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DO NOT PUBLISH

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re:) Bankruptcy Case
) No. 98-3-2705-TC
Ancillary Petition regarding)
PHILIPPINE AIRLINES, INC.,) Ancillary Proceeding
a Philippine corporation,)
)
Debtor.) MEMORANDUM DECISION
)
)
)

On September 9 and 10, 1998, this court conducted a trial regarding the objections of Aviation Sales Leasing Company, General Electric Company, and The Boeing Company to the ancillary proceeding petition filed by Philippine Airlines, Inc. Frederick D. Holden, Jr., Timothy A. Meltzer, and Jeffrey K. Garfinkle appeared for Petitioner. Steven G. Polard, Michael I. Sorochinsky, Steven M. Hedberg, and Jay L. Westbrook appeared for The Boeing Company. D. Farrington Yates and Carrie Beth Lesser appeared for Aviation Sales Leasing Company. David B. Haber and Richard A. Rogan appeared for General Electric Company. For the reasons stated below, the court grants the relief requested by the petitioner.

FACTS

Philippine Airlines, Inc. (PAL), a Philippine corporation, is the national airline of the Republic of the Philippines. On

MEMORANDUM DECISION

1 June 19, 1998, PAL filed a petition for the suspension of payments
2 and corporate rehabilitation with the Philippine Securities and
3 Exchange Commission (PSEC). On June 22, 1998, PAL filed a petition
4 for a case ancillary to a foreign proceeding in this court. On the
5 same date, Judge Newsome issued a temporary restraining order in
6 the ancillary proceeding prohibiting anywhere in the United States:
7 (a) the commencement or continuation of any legal action against
8 PAL; (b) any act to seize or assert a lien against property of PAL
9 or terminate any interest of PAL; and (c) any act to collect a
10 claim against PAL or exercise setoff or recoupment rights against
11 PAL. On June 23, 1998, the PSEC appointed Antonio V. Ocampo,
12 Henry So Uy, Jaime J. Bautista, Mario M. Aguas and Ramon A. Cruz
13 collectively as receiver for PAL (Receiver). On July 2, 1998, this
14 court issued a preliminary injunction in the ancillary proceeding.
15 The preliminary injunction continued the restraints imposed in the
16 temporary restraining order, subject to modifications for the
17 benefit of certain creditors.^{1/}

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19 ANALYSIS

20 _____
21 ^{1/} The court transferred to the United States District Court
22 for the Southern District of New York all section 304 issues
23 related to a breach of contract action brought in that court by
24 Aviation Sales Leasing Company. The court permitted The Boeing
25 Company to attempt to resell aircraft PAL had contracted to
26 purchase, and permitted Boeing to hold the deposit PAL made toward
27 that purchase. PAL stipulated with the Export-Import Bank and
28 First Security Bank that the preliminary injunction would not
prohibit any creditor action permitted by orders of the PSEC. PAL
also stipulated that the preliminary injunction did not affect any
rights or remedies under collective bargaining agreements, did not
eliminate any rights of setoff or recoupment, and did not require
turnover of property by any party who has a lien dependent upon
possession of the property.

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1 A. Legal Standard

2 Section 304 of the Bankruptcy Code authorizes a United States
3 Bankruptcy Court to grant relief designed to further the efficient
4 administration of a foreign bankruptcy proceeding. Specifically,
5 the bankruptcy court may prohibit commencement or continuation
6 of legal actions against the foreign debtor, may prohibit acts
7 against property involved in the foreign proceeding, and may
8 order additional relief that the court determines is appropriate.
9 11 U.S.C. § 304(b).

10 Section 304 affords the bankruptcy court broad discretion
11 both in determining whether to grant relief, and in determining
12 what relief to grant. The Bankruptcy Code does, however, provide
13 the following criteria to guide the bankruptcy court in exercising
14 its discretion.

15 (c) In determining whether to grant relief under
16 subsection (b) of this section, the court shall be guided
17 by what will best assure an economical and expeditious
18 administration of such estate, consistent with -

19 (1) just treatment of all holders of
20 claims against or interests in such estate;

21 (2) protection of claim holders in the
22 United States against prejudice and
23 inconvenience in the processing of claims in
24 such foreign proceeding;

25 (3) prevention of preferential or
26 fraudulent dispositions of property of such
27 estate;

28 (4) distribution of proceeds such estate
substantially in accordance with the order
prescribed by this title;

(5) comity; and

(6) if appropriate, the provision of
an opportunity for a fresh start for the

1 individual that such foreign proceeding
2 concerns.

3 11 U.S.C. § 304(c).

4 Published decisions state that the criteria identified in
5 section 304(c) authorize the bankruptcy court to grant relief in
6 furtherance of principles of comity if the applicable foreign law
7 provides fundamental fairness to United States creditors.

8 These factors are not requirements but are, rather,
9 guideline criteria by which the bankruptcy court should
10 measure the extent to which foreign law is compatible
11 with U.S. practice. . . . [T]he Second Circuit read the
12 provisions of § 304 to permit, "federal courts [to]
13 recognize foreign bankruptcy proceedings provided the
14 foreign laws comport with due process and fairly treat
15 claims of local creditors." Victrix S.S. Co. v. Salen
16 Dry Cargo A.B., 825 F.2d 709, 714 (2d Cir. 1987)
17 (citations omitted).

18 Haarhuis v. Kunnan Enterprises, Ltd., 223 B.R. 252, 255-56 (D.D.C.
19 1998). See also In re Hourani, 180 B.R. 58, 64 (Bankr. S.D.N.Y.
20 1995)("Deference should only be given to those insolvency
21 proceedings that provide a reasonable degree of certainty that the
22 consideration of all parties' rights will be fair and impartial.")

23 B. The Parties' Arguments

24 Objecting creditors argue that the PAL suspension of payments
25 proceeding before the PSEC does not provide the creditor protection
26 necessary for this court to grant relief under section 304.
27 Notably, objecting creditors do not argue that Philippine
28 insolvency law differs materially from United States law.^{2/} Rather,

29 ^{2/} Aviation Sales Leasing Company, for instance, expressly
30 acknowledges "the [Philippine] law generally applicable to
31 insolvency, Act No. 1956[,] . . . generally provides for the
32 restructuring of debt or the liquidation of entities in a manner
33 analogous to that provided by the United States Bankruptcy Code."

(continued...)

1 their sole argument is that the PSEC, which has jurisdiction over
2 the proceeding, is not subject to Philippine insolvency law. In
3 1981, by decree of then President Ferdinand Marcos, jurisdiction
4 over suspension of payments proceedings was transferred from the
5 Philippine courts to the PSEC. Because the Presidential Decree
6 did not incorporate the insolvency law, objecting creditors argue,
7 the PSEC is not bound by any substantive or procedural rules.

8 This argument is unpersuasive.

9 C. Similarity of Philippine Law to U.S. Law

10 I conclude that Philippine insolvency law provides creditors
11 protections similar to those found under United States bankruptcy
12 law and satisfies the criteria of § 304(c).

13 The law governing Philippine suspension of payments
14 proceedings is not integrated into a single code. The substantive
15 provisions governing reorganization and liquidation are found in
16 the Insolvency Act (Act No. 1956), which was enacted by the
17 Philippine legislature in 1909, when the Philippines were a
18 territory of the United States. The provisions governing priority
19 of claims are found in the Civil Code. The provisions defining the
20 jurisdiction and power of the PSEC are found in Presidential Decree
21 902-A (PD 902-A). The PSEC has promulgated its own rules of
22 procedure. The statutory provisions governing appellate review of
23 PSEC decisions are published in a volume entitled Rules of Court.

24 Chapter II of the Insolvency Act governs suspension of
25 payments. It provides that a debtor whose assets exceed

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27 ^{2/}(...continued)
28 Trial Brief of Aviation Sales Leasing Company at 11.

MEMORANDUM DECISION

1 liabilities, but who is unable to pay debts as they come due,
2 may petition the court for suspension of payments. Act No. 1956,
3 section 2. The debtor is required to attach to the petition a list
4 of assets and liabilities and "the proposed agreement" he requests
5 of his creditors. Id., section 2. The court then sets a meeting
6 of creditors and enjoins the debtor from transferring property or
7 paying debts out of the ordinary course of business without court
8 permission. Id., section 3. All listed creditors are provided
9 notice of the meeting of creditors and may attend that meeting.
10 Id., sections 4 and 5. Virtually all unsecured creditors are
11 enjoined from attempting to collect claims from debtor. Id.,
12 section 6. The court counts the votes at the meeting of creditors
13 to see whether the creditors approve debtor's plan. Id.,
14 section 8. The plan is approved if two-thirds in number and three-
15 fifths in amount of creditors vote to accept. Id., section 8.
16 Secured creditors who reject the plan are not bound by the plan
17 and may proceed to enforce their rights. Id., section 9. If
18 creditors reject the plan, the proceeding is terminated and
19 the creditors are free to enforce their rights. Id., section 11.
20 If the plan is approved, but debtor fails to perform, creditors
21 are free to enforce their rights. Id., section 13.

22 Other sections of the Insolvency Act contain additional
23 provisions similar to those of the United States Bankruptcy Code.
24 Section 48 provides that upon filing, property of the debtor is
25 held in trust for creditors. Section 53 adopts a broad definition
26 of claims that includes disputed, contingent and unliquidated
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1 claims.^{3/} Section 55 permits the court to estimate contingent
2 claims. Section 58 preserves rights of setoff. Section 59
3 provides that claims are considered partially secured where the
4 debt exceeds the value of the collateral. Section 61 provides that
5 the claim of a creditor who received a preferential transfer is
6 disallowed until the preference is returned. Section 62 provides
7 for examination of the debtor. Section 70 provides for the
8 recovery of preferences and fraudulent transfers.^{4/}

9 The Philippine Civil Code governs priority of creditors of an
10 insolvent debtor. Section 2241 recognizes numerous types of liens
11 on personal property, including tax liens, mortgages, claims for
12 misappropriation of the property, claims for the purchase price

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14 ^{3/} The Philippine Supreme Court held that the PSEC has
15 jurisdiction to determine claims and adopted the following broad
16 definition of "claims," which is very similar to the definition of
17 claim in section 101(5) of the Bankruptcy Code.

18 Right to payment, whether or not such right is
19 reduced to judgment, liquidated, unliquidated, fixed,
20 contingent, matured, unmatured, disputed, undisputed,
21 legal, equitable, secured, or unsecured; or right to
22 an equitable remedy for breach of performance if such
23 breach gives rise to a right to payment, whether or
24 not such right to an equitable remedy is reduced to
25 judgment, fixed, contingent, matured, unmatured,
26 disputed, undisputed, secured, unsecured.

27 Finasia Investments and Finance Corp. v. Courts of Appeals,
28 237 S.C.R.A. 446, 450 (Phil. Sup. Ct. 1994).

29 ^{4/} Section 70 permits the recovery of a transfer made by the
30 debtor within 30 days before the petition and while the debtor is
31 insolvent if the transfer was made for the purpose of giving a
32 creditor a preference and the party receiving the transfer had
33 reason to know of that purpose. Section 70 also permits recovery
34 of all transfers made by the debtor within one month before the
35 petition date for which the transferee did not pay valuable
36 consideration in good faith. The PSEC has stated that section 70
37 applies in suspension of payment proceedings before the PSEC. See
38 November 3, 1997 letter ruling of Perfecto R. Yasay, Jr. (Chairman
of PSEC).

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1 for the property, hotelkeepers liens, claims for transportation,
2 salvage and repair of the property, and crop liens. Section 2242
3 recognizes various types of liens on real property, including tax
4 liens, mortgages, mechanics liens, and judgment liens. Sections
5 2246-50 provide that property shall be used to satisfy first those
6 creditors who have a lien against the property, and that lien-
7 holders shall be paid pro rata if the value of the property is
8 insufficient to pay all lienholders in full. Section 2244 fixes
9 the priority among unsecured creditors. Some of the priorities
10 recognized are similar to those set forth in the Bankruptcy Code:
11 unpaid wages, costs of administration, and taxes. Other priorities
12 recognized in section 2244 are not recognized in the Bankruptcy
13 Code: funeral expenses, costs of last illness, living expenses
14 during the year before filing, wrongful death and personal injury
15 claims, charitable pledges, and fines. Section 2251 provides that
16 general unsecured creditors are paid pro rata from any remaining
17 assets. All the expert witnesses agreed that Philippine law treats
18 foreign and domestic creditors alike.

19 PD 902-A transferred jurisdiction over certain suspensions of
20 payment proceedings filed from the courts to the PSEC. Section 5
21 provides that the PSEC "shall have original and exclusive
22 jurisdiction to hear and decide" cases involving suspension of
23 payments petitions filed by corporations and partnerships.
24 Section 6 authorizes the PSEC to issue injunctions, issue writs,
25 appoint receivers, appoint management committees for partnerships
26 and corporations, punish contempt, and issue subpoenas. Section 12
27 provides: "All laws, executive orders, decrees, rules and
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1 regulations or parts thereof, contrary to or inconsistent with the
2 provisions of this Decree are hereby repealed, amended or modified
3 accordingly." PD 902-A does not specify the substantive rules to
4 govern suspension of payments proceedings or authorize the PSEC to
5 promulgate substantive law. All the expert witnesses agree that PD
6 902-A should be considered an exercise of legislative power by the
7 President and should be interpreted in the same way as a statute.

8 The PSEC has issued two sets of rules. The Revised Rules of
9 Procedure in the Securities and Exchange Commission, As Amended,
10 fix rules of procedure governing all types of proceedings before
11 the PSEC and are very similar to the Federal Rules of Civil
12 Procedure used by United States Courts. The Proposed Rules of
13 Procedure of the Securities and Exchange Commission for Suspension
14 of Payments would establish rules applicable only in suspension of
15 payments cases. Those proposed rules adopt official forms that
16 specify in detail the schedules debtor must file, and specify how
17 certain proceedings are to be conducted. These proposed rules are
18 consistent with the provisions of the Insolvency Act.^{5/}

19 All decisions of PSEC are subject to review by the Philippine
20 Court of Appeals and by the Philippine Supreme Court. See Figueroa
21 v. Securities and Exchange Commission, 162 S.C.R.A. 689, 690 (Phil.

23 ^{5/} Proposed rule 18(g) is inconsistent with the Insolvency
24 Act. The proposed rule specifies that the requisite majority vote
25 in amount. Section 8 of the Insolvency Act specifies two-thirds
26 in number and three-fifths in amount. In light of the fact that
27 the proposed rule has not yet been adopted, and the rules
28 elsewhere state the intent to be consistent with the Insolvency
Act (see "Items not included in draft recommendations to SEC on
Suspension of payments"), it is most appropriate to determine that
proposed rule 18(g) simply contains a not-yet-corrected mistake.

1 Sup. Ct. 1988); Lim v. Securities and Exchange Commission, Republic
2 of the Philippines Court of Appeal CA-G.R. SP-Nos. 32404, 32469,
3 and 32483 (1995).

4 D. Philippine Insolvency Law Applies in PSEC Proceedings

5 I further conclude that the PSEC is bound by the Insolvency
6 Act and the relevant provisions of the Civil Code. The most
7 obvious reading of PD 902-A is that it only transferred
8 jurisdiction over suspension of payments proceedings from one
9 tribunal to another. The decree did not set forth the substantive
10 rules to apply in such proceedings or authorize the PSEC to
11 establish substantive rules. The decree purported to repeal prior
12 laws only to the extent inconsistent with the decree. The
13 Philippine Supreme Court has stated "[t]he SEC, like any other
14 administrative body, is a tribunal of limited jurisdiction and as
15 such, could wield only such powers as are specifically granted to
16 it by its enabling statute." Ching v. Land Bank of the
17 Philippines, 201 S.C.R.A. 190, 198 (Phil. Sup. Ct. 1991)(footnote
18 omitted). The court also stated "[a] well-recognized rule in
19 statutory construction is that repeals by implication are not
20 favored and will not be so declared unless it be manifest that the
21 legislature so intended." Id. at 202 (footnote omitted). Under
22 these rules of statutory construction, it is reasonable to conclude
23 that PD 902-A intended that the PSEC would be governed by the
24 Insolvency Act and Civil Code, in light of the fact that the decree
25 neither repealed those laws nor authorized the PSEC to promulgate
26 replacement laws.

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MEMORANDUM DECISION

1 In asserting that the PSEC has unfettered discretion in
2 suspension of payments proceedings, objecting creditors rely on
3 the following evidence: (1) the testimony of their expert witness;
4 (2) a newspaper article in which a member of the PSEC is quoted as
5 saying that the PSEC could confirm a plan in the PAL case without
6 creditor consent; and (3) decisions of the PSEC and Philippine
7 courts that allegedly ignore the requirements of the Insolvency
8 Act. This evidence is unpersuasive. First, the testimony of the
9 experts was inconclusive. Mr. Catindig testified that the PSEC was
10 not bound by the Insolvency Act. Mr. Lim testified that the PSEC
11 was "guided" by the Insolvency Act. Mr. Nolasco testified that
12 the PSEC was required to apply the Insolvency Act. Second, I do
13 not judge the newspaper article to be an authoritative expression
14 of either the position of the PSEC or of Philippine law. Third,
15 while a few decisions of the PSEC do appear not to enforce some
16 creditor protections in the Insolvency Act,^{6/} the same criticism
17 could be justly applied to some decisions of United States courts.
18 No published decision states that the PSEC is not bound by the
19 Insolvency Act or Civil Code. Furthermore, having read every PSEC
20 decision and Philippine court decision submitted by the parties, I
21 conclude that the PSEC applies the Insolvency Act and Civil Code
22 with reasonable reliability and is not at all the lawless agency
23 objecting creditors portray it to be.

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25 ^{6/} See, e.g., Ruby Industrial Corporation v. Court of Appeals,
26 Republic of the Philippines Supreme Court G.R. No. 124185-87
27 (1998)(PSEC orders confirming plan despite rejection by unsecured
28 creditors, reversed on appeal on other grounds); In re BF Holmes
Incorporated, PSEC Hearing Panel Order, dated February 2, 1988
(plan confirmed by over objection of secured creditors who were
also required to accept replacement collateral).

1 CONCLUSION

2 The ancillary petition is granted. The preliminary injunction
3 shall remain in effect, subject to the limitations stipulated to by
4 Petitioner. Petitioner's counsel shall prepare and circulate a
5 proposed form of order.

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13 Dated: _____

Thomas E. Carlson
United States Bankruptcy Judge

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MEMORANDUM DECISION