Study supervisor: Prof AL Stander

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1. Introduction

Cross-border insolvency law primarily deals with the situation where an insolvency procedure is initiated in one jurisdiction, in relation to the property of a debtor who is situated in another jurisdiction.¹ The liquidator then has to consider which procedures to follow and which system of law would apply in the administration of the debtor's property, wherever situated, for the benefit of local and foreign creditors. To regulate cross-border insolvency procedures more effectively, South Africa has assented to the *Cross-Border Insolvency Act 42 of 2000* (hereafter the CBA). This act is based on the *UNCITRAL Model Law on Cross-Border Insolvency*. The CBA is still not operational, mainly because of the failure of the Minister of Justice to designate certain states and will only be applicable to cross-border insolvency proceedings once a state is designated. This has the effect that the CBA will assist insolvency agents and creditors of the foreign designated states when they institute insolvency proceedings against a debtor who also has assets or a business in South Africa. The CBA does, however, not assist a South African insolvency agent or South African creditors when instituting insolvency proceedings against a debtor who also has assets or a business in a foreign country. To achieve such reciprocity the foreign state would need a similar act in which South Africa is a designated state. Company N, for example, is situated in the Netherlands, which has not incorporated the UNICTRAL Model Law on Cross-Border Insolvencies. Company S, its creditor, is situated in South Africa. Suppose company A has movable and immovable property in South Africa and the Netherlands. If company N goes bankrupt, a number of problematic questions arise: Where should company S institute insolvency proceedings? Which system of law would apply to the insolvency proceedings and would the courts in the Netherlands recognise a South African court order for the winding-up of company N?

In the absence of a binding international insolvency act that applies universally, states have to turn to their own domestic laws for guidance to

¹ Meskin *Insolvency Law* 17-1.

regulate these proceedings. The sovereignty of states and the protection of national interests contribute to the inefficiency of these proceedings. The question of the appropriate jurisdiction is further complicated by the different insolvency approaches states follow. Some states follow the territorial approach while others follow the universal approach which leads to great conflicts in the determination of the proper forum to institute cross-border insolvency proceedings. With the universal approach two further complications arise, namely forum-shopping and COMI. With forum shopping creditors seek the forum that will provide the greatest advantage to their interests, while COMI (centre of main interest) as a means to determine the appropriate forum under the universal approach is very vague and increases uncertainty rather than clarity. Multinational treaties or conventions prove to be less effective in an effort to increase co-operation between states than expected. Few examples of functional multinational treaties on insolvency exist. Bilateral treaties between countries are another option and easier to negotiate, but just as few examples of functional bilateral treaties exist.

The question that will henceforth be discussed in this dissertation, is whether a protocol between South Africa and foreign countries would contribute to a more workable and effective solution to jurisdiction problems in cross-border insolvency proceedings between these states? In order to address the above mentioned question, the jurisdiction problem, together with the occurrence of the territorial and universal approach in cross-border insolvencies will be discussed in chapter 2. In chapter 3 the South African position in relation to cross-border insolvency jurisdiction will be discussed. Thereafter a discussion on cross-border insolvency protocols will follow in chapter 4. A conclusion and recommendation will then follow in chapter 5.

2. Jurisdiction

Due to the absence of a binding international insolvency act that applies universally to all cross-border insolvencies, states have to turn to their own domestic laws for guidance on the regulation of these proceedings. The sovereignty of states and the protection of national interests contribute to the inefficiency of these proceedings. In most cross-border insolvency cases, the choice of the proper forum for the proceedings is problematic and therefore needs urgent investigation. This chapter will deal with the following aspects of jurisdiction: The universal and territorial approaches to cross-border insolvencies, forum shopping and the centre of main interest (COMI) as principles relevant to the determination of the appropriate forum in cross-border insolvency matters.

2.1 Universalism and territorialism

The main purpose of insolvency proceedings is to protect the interest of creditors and minimize their losses. Some insolvency models are criticised for their supposed inability to achieve such results.² When dealing with cross-border insolvencies, the approach of states fall somewhere between territorial and universal approaches. When following the territorial approach, jurisdictions seek to protect local creditors and their interests before foreign creditors are allowed to utilise the property for their benefit. On the other hand, the universal approach treats the cross-border insolvency as a single matter to ensure equal treatment to creditors from the different jurisdictions.³ At present, a heated debate is going on amongst academics in the United States of America on the best approach to be followed. Academic writers drastically dissent from one another on the advantages and disadvantages of these approaches in their writings.⁴

2.1.1 The territorial approach

2 Pottow 2005 *Michigan Law Journal* 1906.

3 Meskin *Insolvency Law* 17-1.

4 For a detailed discussion on the best approach to follow and ongoing debates on this issue see the articles of Westbrook JL and LoPucki LM on <http://heinonline.org>.

When a strict territorial approach is followed a state does not acknowledge any extraterritorial dimension of the insolvency. Instead, each country tries to seize the local assets of the insolvent **for the benefit of local creditors, which in turn promotes certainty amongst local creditors about the distribution of the assets.**⁵ For example, where a multinational corporation has assets in states A and B, both states following this approach will only be able to deal with and distribute the assets of the corporation situated within its own jurisdictional boundaries. State A will not be able to seize or distribute any of the assets located in state B, even if state A has the most creditors with greater claims. This could lead to unequal treatment of creditors where the majority of the assets are located in state B. This model rests on the idea of national sovereignty where the sovereign enforces its law on all within its reach.⁶ If any foreign creditor wishes to benefit from the assets under the insolvency, he has to institute and prove his claim in a local court and there is no recognition of a foreign proceeding.⁷ This is also referred to as the “grab rule”.⁸ Strictest territorialism takes no note of property situated in foreign countries, although most jurisdictions do recognize an international element where administrators seek property and rely on the necessary authority to call in the assets.⁹ With the territorial approach only the local laws of the jurisdiction is applied to insolvency matters.¹⁰ Although most states follow the territorial approach in cross-border insolvency matters, the development of global markets has lead to a greater interest in the universal approach, allegedly exposing the inadequacy of the territorial approach.¹¹

5 Westbrook 2002 HYPERLINK
<http://www.heinonline.org> 26 Jun.

6 Westbrook 2002 HYPERLINK
<http://www.heinonline.org> 3 Jul.

7 Mason 1995 HYPERLINK
<http://138.25.65.50/au/special/alta/alta95/rmason.html> 20 Jun.

8 Smith and Boraine 2002 *SA Merc LJ* 566.

9 Smith and Boraine 2002 *SA Merc LJ* 566.

10 The local insolvency regime is only applicable to the assets situated within that specific state. A representative can apply for recognition in a foreign court to deal with the assets situated in that state, but this is a cumbersome and long process and the foreign court will apply its own rules and protect its local creditors.

11 Westbrook 2002 HYPERLINK
<http://www.heinonline.org> 3 Jul. Prof JL Westbrook of the University of Texas Law School is one of the main advocates of the universal approach. He is frequently involved in academic debates with his main opponent, Prof L LoPucki, an advocate of the

When following the territorial model, the first **disadvantage** that occurs with the reorganisation of an insolvent is that each local uncoordinated proceeding focuses on maximizing returns for local creditors rather than focussing on the best possible return for the pool of creditors as a whole.¹² Secondly, critics contend that the assets in liquidation would be sold for a higher value if boundaries are disregarded and the assets are sold as a single package.¹³ Thirdly, it is argued that creditors might be treated unequally because each state has its own priority rules and remains in possession of different assets.¹⁴ The preference of creditors might differ from one state to another leading to the unequal treatment of creditors. An imbalance with the distribution of proceeds might also occur where the assets of the debtor situated in one state might be insufficient to satisfy the claims of local creditors, while a greater part of the debtor's assets might be situated in a state with little or one creditor. The fourth problem identified by critics is that modern technology and the globalisation of commerce allow the rapid removal and transport of assets from one state to another to benefit certain creditors. Due to a lack of co-operation between states in relation to insolvency proceedings it is very difficult for administrators to capture or recover these assets.¹⁵ Finally, it is also contended that most creditors in international insolvencies lose against local interests because of the lack of (compulsory) notice given to them of the foreign proceedings.¹⁶

territorialist approach. For further information on the universalist/territorialist debate, see the articles of these writers at <http://www.heinonline.org>.

12 Nicols 2003 HYPERLINK

<http://www.amercol.org/images/Paul> 26 Jun.

13 Farley 2004 HYPERLINK

<http://www.heinonline.org> 3 Jul. Where a multinational corporation, for instance a car manufacturer, has factories in states A, B and C, it could be more advantages to sell all the different car components located in different countries as a whole, rather than trying to sell each factory separately. Another motor company could then take it over and continue business as a whole, retaining production value and increasing its all over value.

14 Farley 2004 HYPERLINK

<http://www.heinonline.org> 3 Jul.

15 Nicols 2003 HYPERLINK

<http://www.amercol.org/images/Paul> 26 Jun.

16 Farley 2004 HYPERLINK

<http://www.heinonline.org> 3 Jul.

In reply to the shortcomings of the traditional territorial approach, a co-operative territorialist model has been proposed.¹⁷ With this model each court would appoint a representative.¹⁸ Where co-operation is then needed the representatives of the different jurisdictions may enter into agreement to regulate certain aspects of the proceedings, although it is not compulsory.¹⁹ Entering into such an agreement increases the distribution of the debtor's assets, which leads to greater equality among creditors. Such an agreement could also prevent the dominance of one jurisdiction in the determination of priority rights of creditors and the distribution of assets among them.²⁰ The problem unfortunately remains unsolved where the representatives of the different jurisdictions fail to reach an agreement.

2.1.2 The universal approach

The universal approach supports primarily a co-operative approach between states when dealing with the insolvency of a multinational corporation. This approach is based on the idea that a central proceeding is used for the administration and collection of all the assets of the debtor, irrespective of where the assets are situated.²¹ The appropriate forum is determined by various considerations under different legal systems. Amongst others the place of incorporation²² is used as an indication of the appropriate forum; the "home country"²³ of a corporation; the place where it has its principal place of

17 See LoPucki 2000 at <http://www.heinonline.org>.

18 Both the local court and foreign court.

19 Biery 2005 HYPERLINK <http://www.heinonline.org> 3 Jul. These agreements are concluded between individuals representing the different jurisdictions and not between courts.

20 Biery 2005 HYPERLINK <http://www.heinonline.org> 3 Jul.

21 Biery 2005 HYPERLINK <http://www.heinonline.org> 3 Jul. Where a multinational corporation has assets in states A and B, a court in one of these states will be appointed with the authority to deal with and distribute the assets located in both states A and B. This could potentially lead to uncertainty amongst foreign creditors on the rules of preference to be used for the distribution of the assets. The rules in relation to recognition could also be uncertain.

22 The "place of incorporation" and the "place where the corporation has its registered office" seem to be synonymous. See Biery 2005 HYPERLINK <http://www.heinonline.org>.

23 This term is used synonymously with the centre of main interest of a corporation. See El-Boraie 2005 HYPERLINK <http://www.heinonline.org> 4 Jul.

business²⁴ or according to the words of the UNCITRAL Model Law, the centre of its main interest (COMI).²⁵ All the creditors, foreign and local then has to file and prove their claims in this forum.²⁶ This forum will be in control of the proceedings and apply its substantive law to the case. To the degree needed, other jurisdictions may convene ancillary proceedings to give effect to the orders of the governing court.²⁷ The assets situated in the foreign jurisdiction could also be transferred to the governing forum if the local jurisdiction does not want to convene ancillary proceedings.²⁸ The universal model rests on the notion that a state needs to cede its sovereignty to another state in order to have the insolvency matter adjudicated in that state. However, most states will gladly apply their insolvency laws to international bankruptcy disputes, but very few will be willing to cede their sovereignty in this regard when they are in the ancillary position.²⁹

This raises two fundamental and problematic questions: Which jurisdiction's substantive law will apply to the proceedings and which forum will be the appropriate one to govern the proceedings?³⁰ Critics argue that unless a unified choice-of-law comes into existence (regulating the choice of the

24 The United States Bankruptcy Code provides that a corporation seeking to reorganize place of business, its principal assets or its domicile (considered to be the place where the corporation is incorporated). See Rasmussen 2000 [HYPERLINK http://www.heinonline.org](http://www.heinonline.org) 4 Jul.

25 S 16(3) of the South African *Cross-Border Insolvency Act* 42 of 2000 assumes, unless the contrary is proven, that this is to be the place where the corporation has its registered office. The "centre of main interest" and "the home country" of a corporation will therefore both be determined by the place of incorporation or the place where a corporation has its registered office, as these terms seem to be used interchangeably by writers on this subject. See fn 22 and 23 above. What happens in the case where a company has its registered office, or its place of incorporation in one place, but conducts most of its business in another place? It could be helpful to distinguish between "place of incorporation" together with "the place where a corporation has its registered office" on the one hand, and "the centre of main interest" together with "the principal place of business" on the other hand for the purpose of determining the appropriate forum for insolvency proceedings. Two cases had recently been decided hereon where reference was made to the *Eurofoods* case. See footnote 69.

26 Farley 2004 [HYPERLINK http://www.heinonline.org](http://www.heinonline.org) 3 Jul

27 Pottow 2005 [HYPERLINK http://www.heinonline.org](http://www.heinonline.org) 3 Jul.

28 Pottow 2005 *Michigan Law Review* 1904.

29 Pottow 2005 *Michigan Law Review* 1904.

30 For a detailed discussion on the inefficiency of the universal approach see LoPucki *The Case for Cooperative Territoriality in International Bankruptcy* 2000 at <http://www.heinonline.org>.

appropriate forum) and a unified insolvency law comes into existence that governs the proceedings in all states, the universal approach is not a workable model.³¹

Because of the inefficiency of the pure form of universalism, a modified version has also been developed. Under modified universalism the local courts have a degree of freedom to decide whether to comply with the requests of the governing jurisdiction or not.³² It has been suggested that the legal standard for compliance might be that the position of local creditors should not be affected and public policy not offended.³³ This means that the assets should be distributed according to the law of the local courts, with foreign courts only having such distribution power with the express consent of the local courts.³⁴ To my mind this position is hardly distinguishable from the territorial approach.

2.2 Forum shopping

The acceptance of the universal approach³⁵ leads to the unacceptable occurrence of forum shopping. Professor LoPucki³⁶ defines forum shopping as:

Attempting to have one's case heard in the forum where it has the greatest chance of success.

The power to choose the appropriate forum for the resolution of an insolvency dispute is important for various reasons. In the first instance the selected

31 For a discussion on these problems see chapter 1.2 and 1.3 below.

32 LoPucki 2000 HYPERLINK
<http://www.heinonline.org> 4 Jul.

33 LoPucki 2000 HYPERLINK
<http://www.heinonline.org> 4 Jul.

34 LoPucki 2000 HYPERLINK
<http://www.heinonline.org> 4 Jul.

35 It seems as if the majority of academic writers accept and prefer the universal approach, especially the American jurists.

36 LoPucki 2000 HYPERLINK
<http://www.heinonline.org> 4 Jul. In this article Prof LoPucki also refers to another definition of forum shopping as "an attempt by a litigant to have his action tried in a particular court or jurisdiction where he feels he will receive the most favourable judgment or verdict." This is the biggest point of criticism against the universal approach.

forum will be the venue where parties have to go to court, possibly leading to great travelling expenses and inconvenience to some, especially in the case of multinational corporations.³⁷ More importantly the choice of forum could determine the outcome of the case. The different approaches a state would follow, for example a territorial or a universal approach, could have a great effect on the outcome of the case and the way in which the interests of creditors are protected.³⁸ When an international or multinational corporation fails, several states may rightfully claim to have jurisdiction to resolve the dispute.³⁹ In the absence of universal choice-of-law rules appointing the appropriate forum, states have to look at their different domestic laws for guidance in this matter. Cross-border insolvencies involve many parties and their interests. These interests not only include those of the debtor and the creditors, but also the interests of courts and lawyers to have a dispute heard in a specific forum. The legal fees of big insolvency cases reaches very high amounts, and is normally paid to attorneys in the city where the proceedings are held. **This provides enough reason for bankruptcy courts to compete for big cases.**⁴⁰ It is also argued that courts could and do adopt legal positions and practices that favour the parties who choose the forum in bankruptcy cases.⁴¹

2.2.1 *The Yukos case*

A very recent example (the case is still pending) of forum shopping occurred where territorialism and universalism clashed. This is the case where the Russian company OAO Yukos Oil (hereafter Yukos) instigated insolvency proceedings under Chapter 15 of the *American Bankruptcy Code*.⁴² Yukos is

37 LoPucki 1991 HYPERLINK
<http://www.heinonline.org> 4 Jul.

38 See 1.1 above for the possible disadvantages of both approaches.

39 Pottow 2005 *Michigan Law Review* 1904.

40 LoPucki 1991 HYPERLINK
<http://www.heinonline.org> 4 Jul.

41 LoPucki 1991 HYPERLINK
<http://www.heinonline.org> 4 Jul.

42 Pottow *The Yukos Adventure* 1-18. Taking into account that the case is still pending all the information contained in this article might not be a precise version contained in the actual case to be reported. The author, however, states that his information is derived

a Russian multinational corporation, with subsidiaries in Russia (YNG)⁴³ and the Netherlands.⁴⁴ Yukos ran into financial problems when the Russian government re-assessed the 2003 and prior year taxes of the corporation. These taxes were disproportionate to any measure and lead the corporation into financial distress.⁴⁵ In 2004 the Russian tax authorities had extensive back-tax claims against Yukos adding up to tens of billions of dollars.⁴⁶ This seemed to have scared a consortium of banks to which Yukos owed money (the Bank Group) which sent notice of default to the corporation and acceleration of the debt. By 2005 the Bank Group had reduced its claim against Yukos from one billion dollars to \$500 million dollars in an **English court** proceeding in London. A second claim was brought by an entity called Moravel Investments for an amount of \$700 million. This entity also reduced its claim against Yukos by way of an international arbitration proceeding in Moscow.⁴⁷ The third claim came from a (former) subsidiary, YNG. None of these claimants instituted involuntary bankruptcy proceedings, but pursued different collecting strategies involving several courts and jurisdictions.⁴⁸ The Russian government, desiring to regain control over oil and gas assets, announced that they would seize and conduct an auction of YNG, holding 60% of Yukos's value. It soon became clear that the Russian government was going to buy YNG at half the price of its value. In an effort to prevent the sale the remaining directors of Yukos tried to place Yukos under Chapter 11 reorganization proceedings in the **United States**.⁴⁹ The managers succeeded and got a Temporary Restraining Order (TRO), but the Russian auctioneer

from United States (hereafter US) pleadings and English translations of Dutch, Lithuanian and Russian press releases.

43 Also known as 'Yugansneftgas'.

44 The Dutch subsidiary consisted of various subsidiaries, the last one down the line was AB Mazeiku Nafta, a Lithuanian corporation and joint venture between a Dutch subsidiary and the Lithuanian government, holding 54% interest in a Lithuanian refinery.

45 Some of the taxes claimed by the Russian tax authorities were more than the gross income of Yukos for some of these years. For an in depth discussion on the absurdity of the taxes claimed, see Pottow *The Yukos Adventure* 1-2.

46 Pottow *The Yukos Adventure* 3.

47 Pottow *The Yukos Adventure* 3.

48 Pottow *The Yukos Adventure* 4. The possibility exists, on the grounds of the balance sheets that Yukos is not insolvent, even though not paying its debts, explaining why none of the claimants filed for involuntary bankruptcy proceedings.

49 Pottow *The Yukos Adventure* 4. The company has some assets in the US and the CFO lived there.

ignored it and went on with the sale. YNG was then sold and transferred to Rosneft, the Russian government's fully owned competitor of Yukos.

The Bank Group petitioned for recognition of their English judgement in a **Russian court** in September 2005, to realize their claim against the Russian assets of Yukos. The Bank Group however went further and tried to find assets of Yukos to seize outside of Russia. That is when they discovered AB Mazeiku Nafta, one of the Dutch subsidiaries of Yukos.⁵⁰ The Bank Group then attached some of Yukos's shares in Yukos Finance, a Dutch subsidiary to get hold of the refinery. Dutch law recognizes only foreign judgements of an international arbitration award or from a court of a recognition-treaty country. Both the Bank Group⁵¹ and Moravel's⁵² awards were recognized under this provision and their attachments of Dutch assets were allowed. YNG sought to follow the same route, but had only a Russian judgement from an Arbitrazh court in Moscow.⁵³ Russia not being a recognition-treaty country had to re-litigate in a **Dutch court**. The Russian government failed to prevent the sale of the refinery and the **Dutch court** held that the sale would proceed.

Shortly after this the Bank Group petitioned for an involuntary bankruptcy in **Russia**. This did not make sense, seeing that the Dutch sale was going smooth and that the Bank Group would try and drive Yukos into bankruptcy for \$500 million - Yukos being a multi-billion dollar corporation. Parallel to the recognition of its English judgement in a Dutch court, the Bank Group also sought **recognition in Russia** where the rest of Yukos assets were situated, which was granted in December 2005. The Bank Group's claim was bought out by the Russian government on condition that the Bank Group opens bankruptcy proceedings against Yukos.⁵⁴ One of the main features of Russian insolvency law is that it is strictly territorialist, not reaching beyond its

50 See fn 42.

51 The award from the English court was recognized because England is a recognition-treaty country of the Netherlands.

52 Moravel got their award from an international arbitration, which is a ground for recognition under Dutch law.

53 Pottow *The Yukos Adventure* 6.

54 Pottow *The Yukos Adventure* 8.

boundaries to assets located in foreign jurisdictions.⁵⁵ Another feature is that corporate form is rigidly adhered to and although Yukos was placed in insolvency procedures in Russia, its separate subsidiaries in the Netherlands would not be placed in insolvency.⁵⁶ The monitor appointed for the insolvency proceedings was Mr. Rebgun, who requested a **Russian arbitrazh court** for a restraining order, prohibiting the sale of all the debtor's assets, whether held "directly or indirectly".⁵⁷ The court granted the order, even though the separation of corporate form was required under Russian law. In effect this order meant that the Russian court was expanding its bankruptcy jurisdiction to the debtor's Dutch subsidiaries, uncharacteristic of the territorialist approach.⁵⁸ Mr. Rebgun then used this Russian court order to try and intervene in the **Dutch proceedings** to prevent the sale of the refinery. This request was to be heard on the 18th of May. Next Mr. Rebgun filed a "petition for recognition" under Chapter 15 of the *US Bankruptcy Code* and as interim relief, pending the outcome of the recognition request, a restrain on the principles of Yukos from continuing with the sale of the refinery.⁵⁹ **The US bankruptcy court in the Southern District of New York** granted the TRO and the court is still exercising its jurisdiction to enforce it. Some of the Yukos managers conducting the refinery sale are US citizens and residents, adhering to the TRO for the fear of facing contempt.⁶⁰

This case, up to this point, serves as a clear illustration of the jurisdiction problem in cross-border insolvencies where one state follows a territorial approach and another state the universal approach. Where two states follow a territorial approach, for instance Russia and the Netherlands, and the one tries to reach assets in the other, the chances of assistance depend on the process of recognition of judgments.⁶¹ In the current case, were it not for the extraordinary nature of the expansive Russian court order, it is uncertain

55 Pottow *The Yukos Adventure* 8.

56 Pottow *The Yukos Adventure* 8.

57 Pottow *The Yukos Adventure* 9.

58 Mr Rebgun held that this was done to avoid the separate sale of the assets to the detriment of all the creditors.

59 Pottow *The Yukos Adventure* 9.

60 Pottow *The Yukos Adventure* 10.

61 Pottow *The Yukos Adventure* 10.

whether the Dutch assets of the debtor could be resolved in the Russian insolvency proceeding and whether ancillary proceedings in the Netherlands would be required.⁶² The United States with its universalist approach has its own problems in a world where territorialism still prevails. Pottow⁶³ correctly sums up the situation in this case by stating that universalist states:

Attract territorialist suitors who want to evade the confines of territorialism when they prove inconvenient, even when there is no connection to the dispute.

In the Yukos case four different courts were involved in the collection of debt at different times, each court being the specific choice of a certain claimant to best serve his interests. The Bank Group approached an English court, a Dutch court and a Russian court. Moravel and the Russian Government also approached the Dutch court. Finally the monitor of the Yukos insolvency proceedings approached the Dutch and US courts. In between the court proceedings many arbitration awards were also made. This creates great unpredictability and **shows that in practice neither the territorialist nor the universalist approach has the perfect answer to combat forum shopping.**

2.3 Centre of main interest (COMI)

As mentioned above, the universal approach is based on the idea that a central proceeding is used for the administration and collection of all the assets of the debtor, irrespective of where the assets are situated.⁶⁴ Critics argue that the universal model provides insufficient guidelines to determine where the central and appropriate forum should be,⁶⁵ thus promoting forum

62 Pottow *The Yukos Adventure* 10.

63 Pottow *The Yukos Adventure* 1-18.

64 Biery 2005 [HYPERLINK](http://www.heinonline.org)
<http://www.heinonline.org> 3 Jul.

65 As discussed in 1.1.2 above, the place of incorporation or the place where a corporation has its registered office is usually used to determine the main forum. This criterion is not very helpful and quite vague where a multinational corporation has registered offices in different countries. This leads to the question whether the main forum would be the one where the parent company operates the subsidiaries, or the country where a subsidiary is incorporated and has the majority of its operations and assets? This could lead to a

shopping and creating unpredictability.⁶⁶ Some of the criticism to the universal approach includes the fear that courts will increasingly compete for big insolvency cases, even though there might be no or a very small connecting factor between the forum and the place of incorporation of the entity or the location of its assets. One author referred to a recent example, where the European Union adopted a universalist bankruptcy scheme in 2000 that became effective in 2002.⁶⁷ Soon after the act came into effect courts immediately started competing for big cases. In a number of those cases the courts of European Union countries have claimed that their jurisdictions were the COMIs of the corporations, **even though neither the assets, operations nor the place of incorporation were in those jurisdictions.**⁶⁸

Under the UNICTRAL Model Law⁶⁹ the recognition of insolvency proceedings should be distinguished between foreign main and foreign non-main proceedings.⁷⁰ This distinction is important for the determination of the appropriate forum where the proceedings are to be held. With foreign main proceedings under the UNICTRAL, reference is made to COMI as a determination of the forum where the proceedings should be held.⁷¹ This centre of its main interest is refutably presumed to be the registered office of the debtor or his habitual residence.⁷² Foreign non-main proceedings in turn are those that take place in a foreign state where the debtor has an establishment, being any place of operations where the debtor carries out a non-transitory economic activity with human beings and goods or services.⁷³ These standards are said to be vague and provide problems in practical situations, especially where multinational corporations are involved.⁷⁴ Where the parent company of a multinational corporation has its registered office in

possible distinction between the administrative and operational functions of a multinational company to determine its centre of main interest.

66 See for eg. LoPucki 2005 *American Bankruptcy Law Journal* 144.

67 LoPucki 2005 *American Bankruptcy Law Journal* 144.

68 LoPucki 2005 *American Bankruptcy Law Journal* 144. The decision of the European Court of Justice in *Eurofood IFCS Ltd* Case C-341/04 serves as an example of this.

69 Hereafter "the Model Law".

70 S 17(2)(a) of the CBA 42 of 2000.

71 S 17(2)(a) of the CBA 42 of 2000.

72 S 16(3) of the CBA 42 of 2000 (based on the Model Law).

73 S 1(c) of the CBA 42 of 2000.

74 LoPucki 2005 *ABLJ* 144.

one state, and all the subsidiaries have registered offices in other states, how is the centre of main interest determined, especially where only a very small part of the multinational corporations' business is carried out at the place where the parent company is located? This criticism is valid indeed and of great importance. In the *Daisytek-ISA Ltd*⁷⁵ case it was stated that:

The centre of main interests should correspond to the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties.⁷⁶

It is further argued that the place of registration of a multinational corporation is only one of the relevant facts in determining its COMI and that the place of registration might well be far down the list of considerations.⁷⁷

From the above it is clear that cross-border insolvency law is by no means unified, great differences exist and the fundamental approaches states follow vary greatly. Neither the territorialist nor the universalist approach provides the perfect solution to cross-border insolvency problems. Both models have their advantages, but fail to provide a workable solution to all cases. The problems with the determination of the most appropriate forum where insolvency should be heard, together with the increasing danger of forum shopping only increase jurisdictional uncertainty in cross-border insolvencies. A mid-way between the two extremes of universalism and territorialism could provide an interim answer. It is also clear that the phenomenon of forum-shopping is undesired, as it does not have the interest of the insolvent estate and its creditors as its primary focus.

75 *Re Daisytek-ISA Ltd* 2003 BCC 562.

76 See also Rajak "Company Groups" 14, contribution delivered at INSOL Academics Meeting Scottsdale 20 May 2006.

77 Rajak "Company Groups" 11, contribution delivered at INSOL Academics Meeting Scottsdale 20 May 2006.

3. The South African position

South Africa adopted the *Cross-Border Insolvency Act 42 of 2000 (CBA)* which came into force on the 28th of November 2003.⁷⁸ This Act has the aim to provide effective mechanisms for the regulation of cross-border insolvency matters, to further regulate the jurisdiction of the High Court in relation thereto and to make provision for related matters. The CBA is, however, not in operation yet since its application is dependent on the designation of certain states by the Minister of Justice.⁷⁹ At this stage no states have been designated and cross-border insolvencies continue to be governed by the common law. This includes the rules of private international law and precedent.⁸⁰ This leads to a situation where parties currently involved in cross-border insolvencies need to carefully consider which legal principles will guide their proceedings. It is thus necessary to discuss the position under the common law.

3.1 *The common law and precedent*

The South African legal system has its origin in the Roman-Dutch law. It is generally referred to as the South African common law.⁸¹ English law also had an influence on the South African legal system, especially in areas of mercantile law and the adoption of the English system of precedent.⁸² To determine which principles would apply to a cross-border insolvency case under the common law, a distinction has to be drawn between the type of property that is involved (movable or immovable property), and the classification of the parties involved (individuals or a company).⁸³

3.1.1 *Movable property*

78 Proclamation R 73 of 2003.

79 S 2(2) of the CBA.

80 *Meskin Insolvency Law* 17-3.

81 Smith and Boraine 2002 *ABI Law Review* 140.

82 Smith and Boraine 2002 *ABI Law Review* 141.

83 Smith and Boraine 2002 *ABI Law Review* 179.

The general rule in relation to movable property is that “it is subject to the same law as that which governs the person of the owner, in other words, the law of his domicile”.⁸⁴ Movables follow the person.⁸⁵ An order granted by the court of the insolvent’s foreign domicile (*lex domicilii*) automatically divests such a person of his or her movables in South Africa, creating a single *concursum creditorum*. This principle therefore supports the universalist approach. This rule has been clearly illustrated in the case of *Trustee of Howse, Sons & Co v Trustees of Howse, Sons & Co*.⁸⁶ In this case an English firm sought liquidation⁸⁷ in London by arrangement or composition. Their creditors which were situated in the Cape Colony later instituted proceedings for sequestration in a Cape court. The firm only had movable assets in the Cape. The property was assigned by virtue of the English law, the law of the debtor’s domicile. This had a universal effect and the insolvent’s movables were transferred from everywhere else as well, including the movables in the Cape Colony.⁸⁸ In applying the rule as stated above and after being satisfied that the local creditors would not be harmed,⁸⁹ the Cape court set aside the sequestration proceedings in the Cape and the local trustee’s appointment. Since this judgment the rule on movable property has often been followed by other courts.⁹⁰ The fiction whereby the movable property is assigned to their owner’s domicile is based on comity.⁹¹ The use of this fiction serves as a means of simplifying the transfer of rights. It prevents the confusion that arises

84 Per De Villiers in *Trustee of Howse, Sons & Co v Trustees of Howse, Sons & Co; Jocelyne v Shearer & Hine* 1884 3 SC 14.

85 Smith 2002 SA Merc LJ 24. In Latin it is stated that the movables “stick to his bones” by the words *mobilia sequuntur personam*.

86 *Trustee of Howse, Sons & Co v Trustees of Howse, Sons & Co; Jocelyne v Shearer & Hine* 1884 3 SC 14.

87 It should be noted here that the English firm sought a “liquidation” order in England, while the creditors in the Cape Colony sought a “sequestration” order. In South Africa a firm is a form of partnership and will not be subject to liquidation, but will however be subject to sequestration.

88 Smith 2002 SA Merc LJ 25.

89 The court warned that it would not take this step if the local creditors would have lost local preferences. Therefore, according to my mind, the creditors would retain their local preference although they might have to claim in accordance with English procedure.

90 *Midgley’s Trustee v Balance & Letchford* 1884 5 NLR 309; *Leslie’s Trustee v Leslie* 1903 TS 839; *Van Heerden’s Trustee v Glatt* 1909 26 (SC) 592; *Herman NO v Tebb* 1929 CPD 65; *Viljoen v Venter* NO 1981 2 SA 152 (W).

91 Comity is the recognition which one nation allows within its territory to the judicial acts of another state. For a further discussion on this fiction see Forsyth CF *Private International Law* 3rd ed (1996) 36-41.

with conflicting *leges rei sitae*.⁹² This has the effect that all the movable property of the insolvent is considered to be present in his domicile, and also vests⁹³ in the trustee appointed in accordance with his *lex domicilii*, as it was stated in *Re Estate Morris*.⁹⁴

It is clear...that sequestration at the domicile vests in the trustee of the insolvent all the latter's movables, wherever situated. By a fiction of law the insolvent's movable property is all considered to be present at his domicile, and sequestration there operates at once to transfer that movable property, wherever it is actually situated, to the trustee when appointed.

Although the movable property is deemed to be owned by the foreign trustee, the foreign order still needs to be given effect to under the South African law.⁹⁵ The foreign trustee's ownership of the movable property is therefore not unlimited. Courts might impose certain conditions⁹⁶ with which the trustee should comply before being allowed to remove the property from the jurisdiction.⁹⁷ This step appears to bring one closer to the territorial approach. Usually this condition consists of the protection of the preference of local creditors.⁹⁸ This approach could be a practical solution to and, to my mind, constitutes a midway between the extremes of universalism and territorialism.

92 Smith 2002 *SA Merc LJ* 26.

93 In his article Smith states that "the trustee already 'owns' the movable property", Smith 2002 *SA Merc LJ* 26. In the South African law of insolvency there has not yet been an Appellate decision pertinently indicating that ownership transfers to the trustee. In *De Villiers NO v Delta Cables (Pty) Ltd* 1992 1 SA 9 (A) the court only made an *obiter* remark in this regard. The words "vests in" are generally accepted to mean that ownership has passed.

94 In *re Estate Morris* 1907 TS 657.

95 Smith and Boraine 2002 *ABI Law Review* 179. In order for a foreign representative to be recognized as such in South Africa, he must apply to a local High Court for recognition and assistance (Meskin *Insolvency Law* 17-7). Where the rights of a third party may be affected by the application, such a third party must be notified of the application (*Clegg v Priestly* 1985 3 SA 950 (W) 311F).

96 For further reading on the different conditions a court could impose, see Ailola DA "Recognition of Foreign Proceedings, Orders and Officials in Insolvency in Southern Africa: A Call for a Regional Convention" 1999 *Juta Business Law* 23-25.

97 Smith 2002 *SA Merc LJ* 26.

98 In *Trustee of Howse, Sons & Co v Trustees of Howse, Sons & Co; Jocelyne v Shearer & Hine* 1884 3 SC 14 it was made clear that the court would only allow a foreign trustee to remove local assets if the preference of local creditors would be protected. This means, to my mind, the preference according to the South African law of insolvency, hence secured, preferent and concurrent preferences and does not mean that local creditors should necessarily be paid out first. The question then arises, "Do local concurrent

In *Ex parte Palmer: in re Hahn*⁹⁹ it was stated that where movable property is concerned, a formal application to local courts for the recognition of the foreign trustee is not strictly necessary.¹⁰⁰ The court stated that:

As a matter of practice however such an application is invariably made and the need for formal recognition has been elevated into a principle.

The court also referred to the judgement in *Moolman v Builders & Developers (Pty) Ltd*¹⁰¹ regarding the need for formal recognition of trustees. In this case the court held that the representative would not practically be able to act in respect of the local goods without the active assistance of the local courts and that the representative needed to be recognised by a local court in order to be qualified to deal with the local assets. Therefore *Ex Parte Palmer* concluded that it is not a rule that foreign trustees should seek **recognition** from local courts to be able and assisted in dealing with local movables. The need for active assistance by the local courts however elevated this practice into a principle. Smith and Boraine is also of the opinion that a representative will very seldomly be recognised if he/she has not been appointed by the court of the *lex domicilii* of the insolvent.¹⁰² Even then the recognition will only be applicable to property within that court's jurisdiction.¹⁰³ From the above it is clear that formal recognition of trustees in regard to movable property is not a statutory requirement. Practice, practical considerations and the fact that it is

creditors enjoy a preference? There is no clear decision of the South African courts in this regard. The orders granted by our courts could create the impression that local concurrent creditors are preferred above non-local creditors. In *Ex Parte Steyn* 1979 2 309 (O) at 311B-D it was stated that "Creditors will probably enjoy priority, whether as a secured creditor or otherwise, only if priority is recognised by the *lex fori*." The position of concurrent creditors has not been decided authoritatively and the position may still be as it was set out in early Colonial legislation of the turn of the century before the repeal thereof. In this regard section 9 of the *Foreign Trustees and Liquidators Recognition Act* 7 of 1907 could serve as an example, stating that the balance after payment of local preferent creditors was available for distribution among the general body of creditors, including local concurrent creditors, provided that the balance had to remain in the Colony until the dividend of local concurrent creditors had been paid, in so far as such balance allowed a payment.

99 *Ex parte Palmer NO: in re Hahn* 1993 3 SA 359 (C) 362 F.

100 *Ex parte Palmer NO: in re Hahn* 1993 3 SA 359 (C) 362 F.

101 *Moolman v Builders & Developers (Pty) Ltd* 1990 1 SA 954 (A).

102 Smith and Boraine 2002 *ABI Law Review* 179.

103 Smith and Boraine 2002 *ABI Law Review* 179.

elevated into a principle should however be sufficient to persuade any foreign trustee that it is the most appropriate and safest way to follow.

3.1.2 *Immovable property*

With immovable property the law of the location of the property (the *lex situs* or the *lex rei sitae*) is decisive.¹⁰⁴ The effect of the foreign sequestration order is therefore limited territorially.¹⁰⁵ Before a representative will be allowed to deal with local immovable property, he must first approach the South African court for recognition of his appointment. The South African courts exercise discretion when hearing such an application, based on comity, convenience and equity.¹⁰⁶ It seems to be a tendency of international law that immovable property should be governed by the laws of the country in which it is located.¹⁰⁷

3.1.3 *The distinction between individuals and companies*

Unlike the position with movable property where an individual is not obliged to seek the recognition of a local court, with the liquidation of a company or a close corporation that is domiciled in a foreign country, the foreign representative is compelled to seek the recognition of the local courts.¹⁰⁸ In *Ward v Smith: in re Gurr v Zambia Airways Corporation Ltd*¹⁰⁹ the court demonstrated the danger of not seeking recognition from the local courts. In this case, the Zambian liquidators of the external company, Zambia Airways, relied on section 354 of the South African *Companies Act*¹¹⁰ for a court order containing the following: Recognition of their appointment, declaring them empowered to administer the company's South African estate, the setting aside of a provisional and final winding-up order granted to a South African

104 *Ex parte Palmer NO: in re Hahn* 1993 3 SA 359 (C) 362.

105 *Smith* 2002 SA Merc LJ 29.

106 *Re Estate Morris* 1907 TS 657; *Ex parte Stegmann* 1902 TS; *Chaplin v Gregory* 1950 3 SA 555 (C). See p 2.1.4 below.

107 *Ex parte Singer: in re Insolvent Estate Skeen* 1905 26 NLR 536; *El Cid Ltd v New Jersey Zinc Co* 575 F 1513 (SDNY) 983.

108 *Donaldson v Brititish SA Asphalt and Mfg Co Ltd* 1905 TS 753.

109 *Ward v Smith: in re Gurr v Zambia Airways Corporation Ltd* 1998 3 SA 175 (SCA).
110 61 of 1973

employee and compelling the provisional liquidator to hand them the company's assets.¹¹¹ Without the recognition from South African courts of their appointment, the foreign liquidators, however, tried to deal with the South African assets. The Supreme Court of Appeal dismissed their application and held that the appointment of the foreign liquidators and authorisation by the court of the company's incorporation (Zambia) had no effect outside its jurisdiction. Unless duly recognised by the local court, foreign liquidators cannot deal with movable or immovable assets of a company¹¹² in South Africa. In this case the court also held that a misunderstanding of the South African law will not be an acceptable excuse for a foreign liquidator's tardiness and attempts at dealing with local assets without the necessary recognition from the local courts.¹¹³ The inference could therefore be drawn that formal recognition of foreign trustees should always be applied for in local courts, irrespective of the assets being movable, immovable, that from an individual or a company's. The position of foreign trustees is therefore really the same.

3.1.4 Comity, convenience and equity

Where a local court has to consider granting an application for recognition of a foreign trustee, it has to exercise this discretion on the grounds of comity and convenience.¹¹⁴ This discretion of the court is absolute.¹¹⁵ Although comity and convenience are factors which influence a court's decision to grant an application for recognition of a foreign trustee, they are not separate grounds for granting a trustee such an order.¹¹⁶ In *Ex Parte Palmer* the court made it clear that there is no authority for the contention that a South African court will grant an order for the recognition of a foreign trustee simply on the grounds of comity and convenience, without having regard to the insolvent's domicile.¹¹⁷

111 Smith 2002 SA Merc LJ 28.

112 Or a close corporation.

113 Smith 2002 SA Merc LJ 28.

114 *Ex parte Palmer NO: in re Hahn* 1993 3 SA 359 (C) 362-363.

115 *Ex parte Palmer NO: in re Hahn* 1993 3 SA 359 (C) 362-363. The "absolute discretion refers to immovable property.

116 *Ex parte Palmer NO: in re Hahn* 1993 3 SA 359 (C) 362-363.

117 *Ex parte Palmer NO: in re Hahn* 1993 3 SA 359 (C) 365.

A clear definition of **comity** is found in the case of *Hilton v Guyot*¹¹⁸ where the judge said that it 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 law.**¹¹⁹

Comity does however not mean that a court has to cede its own authority over its process and the application of substantive laws of its own jurisdiction.¹²⁰ It has been argued that the proper basis for the enforcement of a foreign judgment is not comity, but the existence of a right in the person seeking the enforcement, or a duty on the part of the person against whom enforcement is sought.¹²¹ The weight of authority is however against this contention. It has also been argued that comity as a consideration for the granting of a recognition order in cross-border insolvency proceedings **has to be balanced with the protection of local stakeholders' interests.**¹²² In my view comity could be defined as the recognition by country A of the legislative, executive and judicial acts of country B, after careful consideration of a possible disadvantage to local creditors.¹²³

The principle of **convenience** and **equity** is clearly illustrated in the case of *Deutsche Bank AG v Moser*.¹²⁴ The applicant was a company duly incorporated and registered in Germany. The first respondent was a German citizen, who permanently resided in Germany. Between 1987 and 1992 the first respondent signed three agreements of suretyship in favour of the applicant, whereby he stood surety for the debts of three German companies

118 *Hilton v Guyot* 1895 159 US 113 at 163-164.

¹¹⁹ Emphasis added.

120 Sarra "Northern Lights" 16-17, contribution delivered at INSOL Academics Meeting Scottsdale 20 May 2006.

121 *Steinber v Cosmopolitan National Bank Of Chicago* 1973 4 SA 564 (RA).

122 *Steinber v Cosmopolitan National Bank Of Chicago* 1973 4 SA 564 (RA).

123 The word "recognition" therefore means it is "acceptable" to country A, but only after considering and balancing the rights of country A's own citizens in the specific case. It is therefore not mere goodwill and courtesy.

124 *Deutsche Bank AG v Moser and Another* 1999 (4) SA 216 (C).

of which he was a shareholder and managing director. One of the companies had been wound up in Germany, while the other two were *de facto* insolvent. The first respondent had virtually no assets in Germany but he owned immovable property at Plettenberg Bay, Cape, which was within the area of jurisdiction of the South African court.

The first respondent's contention was that it was neither **convenient nor equitable** that his estate be sequestrated in this country (South Africa) and that the applicant should have sought relief in a court in Germany. In support of this contention, the first respondent referred to section 149(1)(a) of the *Insolvency Act*¹²⁵ stating that the court shall have jurisdiction under this Act over every debtor and in regard to the estate of every debtor who owns or is entitled to property situated within the jurisdiction of this court. This provision is however subject to the qualification that when it appears to the court **equitable or convenient** that the estate of a person not domiciled in South Africa should be sequestrated elsewhere, the court may refuse or postpone the sequestration. The first respondent contended that it would be inconvenient and inequitable for himself to come to South Africa for the sequestration proceedings, as well as for his creditors having to come to South Africa to attend creditors meetings.

The court then held that any inconvenience or inequity caused by the grant of a provisional order in the South African court far outweighed the convenience of dealing with immovable property in this country. The court then stated that:

When considering the question of convenience, what matters is not the convenience of the courts but what happens after the order is granted.

The court held that the only asset the first respondent owned was the immovable property situated in Plettenberg Bay. It was surely more convenient that the matter be adjudicated in this court, especially **regarding the enforceability and execution of the order**. Even if an application was

125 24 of 1936.

brought in a German court and an order be granted, it would not in itself divest the first respondent of its immovable property in Plettenberg Bay.

Hence, comity, convenience and equity are not synonymous. Comity refers to the willingness of courts to cooperate with other states and to accept the legislative, executive and judicial acts of that nation, but also implies a balancing of interests. This is an aspect that is not always mentioned together with comity. Convenience, as a consideration to determine the most appropriate forum where a dispute should be heard, takes into account the administration of the sequestrated estate and the ability of a court to enforce and execute the order that it has made. Equity, then, refers to the equal treatment of creditors by taking into account the preferential rights that already exist for the various creditors in insolvency matters.

3.2 The South African Cross-Border Insolvency Act 42 of 2000

As mentioned above, the CBA only applies where a state has been designated by the Minister of Justice in the *Government Gazette*. The CBA has a certain scope of application as set out in section 2(1). The Act applies in the following four situations:

- Where a foreign court or representative seeks South African assistance in a foreign proceeding (also known as an inward-bound request)¹²⁶ or, conversely;
- Where such assistance is requested in a foreign court in proceedings under the law of the Republic relating to insolvency (this is also referred to as local proceedings or outward-bound request);¹²⁷
- Where a foreign and local insolvency proceeding run concurrently in respect of the same debtor; or
- Where creditors or a foreign representative ask to begin or take part in a South African insolvency proceeding.

126 Smith and Boraine 2002 *ABI Law Review* 190.

127 Assistance is then requested from the foreign court and is referred to as an outward-bound request.

From this section it is clear that the CBA will apply to cross-border insolvency matters in relation to inward-bound requests, outward-bound requests and even to concurrent proceedings running in two different states at the same time concerning the same debtor. The designation of states by the Minister seems to be restricted by the requirement of **reciprocity**. Currently the Minister has not designated any states yet and the Act, even though in force,¹²⁸ still does not take effect. A dualistic approach seems to be inevitable for the time being until the Minister has designated some states. Where no such state has been designated, the common law will still regulate the cross-border insolvency matter. For the purpose of this paper, that mainly focuses on the problem of jurisdiction in cross-border insolvency matters, a further discussion of the CBA will not be necessary.¹²⁹ Currently the South African law on cross-border insolvencies follow a dualistic approach: Until the Minister of Justice designates certain states and the CBA comes into force, the common law principles will regulate these proceedings. Many problems however still occur in cross-border insolvency cases. Among these are the establishment of jurisdiction; the problems with different insolvency models, for instance a universal model *versus* a territorial model; forum shopping that especially, as we have seen, increasingly features in first world countries; the determination of COMI; and especially in a South African context, the requirement of reciprocity and designation. Therefore, until these issues are addressed, the application of cross-border insolvency protocols might be an effective interim solution.

3.2.1 *Reciprocity*

The requirement of reciprocity with the designation of states is one aspect where the CBA differs greatly from the Model Law. A designation may only be made if the Minister of Justice is satisfied that the recognition accorded by a foreign state to proceedings under the South African law of insolvency is such that it justifies the application of the CBA to foreign proceedings in such

128 The Act has been in force since 28 Nov 2003.

129 For a detailed discussion of the Act, see Meskin *Insolvency Law* 17-1 and Smith and Boraine 2002 *ABI Law Review* 186-215.

states.¹³⁰ In other words, where state A sufficiently recognizes South African insolvency law and undertakes to give effect to it, the Minister of Justice will designate that state.¹³¹ This enables state A to utilise all the benefits and assistance that the CBA provides when conducting proceedings in relation to local assets. In such circumstances both trustees in local proceedings seeking foreign assistance, and foreign trustees seeking local assistance can be assured of clear regulation by the CBA and the necessary reciprocal assistance when dealing with assets situated in the foreign state. The limited application of the Model Law under article 1(2) is much less restrictive than the CBA. Excluding only specialised institutions from its application, the Model Law differs from the CBA that excludes whole legal systems from its application.¹³² This is the biggest problem across the globe because most states operate in the same way as South Africa. This makes the aspect of “reciprocity” one of the biggest stumbling blocks in dealing with cross-border insolvencies. In my opinion this could very well be a consequence of the widespread acceptance of territorialism as an insolvency model.

130 *Meskin Insolvency Law* 17-16.

131 It is unclear in what form this undertaking will be embodied. A cross-border insolvency protocol could also play a part here.

132 *Meskin Insolvency Law* 17-15.

4. Cross-border insolvency protocols

Cross-border insolvency protocols are legal arrangements between two or more courts¹³³ in different jurisdictions, governing the way in which assets in the different countries will be dealt with.¹³⁴ Generally protocols determine the procedure whereby courts of the different jurisdictions will co-ordinate their proceedings. A possible definition of cross-border insolvency protocols could be:

To provide a case-specific structure to govern how parties to an international insolvency communicate, take actions and apply the procedural and substantive elements of the law.¹³⁵

Therefore the function of the protocol is not to establish jurisdiction through agreement between the two foreign courts. It rather functions as a legal instrument that provides procedures for the effective administration of assets between two foreign courts and this protocol arrangement could be based on the jurisdiction the High Court has in terms of section 25 of the CBA. S 25 of the CBA makes provision for the co-operation and direct communication between local courts and the foreign courts. Cross-border insolvency protocols have also been described as “mini treaties” between two foreign courts.¹³⁶ The majority of cases in which cross-border insolvency protocols are implemented occurs between courts of the US and Canada. Unlike the universal approach with its single or main forum conducting the proceedings, here both the US and Canadian courts hear the proceedings instituted in their respective jurisdictions in relation to the assets located within its jurisdiction of the same multinational corporation.¹³⁷ The protocol is the means used to co-

133 The South African court must be a “competent court” in terms of s 4 of the Act. For the purpose of co-operation with foreign courts any High Court referred to in section 166(c) of the *Constitution of the Republic of South Africa*, 1996 will be such a court, as long as the general jurisdictional provisions are complied with in every individual case.

134 El-Boraie 2005 HYPERLINK
<http://www.heinonline.org> 31 Jul 2006.

135 El-Boraie 2005 HYPERLINK
<http://www.heinonline.org> 31 Jul 2006.

136 Fitz-James 2002 HYPERLINK
<http://www.gtlaw.com/pub/media/2002/leshawj02a.pdf> 1 Aug 2006.

137 This leans toward the territorial approach, but with a definite undertaking between the courts to co-operate, so to benefit the creditors.

ordinate both these proceedings to reduce the loss of time and to increase the benefit of creditors. The purpose of the protocol could broadly be said to be the following: To honour the sovereignty and integrity of both courts; to synchronize and coordinate the activities in multinational insolvencies; to effectively administer the multinational insolvency so that costs could be reduced and double efforts be prevented; to advance co-operation between foreign courts and promote comity; to facilitate the insolvency proceedings in such a manner that creditors would benefit from the open administration of the proceedings and lastly, to provide a general structure of principles to deal with administrative issues arising from the cross-border insolvency.¹³⁸ Hence, it is clear that the use of a protocol could especially be effective in cross-border insolvency cases, where problems of this nature frequently arise. Of special importance here is the fact that it excludes forum-shopping (which preconceives the benefit of others).

4.1 The implementation of insolvency protocols

The successful implementation of insolvency protocols rely heavily on a mutual judicial desire to co-operate, harmonize proceedings and where necessary even to defer to the order of another court.¹³⁹ Courts could often shy away from implementing a protocol for the fear of the restriction of their sovereignty and jurisdiction. This is a sensitive issue especially relating to substantial and procedural matters. Therefore it is of great importance that insolvency protocols make provision for clear guidelines with regard to the integrity of courts and their role in co-operation. In 1995 the International Bar Association approved the Cross-Border Insolvency Concordat (hereafter the Concordat).¹⁴⁰ This Concordat is a set of guidelines of general principles which could be adopted by parties to address their specific circumstances when drafting a protocol.¹⁴¹ Usually the general key players to an insolvency

138 Tay 1999 HYPERLINK
<http://www.insol.org> 20 June 2006.

139 Tay 1999 HYPERLINK
<http://www.insol.org> 20 June 2006.

140 Farley 1997 HYPERLINK
<http://www.insol.org> 20 June 2006.

141 Farley 1997 HYPERLINK

draw up a draft protocol, have the parties agree to it and then present it to the different courts for approval. In the earlier cases¹⁴² where insolvency protocols were implemented the debtor and key creditors were all signatories to the protocol indicating their consent to the terms thereof.¹⁴³ In the most recent cases, however, the parties to the proceedings were not signatories of the protocol. This is because the protocol is an order of the court, binding upon all the parties to the proceedings.¹⁴⁴ It is usually the debtor that proposes the incorporation of a protocol to assure the orderly implementation of the plan of arrangement.¹⁴⁵ At first the implementation of protocols only occurred in the later stages of the proceedings, but ever since the *Loewen* case¹⁴⁶ protocols have been incorporated in the first day orders of the various courts involved in the restructuring proceedings.¹⁴⁷ For the protocol to be effective both courts have to approve it in identical form. Should either court want to effect changes to the protocol, this would be possible by accepting an interim protocol with both courts proposing amendments thereto.¹⁴⁸ On agreement of the amendments and proposed changes the protocol can then be approved by both of the courts.

4.2 Key elements of cross-border insolvency protocols

<http://www.insol.org> 20 June 2006.

142 In *Re Everfresh Beverages Inc.* between the Ontario Court of Justice, Toronto. 32-077978 1995 and United States Bankruptcy Court for the Southern District of New York 95 B 45405 1995; *Cross-Border Insolvency Protocol in Re Olympia & York Developments Limited* between Ontario Court of Justice, Toronto B125/92 1993 and United States Bankruptcy Court for the Southern District of New York 92-B-42698-42701 1993.

143 Tay 1999 HYPERLINK
<http://www.insol.org> 20 June 2006.

144 Tay 1999 HYPERLINK
<http://www.insol.org> 20 June 2006.

145 Tay 1999 HYPERLINK
<http://www.insol.org> 20 June 2006.

146 *Cross-Border Insolvency Protocol in Re Loewen Group* between United States Bankruptcy Court for the District of Delaware 99-1244 1999 and Ontario Superior Court of Justice, Toronto 99-CL-3384 1999.

147 In the *Loewen* case the Canadian court incorporated the protocol as a term of its first day order under the *Companies' Creditors Arrangement Act* R.S. 1985 C-36 (CCAA), as well as the US court under the *US Bankruptcy Code Chapter 11* proceedings.

148 Tay 1999 HYPERLINK
<http://www.insol.org> 20 June 2006.

The key elements of an insolvency protocol will briefly be discussed with reference to the case of *360Networks Inc and Its affiliated Companies*¹⁴⁹ (hereafter the *360Networks Protocol*).¹⁵⁰ In this case insolvency proceedings were instituted in both the US and Canadian courts. The implementation of a protocol to co-ordinate proceedings was used.

4.2.1 Case information

The first few articles of the protocol provide a summary of the state of affairs up to the point where the courts have to approve the protocol. This includes a description of the debtor, its principal place of business and the different jurisdictions in which insolvency proceedings have been instituted.¹⁵¹

4.2.2 Purpose and goals

The main purpose of the protocol is the implementation of basic administrative procedures to coordinate certain activities of the proceedings, to protect the rights of parties involved and maintain the court's independent jurisdiction while the insolvency proceedings are pending in the various courts (in this instance the US and Canadian courts).¹⁵² It further states the specific desires and goals both courts mutually agree to promote.¹⁵³

4.2.3 Comity and the independence of the courts

This section of the protocol emphasizes the absolute sovereignty of the various courts involved, stating that the implementation of the protocol shall not divest nor diminish the various courts' independent jurisdiction over the

149 *360Networks Inc* between British Columbia Supreme Court, Vancouver L011792 2001 and United States Bankruptcy Court for the Southern District of New York 01-13721 2001.

150 *360Networks Protocol* HYPERLINK
<http://www.iiiglobal.org> 3 Aug 2006.

151 A 1 to 5 of the *360Networks Protocol*.

152 A 6 of the *360Networks Protocol*.

153 See par 3 above for the specific goals and desires the courts want to promote.

subject matter in their respective proceedings.¹⁵⁴ Article 8 of the *360Networks Protocol* states that:

The US Court shall have sole and exclusive jurisdiction and power over the conduct and hearing of the US proceedings. The Canadian Court shall have sole and exclusive jurisdiction and power over the conduct and hearing of the Canadian proceedings.

Both courts therefore retain their exclusive jurisdiction and power over their local insolvency proceedings. This approach closely relates to the territorial approach as discussed above. From this the inference could be drawn that the substantive law of each state will be applied to the assets located within its jurisdiction.¹⁵⁵ Where this law is in conflict with the substantive law of the other state, the protocol could set out procedures to deal with it effectively. The implementation of insolvency protocols therefore does not require courts to abandon their exclusive jurisdiction. This makes the use of protocols more acceptable for the majority of states.

4.2.4 Co-operation

Both courts involved in the insolvency proceedings undertake to use its best efforts to coordinate their activities and even defer to the judgement of the other court where it is appropriate and feasible.¹⁵⁶ The courts further undertake to communicate with one another in respect to any matter relating to the insolvency proceedings and may also conduct joint hearings where they deem it to be necessary or advisable. The protocol contains specific provisions for the conducting of joint hearings, which include *inter alia* the means of communication to be used, the procedure for filing written evidential materials, submissions and applications and direct communication between the judges of the respective courts.¹⁵⁷ The *360Networks Protocol* makes provision that the communication to be used in joint hearings between the two

154 A 7 of the *360Networks Protocol*.

155 In other words, the domicile of the movable and immovable assets.

156 A 12 of the *360Networks Protocol*.

157 *360Networks Protocol* HYPERLINK

<http://www.iiiglobal.org> 3 Aug 2006.

courts should be by means of telephone or video link.¹⁵⁸ In a recent international insolvency case, the *Livenet* case,¹⁵⁹ the courts communicated by means of a satellite television feed.¹⁶⁰ The multi camera setup in the courtroom enabled everyone in each court to see both the judge and the council making submissions in the other country.¹⁶¹ During the proceedings the judges of both countries interrogated the counsel in the other and on occasion, the council in one country cross-examined a witness in the other by means of television. This hearing successfully concluded within two days with both courts making complimentary orders, which allowed the sale of assets situated in both countries to a single purchaser.¹⁶² It is argued that the vehicle of communication need not be limited to telephone and video lines, but that simpler means of communication for example fax or e-mail could also be sufficient.¹⁶³ The measure of cooperation between the courts is however still subject to their independence. Article 13 of the *360Networks Protocol* states that:

Although the Courts will seek to cooperate and coordinate with each other in good faith, each of the Courts shall be entitled at all times to exercise its independent jurisdiction and authority with respect to: (a) matters presented to such Court; and (b) the conduct of the parties appearing in such matters.

From this provision it is clear that courts need not fear a restriction of their independent jurisdiction. Although cooperation is encouraged and required for the successful implementation of a protocol, it is not an unqualified obligation upon a court.

158 A 12(a) of the *360Networks Protocol*.

159 *Re Livent Inc.* between United States Bankruptcy Court for the Southern District of New York 98-B-48312, and Ontario Superior Court of Justice, Toronto 98-CL-3162 1999.

160 Leonard 1999 HYPERLINK
<http://www.heinonline.org> 3 Aug 2006.

161 Leonard 1999 HYPERLINK
<http://www.heinonline.org> 3 Aug 2006.

162 Leonard 1999 HYPERLINK
<http://www.heinonline.org> 3 Aug 2006.

163 Farley 1997 HYPERLINK
<http://www.insol.org> 20 June 2006. In 2000 the American Law Institute adopted a document called "Guidelines Applicable to Court-To-Court Communication in Cross-Border Cases".

4.2.5 Further key elements

The *360Networks Protocol* further provides for the rights of parties to appear and be heard before the appropriate court;¹⁶⁴ procedures with regard to notice of any motion, application or pleadings;¹⁶⁵ joint recognition of stays of proceedings of the various courts;¹⁶⁶ procedures for dispute resolution under the protocol¹⁶⁷ and the preservation of rights.¹⁶⁸ Neither the terms of the protocol nor any action taken in accordance with the protocol will affect the **rights**, powers, claims and defences of the entity in distress or the **creditors** of the insolvent entity.¹⁶⁹ It therefore seems as if the preference of creditors remains the same while the pool of concurrent creditors is enlarged.

It is almost six years since the *Cross-Border Insolvency Act* was adopted and still it remains without force. This is simply because no states have been designated yet. Cross-Border insolvency protocols could play an important role in this interim time where the CBA is adopted but not in force yet. A cross-border insolvency protocol between a South African court and a foreign court could be drafted on the principles contained in the CBA. It could serve as a guideline for the proceedings under the protocol, relieving its drafters of the burden to take note of unknown procedural principles. In effect a protocol could indirectly enforce the principles already contained in South African cross-border insolvency legislation until the CBA comes into full operation.

164 A 20 of the *360Networks Protocol*.

165 A 21 of the *360Networks Protocol*.

166 A 22 of the *360Networks Protocol*.

167 A 27 of the *360Networks Protocol*.

168 A 32, 33 and 34 of the *360Networks Protocol*.

169 A 32 of the *360Networks Protocol*.

5. Conclusion

Many problems still occur in cross-border insolvency cases. Among these are the establishment of jurisdiction; the problems with different cross-border insolvency models, for instance a universal model *versus* a territorial model; forum shopping that especially, as have been seen, increasingly features in first world countries; the determination of COMI; and in a South African context, the requirement of reciprocity and designation.

Cross-border insolvency law is by no means unified. Great differences exist and the fundamental approaches states follow vary greatly. When dealing with cross-border insolvencies, states usually follow one of two approaches, either a universal or a territorial approach. When following the territorial approach, jurisdictions seek to protect local creditors and their interests before foreign creditors are allowed to utilise the property for their benefit. On the other hand, the universal approach treats the cross-border insolvency as a single matter to ensure equal treatment to creditors from the different jurisdictions. In reply to the shortcomings of the traditional territorial approach, a co-operative territorialist model has been proposed. With this model each court, both local and foreign, would appoint a representative. Where co-operation is then needed the representatives of the different jurisdictions may enter into agreement to regulate certain aspects of the proceedings, although it is not compulsory. Entering into such an agreement increases the distribution of the debtor's assets which leads to greater equality among creditors. Such an agreement could also prevent the dominance of one jurisdiction in the determination of priority rights of creditors and the distribution of assets among them. The problem unfortunately remains unsolved where the representatives of the different jurisdictions fail to reach an agreement.

Because of the inefficiency of the pure form of universalism a modified version has also been developed. Under the modified universalism approach the local courts have a degree of freedom to decide whether to comply with the requests of the governing jurisdiction or not. It has been suggested that the legal standard for compliance might be that the position of local creditors

should not be affected and public policy not offended. This means that the assets should be distributed according to the law of the local courts, with foreign courts only having such distribution power with the express consent of the local courts. To my mind this position is hardly distinguishable from the territorial approach.

Neither the territorialist nor the universalist approach provides the perfect solution to cross-border insolvency problems. Both models have their advantages, but fail to provide a workable solution to all cases. A mid-way between the two extremes of universalism and territorialism could provide an interim solution. The use of cross-border insolvency protocols could provide that interim solution. With the co-operative territorial approach, each of the courts could appoint a representative, which may enter into agreements with each other to regulate certain procedural aspects. The only problem with this approach is that it is not compulsory for courts to enter into such a co-operation agreement, which leaves the possibility that courts could refuse to give their co-operation. Where courts enter into a cross-border insolvency protocol on the other hand, co-operation is compulsory as this is the essence of the protocol. With a modified universalism approach the local courts have a degree of freedom to decide whether to comply with the requests of foreign courts. The assets will therefore be distributed according to the law of the local courts, with foreign courts only having such distribution power with the express consent of local courts. Here again, the local court is in no way obliged to co-operate with the foreign jurisdiction, retaining the power not to co-operate. As with the co-operative territorial approach, this also leaves the parties to cross-border insolvencies without any guarantee of foreign co-operation.

The problems with the determination of the most appropriate forum where insolvency should be heard together with the increasing danger of forum shopping only increase jurisdictional uncertainty in cross-border insolvencies. In the absence of universal choice-of-law rules appointing the appropriate forum, states have to look at their different domestic laws for guidance in this matter. The place of incorporation, the place where a corporation has its

registered office or the place where the corporation has its centre of main interests is usually used to determine the main forum. These standards are vague and provide problems in practical situations, especially where multinational corporations are involved. Where the parent company of a multinational corporation has its registered office in one state, and all the subsidiaries have registered offices in other states, how is the centre of main interest determined, especially where only a very small part of the multinational corporations' business is carried out at the place where the parent company is located? Would the main forum be the one where the parent company operates the subsidiaries, or the country where a subsidiary is incorporated and has the majority of its operations and assets? This could lead to a possible distinction between the administrative and operational functions of a multinational company to determine its centre of main interest.

In the Yukos case, for example, four different courts were involved in the collection of debt at different times, each court being the specific choice of a certain claimant to best serve his own interests. The Bank Group approached an English court, a Dutch court and a Russian court. Moravel and the Russian Government also approached the Dutch court. Finally the monitor of the Yukos insolvency proceedings approached the Dutch and US courts. In between the court proceedings many arbitration awards were also made. This creates great unpredictability **and shows that in practice neither the territorialist nor the universalist approach has the perfect answer to combat forum shopping.**

A further problem that stimulates forum-shopping is that cross-border insolvencies involve many parties and their interests. These interests not only include those of the debtor and the creditors, but also the interests of courts and lawyers to have a dispute heard in a specific forum. The legal fee's of big insolvency cases reach very high amounts and is normally paid to attorneys in the city where the proceedings are held. **This provides enough reason for bankruptcy courts to compete for big cases.** It is also argued that courts could and do adopt legal positions and practices that favour the parties who choose the forum in bankruptcy cases. It is very clear that the phenomenon of

forum-shopping is undesired, as it does not have the interest of the insolvent estate as its primary focus.

The South African *Cross-Border Insolvency Act* which came into force on the 28th of November 2003 is not in operation yet since its application is dependent on the designation of certain states, and as no states have been designated yet, cross-border insolvencies continue to be governed by the common law. Where the goods of the insolvent estate consists of movable goods, the general rule is that "it is subject to the same law as that which governs the person of the owner, in other words, the law of his domicile". An order granted by the court of the insolvent's foreign domicile (*lex domicilii*) automatically divests such a person of his or her movables in South Africa, creating a single *concursum creditorum*. This principle therefore supports the universalist approach. Although the movable property is deemed to be owned by the foreign trustee, the foreign order still needs to be given effect to under the South African law. The foreign trustee's ownership of the movable property is therefore not unlimited. Courts might impose certain conditions with which the trustee should comply before being allowed to remove the property from the jurisdiction. Usually this condition consists of the protection of the local preference of local creditors. With immovable property the law of the location of the property (the *lex situs* or the *lex rei sitae*) is decisive. The effect of the foreign sequestration order is therefore limited territorially. Before a representative will be allowed to deal with local immovable property, he must first approach the South African court for recognition of his appointment. Recently in *Ward v Smith: in re Gurr v Zambia Airways Corporation Ltd* it was made clear that the formal recognition of foreign trustees should always be applied for in local courts, irrespective of the assets being movable, immovable, or whether the assets belong to an individual or a company. The South African courts exercise their discretion when hearing such an application, based on comity, convenience and equity.

In my view comity could be defined as the recognition by country A of the legislative, executive and judicial acts of country B. The word "recognition" means that it is acceptable to country A, but only after considering the rights of

the citizens of country A in the specific case. Thus, comity as a consideration for the granting of a recognition order in cross-border insolvency proceedings **has to be balanced with** the protection of local stakeholders' interests. Comity, convenience and equity are not synonymous. Comity refers to the willingness of courts to cooperate with other states and to accept the legislative, executive and judicial acts of that nation, but also implies a balance of interests. This is an aspect that is not always mentioned with comity. Convenience, as a consideration to determine the most appropriate forum where a dispute should be heard, takes into account the administration of the sequestrated estate and the ability of a court to enforce and execute the order that it has made. Equity refers to the equal treatment of creditors by taking into account the preferential rights that already exist for the various creditors in insolvency matters.

The requirement of reciprocity in cross-border insolvencies, especially in South Africa where the CBA will only apply with the designation of states, makes this one of the biggest stumbling blocks in dealing with cross-border insolvencies. Unfortunately this problem is not isolated to South Africa, as most states across the globe operate in the same way as South Africa, requiring reciprocity. In my opinion this could very well be a consequence of the widespread acceptance of territorialism as an insolvency model. Considering all the hindrances to an effective and unified international cross-border insolvency system, the application of cross-border insolvency protocols might be an effective interim solution in South Africa.

Cross-border insolvency protocols are legal arrangements between two or more courts in different jurisdictions, governing the way in which assets in the different countries will be dealt with. The South African court must be a "competent court" in terms of section 4 of the CBA. For the purpose of co-operation with foreign courts any High Court referred to in section 166(c) of the *Constitution of the Republic of South Africa, 1996* will be a competent court, as long as the general jurisdictional provisions are complied with in every individual case. The function of the protocol is not to establish jurisdiction through agreement between the two foreign courts. It rather

functions as a legal instrument that provides procedures for the effective administration of assets between two foreign courts, based on the jurisdiction that the High Court has in terms of section 25 of the Act. Both courts retain their exclusive jurisdiction and power over their local insolvency proceedings. The implementation of insolvency protocols therefore does not require courts to abandon their exclusive jurisdiction, which makes the use of protocols more acceptable to the majority of states. This closely relates to the territorial approach as discussed above. The substantive law of each state will be applied to the assets located within its jurisdiction and where this law is in conflict with the substantive law of the other state, the protocol could set out procedures to effectively deal with it.

Cross-Border insolvency protocols could play an important role in this interim time where the CBA is adopted but not in force yet. Because of the requirement of reciprocity it might also take a long time still before it comes into operation. A cross-border insolvency protocol between a South African court and a foreign court could be drafted on the principles contained in the CBA. It could serve as a guideline for the proceedings under the protocol, relieving its drafters of the burden to take note of unknown procedural principles. In effect a protocol could indirectly enforce the principles already contained in South African cross-border insolvency legislation.

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APPENDIX A

**CROSS-BORDER INSOLVENCY PROTOCOL
FOR 360NETWORKS INC. AND ITS AFFILIATED COMPANIES**

1. Certain defined terms used in this Protocol shall have the meanings assigned to them in Appendix "A".
2. The 360 Group has developed this Protocol which when approved by the Canadian Court and the U.S. Court shall govern the conduct of all parties in interest in the Insolvency Proceedings.
3. The Parent is a Nova Scotia company extra provincially registered in British Columbia and is the ultimate parent company of an enterprise that operates through its various subsidiaries and affiliates, in Canada, the United States and various other countries throughout the world.
4. The Parent and the 360 Canada Group have commenced the Canadian Proceedings by filing an application under the applicable provisions of the *Companies' Creditors Arrangement Act* in the British Columbia Supreme Court. The Parent and the 360 Canada Group have sought the CCAA Order pursuant to which:
 - (a) the Parent and the 360 Canada Group have been determined to be entities to which the CCAA applies, all proceedings in Canada have been stayed as against them and they have been authorized to continue reorganization steps under the CCAA; and
 - (b) the Monitor was appointed as monitor of the Parent and the 360 Canada Group, with the rights, powers, duties and limitations upon liabilities set forth in the CCAA Order.
5. The 360 US Group have commenced the U.S. Proceedings under chapter 11 of the United States Bankruptcy Code, 11 U.S.C. § 101-1330 in the United States Bankruptcy Court for the Southern District of New York. The members of the 360 U.S. Group are continuing in possession of their respective properties managing their respective businesses as debtors in possession, pursuant to sections 1107 and 1108 of the Bankruptcy Code. The U.S. Trustee has not yet appointed any official U.S. Committee in the U.S. Proceedings.

Purpose and Goals

6. While the Insolvency Proceedings are pending in Canada, the United States and elsewhere for the 360 Group, the implementation of basic administrative procedures is necessary to coordinate certain activities in the Insolvency Proceedings, protect the rights of parties thereto and ensure the maintenance of the Court's independent jurisdiction and comity. Accordingly, this Protocol has been developed to promote the following mutually desirable goals and

objectives in both the U.S. Proceedings and the Canadian Proceedings and, to any extent necessary, the Foreign Proceedings:

- (a) harmonize and coordinate activities in the Insolvency Proceedings before the Canadian Court, the U.S. Court and any foreign court;
- (b) promote the orderly and efficient administration of the Insolvency Proceedings to, among other things, maximize the efficiency of the Insolvency Proceedings, reduce the costs associated therewith and avoid duplication of effort;
- (c) honour the independence and integrity of the Courts and other courts and tribunals of Canada, the United States or other countries;
- (d) promote international cooperation and respect for comity among the Courts, the 360 Group, the Committees, the Estate Representatives and other creditors and interested parties in the Insolvency Proceedings;
- (e) facilitate the fair, open and efficient administration of the Insolvency Proceedings for the benefit of all of the creditors of the 360 Group and other interested parties, wherever located; and
- (f) implement a framework of general principles to address basic administrative issues arising out of the cross-border and international nature of the Insolvency Proceedings.

Comity and Independence of the Courts

7. The approval and implementation of this Protocol shall not divest or diminish the U.S. Court's and the Canadian Court's independent jurisdiction over the subject matter of the U.S. Proceedings and the Canadian Proceedings, respectively. By approving and implementing this Protocol, neither the U.S. Court, the Canadian Court, the 360 Group nor any creditors or interested parties shall be deemed to have approved or engaged in any infringement on the sovereignty of the United States or Canada.

8. The U.S. Court shall have sole and exclusive jurisdiction and power over the conduct and hearing of the U.S. Proceedings. The Canadian Court shall have sole and exclusive jurisdiction and power over the conduct and hearing of the Canadian Proceedings.

9. In accordance with the principles of comity and independence established in the two preceding paragraphs, nothing contained herein shall be construed to:

- (a) increase, decrease or otherwise modify the independence, sovereignty or jurisdiction of the U.S. Court, the Canadian Court or any other court or tribunal in the United States or Canada, including the ability of any such court or tribunal to provide appropriate relief under applicable law on an ex parte or "limited notice" basis;

- (b) require the 360 Group, the Committee or the Estate Representatives to take any action or refrain from taking any action that would result in a breach of any duty imposed on them by any applicable law;
- (c) authorize any action that requires the specific approval of one or both of the Courts under the Bankruptcy Code or the CCAA after appropriate notice and a hearing (except to the extent that such action is specifically described in this Protocol); or
- (d) preclude any creditor or other interested party from asserting such party's substantive rights under the applicable laws of the United States, Canada or any other jurisdiction including, without limitation, the rights of interested parties or affected persons to appeal from the decisions taken by one or both of the Courts.

10. The 360 Group, the Committee, the Estate Representatives and their respective employees, members, agents and professionals shall respect and comply with the independent, non-delegable duties imposed upon them by the Bankruptcy Code, the CCAA, the CCAA Order and other applicable laws.

Cooperation

11. To assist in the efficient administration of the Insolvency Proceedings, the 360 Group, the Committee and the Estate Representatives shall:

- (a) reasonably cooperate with each other in connection with actions taken in both the U.S. Court and the Canadian Court; and
- (b) take any other reasonable steps to coordinate the administration of the U.S. Proceedings and the Canadian Proceedings for the benefit of the 360 Group's respective estates and stakeholders.

12. To harmonize and coordinate the administration of the Insolvency Proceedings, the U.S. Court and the Canadian Court each shall use its best efforts to coordinate activities with and defer to the judgment of the other Court, where appropriate and feasible. The U.S. Court and the Canadian Court may communicate with one another with respect to any matter relating to the Insolvency Proceedings and may conduct joint hearings with respect to any matter relating to the conduct, administration, determination or disposition of any aspect of the U.S. Proceedings and the Canadian Proceedings, in circumstances where both Courts consider such joint hearings to be necessary or advisable and, in particular, to facilitate or coordinate with the proper and efficient conduct of the U.S. Proceedings and the Canadian Proceedings. With respect to any such hearing, unless otherwise ordered, the following procedures will be followed:

- (a) a telephone or video link shall be established so that both the U.S. Court and the Canadian Court shall be able to simultaneously hear the proceedings in the other Court;

- (b) any party intending to rely on any written evidentiary materials in support of a submission to the U.S. Court or the Canadian Court in connection with any joint hearing shall file such materials, which shall be identical insofar as possible and shall be consistent with the procedure and evidentiary rules and requirements of each Court, in advance of the time of such hearing or the submissions of such application. If a party has not previously appeared in or attorned or does not wish to attorn to the jurisdiction of either court, it shall be entitled to file such materials without, by the act of filing, being deemed to have attorned to the jurisdiction of the Court in which such material is filed, so long as it does not request in its materials or submissions any affirmative relief from the Court to which it does not wish to attorn;
- (c) submissions or applications by any party shall be made only to the Court in which such party is appearing, unless specifically given leave by the other Court to make submissions or applications to it;
- (d) the Judge of the U.S. Court and the Justice of the Canadian Court who will hear any such application shall be entitled to communicate with each other in advance of the hearing on the application, with or without counsel being present, to establish guidelines for the orderly submission of pleadings, papers and other materials and the rendering of decisions by the U.S. Court and the Canadian Court, and to deal with any related procedural, administrative or preliminary matters; and
- (e) the Judge of the U.S. Court and the Justice of the Canadian Court, having heard any such application, shall be entitled to communicate with each other after the hearing on such application, without counsel present, for the purpose of determining whether consistent rulings can be made by both Courts, and the terms upon which such rulings shall be made, as well as to address any other procedural or non-substantive matter relating to such applications.

13. Notwithstanding the terms of the preceding paragraph, the Protocol recognizes that the U.S. Court and the Canadian Court are independent courts. Accordingly, although the Courts will seek to cooperate and coordinate with each other in good faith, each of the Courts shall be entitled at all times to exercise its independent jurisdiction and authority with respect to:

- (a) matters presented to such Court; and
- (b) the conduct of the parties appearing in such matters.

Retention and Compensation of Estate Representatives and Professionals

14. The Monitor, the Affiliated Professionals, the Canadian Representatives and Canadian Professionals appointed in the Canadian Proceedings shall all be subject to the sole and exclusive jurisdiction of the Canadian Court with respect all matters, including:

- (a) their tenure in office;
- (b) their retention and compensation;
- (c) their liability, if any, to any person or entity, including the 360 Canada Group and any third parties, in connection with the Insolvency Proceedings; and
- (d) the hearing and determination of any matters relating to them arising in the Canadian Proceedings under the CCAA or other applicable Canadian law.

15. The Monitor, Affiliated Professionals, Canadian Representatives and Canadian Professionals shall not be required to seek approval of their retention in the U.S. Court. Additionally, the Monitor, Affiliated Professionals, Canadian Representatives and Canadian Professionals:

- (a) shall be compensated for their services solely in accordance with the CCAA and other applicable Canadian law or orders of the Canadian Court; and
- (b) shall not be required to seek approval of their compensation in the U.S. Court.

16. The Monitor and any Affiliated Professionals and their officers, directors, employees, counsel and agents, wherever located, shall be entitled to the same protections and immunities in the United States as those granted to them under the CCAA Order. In particular, except as otherwise provided in any subsequent order entered in the Canadian Proceedings, the Monitor and its Affiliated Professionals shall incur no liability or obligations as a result of the CCAA Order, the appointment of the Monitor or carrying out of the provisions of the CCAA Order by the Monitor or its Affiliated Professionals, except any such liability arising from actions of the Monitor or its Affiliated Professionals constituting gross negligence or willful misconduct.

17. Any U.S. Representative appointed in the U.S. Proceedings and any examiner or trustee appointed in accordance with section 1104 of the Bankruptcy Code, shall be subject to the sole and exclusive jurisdiction of the U.S. Court with respect to all matters, including:

- (a) their tenure in office;
- (b) their retention and compensation;

- (c) their liability, if any, to any person or entity, including the 360 U.S. Group and any third parties, in connection with the Insolvency Proceedings; and
- (d) the hearing and determination of any other matters relating to them arising in the U.S. Proceedings under the Bankruptcy Code or other applicable laws of the United States.

18. The U.S. Representatives shall not be required to seek approval of their retention in the Canadian Court. Additionally, the U.S. Representatives:

- (a) shall be compensated for their services solely in accordance with the Bankruptcy Code and other applicable laws of the United States or orders of the U.S. Court; and
- (b) shall not be required to seek approval of their compensation in the Canadian Court.

19. Nothing in this Protocol shall be deemed to subject the Monitor to the jurisdiction of the U.S. Court or any court in the United States. To the extent that the Monitor may from time to time utilize the services and expertise of Affiliated Professionals in performing its role as monitor in the Canadian Proceedings, those Affiliated Professionals may include employees of, partners in or other individual affiliated with the Monitor in any jurisdiction including the United States. All services provided by such Affiliated Professionals in connection with the provision of monitoring services to the 360 Group, including services provided by individuals affiliated with the Monitor, shall be billed to the 360 Canada Group by and through the Monitor and shall be subject to the procedures and standards for review and approval of compensation applicable in the Canadian Court under the CCAA, the CCAA Order and any other applicable Canadian law or orders of the Canadian Court, and shall be subject to review and approval solely by the Canadian Court.

Rights to Appear and Be Heard

20. Each of the 360 Group, their creditors and other interested parties in the Insolvency Proceedings, including the Canadian Representatives and the U.S. Representatives, shall have the right and standing to:

- (a) appear and be heard in either the U.S. Court or the Canadian Court in the Insolvency Proceedings to the same extent as a creditor and other interested party domiciled in the forum country, but solely to the extent such party is a creditor or other interested party in the forum country, subject to any local rules or regulations generally applicable to all parties appearing in the forum; and
- (b) file notices of appearance or other papers with the Clerk of the U.S. Court or the Canadian Court in the Insolvency Proceedings; provided, however, that any appearance or filing may subject a creditor or interested party to the jurisdiction of the Court in which the appearance or filing occurs; provided further, that appearance by the U.S. Committee in the Canadian

Proceedings or the Canadian Committee in the U.S. Proceedings, shall not form a basis for personal jurisdiction in Canada over the members of the U.S. Committee or vice versa. Notwithstanding the foregoing, and in accordance with the policies set forth above:

- (i) the Canadian Court shall have jurisdiction over the U.S. Representatives and the U.S. Trustee solely with respect to the particular matters as to which the U.S. Representatives or the U.S. Trustee appear before the Canadian Court; and
- (ii) the U.S. Court shall have jurisdiction over the Canadian Representatives solely with respect to the particular matters as to which the Canadian Representatives appear before the U.S. Court.

Notice

21. Notice of any motion, application or other pleading or paper filed in one or both of the Insolvency Proceedings and notice of any related hearings or other proceedings mandated by applicable law in connection with the Insolvency Proceedings or the Protocol shall be given by appropriate means (including, where circumstances warrant, by courier, telecopier or other electronic forms of communication) to the following:

- (a) to creditors, including Estate Representatives, and other interested parties in accordance with the practice of the jurisdiction where the papers are filed or the proceedings are to occur; and
- (b) to the extent not otherwise entitled to receive notice under subpart (a) of this paragraph, to:
 - (i) the Parent, 1066 West Hastings Street, Vancouver, B.C., Canada, V6E 3X1, attention: Catherine McEachern, Vice-President;
 - (ii) U.S. Bankruptcy Counsel, Willkie Farr & Gallagher, 787 Seventh Avenue, New York, New York, U.S.A., 10019, attention: Alan J. Lipkin, Esq.; and
 - (iii) CCAA counsel, Fasken Martineau DuMoulin LLP, 2100 - 1075 West Georgia Street, Vancouver, B.C., V6E 3G2, Canada, attention: Michael A. Fitch, Q.C.;
 - (iv) the Monitor and its counsel, PricewaterhouseCoopers LLP, 601 West Hastings Street, Vancouver, B.C., V6B 5A5, Canada, attention: David Bowra;
 - (v) counsel to any statutory committee or any other official appointed in the U.S. Cases or the Canadian Cases; and

- (vi) the Office of the United States Trustee, 33 Whitehall Street, 21st Floor, New York, New York, U.S.A., 10004;

and such other parties as may be designated by either Court from time to time.

Joint Recognition of Stays of Proceedings Under the Bankruptcy Code and the CCAA

22. In recognition of the importance of the Canadian Stay affecting creditors of the 360 Canada Group, their directors and others, and to the extent appropriate, the U.S. Court shall extend and enforce the Canadian Stay in the United States (to the same extent such stay of proceedings and actions is applicable in Canada) to prevent adverse actions against the 360 Canada Group, their directors and the assets, rights and holdings of the 360 Canada Group in the United States. In implementing the terms of this paragraph, the U.S. Court may consult with the Canadian Court regarding:

- (a) the interpretation and application of the Canadian Stay and any orders for the Canadian Court modifying or granting relief from the Canadian Stay; and
- (b) the enforcement in the United States of the Canadian Stay.

23. In recognition of the importance of the U.S. Stay affecting creditors of the 360 U.S. Group and their assets under section 362 of the Bankruptcy Code for the benefit of the 360 Group and their respective estates and stakeholders, and to the extent appropriate, the Canadian Court shall extend and enforce the U.S. Stay in Canada (to the same extent such stay of proceedings and actions is applicable in the United States) to prevent adverse actions against the assets, rights and holdings of the 360 U.S. Group in Canada. In implementing the terms of this paragraph, the Canadian Court may consult with the U.S. Court regarding:

- (a) the interpretation and application of the U.S. Stay and any orders of the U.S. Court modifying or granting relief from the U.S. Stay; and
- (b) the enforcement in Canada of the U.S. Stay.

24. Nothing contained herein shall affect or limit the 360 Group or other parties' rights to assert the applicability or non-applicability of the U.S. Stay or the Canadian Stay to any particular proceeding, property, asset, activity or other matter, wherever pending or located.

Effectiveness; Modification

25. This Protocol shall become effective only upon its approval by both the U.S. Court and the Canadian Court.

26. This Protocol may not be supplemented, modified, terminated or replaced in any manner except by the U.S. Court and the Canadian Court. Notice of any legal proceeding to supplement, modify, terminate or replace this Protocol shall be given in accordance with the notice provision contained in this Protocol.

Procedure for Resolving Disputes Under the Protocol

27. Disputes relating to the terms, intent or application of this Protocol may be addressed by interested parties to either the U.S. Court, the Canadian Court or both Courts upon notice as set forth above. Where an issue is addressed to only one Court, in rendering a determination in any such dispute, such Court:

- (a) shall consult with the other Court; and
- (b) may, in its sole discretion, either:
 - (i) render a binding decisions after such consultation;
 - (ii) defer to the determination of the other Court by transferring the matter, in whole or in part, to the other Court; or
 - (iii) seek a joint hearing of both Courts.

28. Notwithstanding the foregoing, each Court in making a determination shall have regard to the independence, comity or inherent jurisdiction of the other Court established under existing law.

Foreign Proceedings

29. To the extent that Foreign Proceedings are initiated, all persons affected hereby shall to the greatest extent possible, and provided that all creditors in such Foreign Proceedings are treated equally irrespective of their place of domicile, implement the procedures contemplated hereby in any Foreign Proceedings and be governed to the greatest extent possible by the purpose and policies of this Protocol in dealings related to the Foreign Proceedings.

30. If the Canadian Court enters an order approving a protocol with the courts of a jurisdiction other than the U.S. Court, the U.S. Court shall honour such protocol to the extent permitted by the laws and treaties of the United States and consistent with the principles of comity and cooperation.

31. If the U.S. Court enters an order approving a protocol with the courts of a jurisdiction other than the Canadian Court, the Canadian Court shall honour such protocol to the extent permitted by the laws and treaties of Canada and consistent with the principles of comity and cooperation.

Preservation of Rights

32. Neither the terms of this Protocol nor any actions taken under the terms of this Protocol shall prejudice or affect the powers, rights, claims and defenses of the 360 Group and their estates, the Estate Representatives, the U.S. Trustee or any of the 360 Group creditors or equity holders under applicable law, including the Bankruptcy Code and the CCAA.

33. This Protocol shall be binding on and inure to the benefit of the parties hereto and their respective successors, assigns, representatives, heirs, executors, administrators, trustees (including any trustees of the 360 Group under chapters 7 or 11 of the *Bankruptcy Code*), and receivers, receiver-managers, trustees or custodians appointed under Canadian law, as the case may be.

34. Nothing contained herein shall alter the obligations of any number of the 360 U.S. Group to pay fees due under 28 U.S.C. § 1930(a)(6) based upon all disbursements made by U.S. Debtors in any jurisdictions

APPENDIX "A"

The following terms shall have the following definitions:

- (a) "Affiliated Professionals" means any person or corporation in any manner related to the Monitor who provides professional services in furtherance of the Insolvency Proceedings, the restructuring and reorganization of the 360 Group or any member thereof or who provides any professional service in the normal course of the business of any member of the 360 Group;
- (b) "Bankruptcy Code" means Title 11 of the United States Code, 11 U.S.C. § 101 et. seq.;
- (c) "Canadian Court" means the Supreme Court of British Columbia which is seized of the Canadian Proceedings and any Court which considers an appeal therefrom;
- (d) "Canadian Proceedings" shall mean those proceedings commenced under the CCAA in the Canadian Court in the Supreme Court of British Columbia, Vancouver Registry;
- (e) "Canadian Professionals" shall mean any person or corporation retained by any of the Monitor, the 360 Group, or the Canadian Committees as approved by the Court who provides services of a professional nature in furtherance of the Canadian Proceedings or the restructuring or reorganization contemplated by the Canadian Proceedings;
- (f) "Canadian Committees" shall mean any person, corporation or group appointed in the Canadian Proceedings to represent the interests of any one or more group of creditors or other interested parties;
- (g) "Canadian Representatives" shall mean the Monitor, the Affiliated Professionals, the Canadian Committees and the Canadian Professionals;
- (h) "Canadian Stay" means the stay of proceedings contained in the CCAA Order as it may be amended from time to time;
- (i) "CCAA" means the Companies' Creditors Arrangement Act R.S.C. 1985, c. C-36 as amended from time to time;
- (j) "CCAA Order" means that Order made in the Canadian Proceedings dated June 28, 2001 and any other orders or consequential orders that vary, amend or alter the CCAA Order;

- (k) "Court" means any court wherever located wherein proceedings are taken so as facilitate the object of the restructuring and reorganization of the 360 Group.
- (l) "Estate Representatives" means the U.S. Representatives and the Canadian Representatives;
- (m) "Foreign Proceedings" means any proceedings brought in countries other than the United States or Canada for the purposes of effecting a restructuring and reorganization of the business and affairs of any member of the 360 Group;
- (n) "Insolvency Proceedings" means the Canadian Proceedings and the U.S. Proceedings and any other Foreign Proceedings that may be required for the reorganization and restructuring of the 360 Group;
- (o) "Monitor" means PricewaterhouseCoopers Inc. appointed pursuant to the CCAA Order to monitor the affairs of certain members of the 360 Group;
- (p) "Parent" means 360networks inc.;
- (q) "Protocol" means this Cross-Border Insolvency Protocol as amended from time to time;
- (r) "360 Group" means those companies listed in Schedule "A" hereto and includes the Parent, 360 Canada Group and 360 U.S. Group;
- (s) "360 Canada Group" means those companies listed in Schedule A-1;
- (t) "360 U.S. Group" means those companies listed in Schedule A-2;
- (u) "U.S. Committee" means that committee appointed under the Bankruptcy Code to represent the interests of creditors or other parties in the U.S. Proceeding;
- (v) "U.S. Court" means the United States Bankruptcy Court for the Southern District of New York and any Court which hears an appeal therefrom;
- (w) "U.S. Proceeding" means that proceeding commenced in the U.S. Bankruptcy Court for the Southern District of New York by the 360 U.S. Group;
- (x) "U.S. Professional" means any person or corporation retained pursuant to Sections 327 or 1104 of the Bankruptcy Code the U.S. Proceedings;
- (y) "U.S. Representatives" means the U.S. Committee and the U.S. Professionals;

- (z) "U.S. Stay" means that automatic stay of proceedings arising in the U.S. Proceedings or that applies under the Bankruptcy Code or as may be ordered or amended by the U.S. Court; and
- (aa) "U.S. Trustee" means the United States Trustee in the U.S. Proceedings.