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NORTH CAROLINA JOURNAL OF INTERNATIONAL LAW AND COMMERCIAL REGULATION

Volume 10 | Number 2

Article 2

Spring 1985

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Recommended Citation

Timothy E. Powers & Rona R. Mears, *Protecting a U.S. Debtor's Assets in International Bankruptcy: A Survey and Proposal for Reciprocity*, 10 N.C. J. INT'L L. & COM. REG. 303 (1985).

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Protecting a U.S. Debtor's Assets in International Bankruptcy: A Survey and Proposal for Reciprocity

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It is obvious that, in the present state of commerce and communication, it would be better in nine cases out of ten that all settlements of insolvent debtors with their creditors should be made in a single proceeding and generally at a single place, better for the creditors, who would thus share alike and better for the debtor because all his creditors would be equally bound by his discharge. John Lowell (1888).¹

I. Introduction

A bankruptcy proceeding attains the status of an international bankruptcy when the assets and creditors of the insolvent debtor are located in more than one country. With increased international trade and economic interdependence, international bankruptcies most likely will become commonplace. Unfortunately, the current status of treaties, statutes, and case law on this subject remains in an embryonic stage, even though several commentators have proposed solutions and a number of treaties have been introduced over the past century.²

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The authors wish to thank Robin E. Phelan, partner and chairman of the bankruptcy section of Haynes and Boone, Dallas, Texas, for his comments and guidance in developing this article. Thanks also are extended by the authors to the seven foreign counsel who reviewed, and in several instances added substantially to, the subsection on bankruptcy law of the foreign jurisdictions. The views expressed herein are solely those of the authors and should not be attributed to foreign counsel.

¹ Lowell, *Conflicts of Law as Applied to Assignments for Creditors*, 1 HARV. L. REV. 259, 264 (1888).

² To say that case law on the subject of international bankruptcy is underdeveloped is an understatement. Over the past century, only six noteworthy cases with international bankruptcy implications have been decided by U.S. courts: *Canada Southern Ry. v. Gebhard*, 109 U.S. 527 (1883); *Banque de Financement, S.A. v. First Nat'l Bank of Boston*, 568 F.2d 911 (2d Cir. 1977); *Israel-British Bank (London), Ltd. v. FDIC*, 536 F.2d 509 (2d Cir.), cert. denied, 429 U.S. 978 (1976); *Kenner Products Co. v. Societe Fonciere et Financiere Agache-Willot*, 532 F. Supp. 478 (S.D.N.Y. 1982); *Cornfeld v. Investors Over-*

The goal in an international bankruptcy is to protect the estate of the insolvent debtor from dismemberment, accomplish an equitable distribution of assets among both domestic and foreign creditors in liquidation, and allow for the equitable administration of the estate in reorganization. This article focuses primarily on current techniques for the protection of the foreign assets of a debtor (the U.S. Debtor) under the United States Bankruptcy Code (U.S. Bankruptcy Code).³ Such protection is necessitated by the reluctance of the major trading partners⁴ of the United States to recognize the assertion of "universal" jurisdiction over the estate of the U.S. Debtor under the U.S. Bankruptcy Code.

This article also contrasts the means by which the representative of a foreign debtor involved in a foreign bankruptcy proceeding may institute ancillary proceedings under the U.S. Bankruptcy Code to protect the U.S. assets of the foreign debtor.⁵ Finally, the article proposes that if the major trading partners of the United States do not follow the U.S. model, the U.S. bankruptcy courts, prior to authorizing an ancillary proceeding under the U.S. Bankruptcy Code, require reciprocal treatment from the jurisdiction of a petitioning foreign representative. Alternatively, it is suggested that the U.S. Bankruptcy Code be amended to provide such requirement—which

seas Servs. Ltd., 471 F. Supp. 1255 (S.D.N.Y.), *aff'd*, 614 F.2d 1286 (2d Cir. 1979); *In re Aktiebolaget Kreuger & Toll*, 20 F. Supp. 964 (S.D.N.Y. 1937), *aff'd*, 96 F.2d 768 (2d Cir. 1938).

Although inconsistent and confusing, these decisions are based on comity of nations. The most famous international insolvency proceeding, Bankhaus I.D. Herstatt Kommanditgesellschaft auf Aktien (*Herstatt*), was not decided by a U.S. court, even though an involuntary petition was filed against Herstatt in New York (Bankruptcy No. 74-1134 [S.D.N.Y.]). In *Herstatt* the creditors from all nations agreed to an out-of-court liquidation plan based on the belief that legal precedent was inadequate to bring about prompt and satisfactory results. For a detailed analysis of the *Herstatt* affair and the various commentary on international insolvency proceedings, see Nadelmann, *Rehabilitating International Bankruptcy Law: Lessons Taught by Herstatt and Company*, 52 N.Y.U. L. REV. 1 (1977); Becker, *International Insolvency: The Case of Herstatt*, 62 A.B.A. J. 1290 (1976); Nadelmann, *Israel-British Bank (London) Ltd.: Yet Another Transatlantic Crossing*, 52 AM. BANKR. L.J. 369 (1978). For a discussion of existing treaty proposals, see *infra* notes 264-81 and accompanying text. Treatises and articles on international bankruptcy also are scarce, except for the contributions of Kurt H. Nadelmann and J. H. Dalhuisen, cited *infra* notes 6 & 31. Very few other sources are available. See also H. HANISCH, J. LEMONTEY & S. RISENFELD, *PROBLEME DES INTERNATIONALEN INSOLVENZRECHTS* (1982).

³ Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified as amended at 11 U.S.C. §§ 101-151326 and in scattered sections of 28 U.S.C. and scattered sections under other titles). Unless otherwise indicated, all "section" references in the article will be to the applicable section of the U.S. Bankruptcy Code.

⁴ For the purpose of this article, the major trading partners of the United States are Brazil, Canada, France, Germany, Great Britain, Japan, and Mexico. An analysis of the laws of these countries relating to insolvency proceedings was undertaken, not only because of the high volume of trade between the countries and the presence of United States investment, but also because it provides the reader with a glimpse of the insolvency law of a representative group of common-law and civil-law countries located in the major trading hemispheres.

⁵ See 11 U.S.C. § 304 (1982). See generally *infra* text accompanying notes 220-62.

may prompt foreign countries to adopt similar legislation on ancillary bankruptcy proceedings.

Additionally, such legislation ultimately may lead to the adoption of treaties or a body of international bankruptcy law that recognizes the value of the central administration of bankruptcy proceedings and effectuates the goal of worldwide equality of distribution of assets that otherwise might be frustrated by preferential local attachments and levies.

II. Jurisdictional Principles

A. *Bankruptcy Code*

Upon commencement of a case under the U.S. Bankruptcy Code, the district court in which the case is filed has exclusive jurisdiction over all property of the U.S. Debtor (the estate), wherever located, as of the commencement.⁶ This unlimited geographical reach with respect to the estate also has been held to carry with it personal jurisdiction of equally unlimited scope.⁷ In theory, therefore, all creditors of the U.S. Debtor, wherever located, are stayed from further action against both the U.S. Debtor and the estate property during the pendency of the bankruptcy proceeding.⁸ This automatic stay is designed to provide an orderly liquidation procedure under which all creditors are treated equally.⁹

Such a jurisdictional claim has no force of its own outside the United States, however, and its effectiveness depends on the cooperation of the courts in the jurisdiction where the foreign assets are located. Unfortunately, none of the major trading partners of the United States have recognized the extraterritorial jurisdiction of the U.S. Bankruptcy Code. Fortunately, there are methods of protecting the assets of the U.S. Debtor located in the jurisdictions of these major trading partners.¹⁰

B. *Historical Concepts*

Historically, the two central and opposing doctrines that underlie the jurisdictional principles of an international bankruptcy are "universality" and "territoriality." Universality presumes the full in-

⁶ 28 U.S.C. § 1334 (1982). This type of provision, which grants jurisdiction over all the assets of an insolvent debtor, is found in the bankruptcy laws of many countries, including Belgium, Canada, England, France, Germany, Italy, and Luxembourg. For a discussion of applicable statutes, see 1 J. DALHUISEN, *DALHUISEN ON INTERNATIONAL INSOLVENCY AND BANKRUPTCY* § 2.02[2], at 3-158 (1984). See also 11 U.S.C. § 541 (1982), which lists the assets included in an estate for bankruptcy purposes.

⁷ *In re Universal Money Order Co.*, 470 F. Supp. 869, 882 (S.D.N.Y. 1977).

⁸ 11 U.S.C. § 362 (1982).

⁹ For a discussion of the automatic stay provision of section 362, see Phelan & Capshaw, *Solomon's Capitulation: The Automatic Stay, Adequate Protection and Use of Collateral*, 317 P.L.I. COMMERCIAL LAW AND PRACTICE COURSE HANDBOOK (1984).

¹⁰ See generally *infra* text accompanying notes 16-219.

ternational effect of local bankruptcy adjudications and is supported primarily by principles such as the unity of the debtor's estate, equality among creditors, effectiveness of the bankruptcy proceeding as relief for the debtor, and the efficiency of the proceeding.¹¹

The concept of universality envisions a single bankruptcy administration of the entire estate at the domicile of the debtor. The principle relies on the doctrine of *lex fori* to conduct the entire bankruptcy proceeding under the laws of the domicile of the debtor. As to bankruptcies within their own jurisdictions, most countries follow the principle of universal jurisdiction, even if recognition of foreign bankruptcy proceedings in that jurisdiction is limited severely.¹²

Conversely, the principle of territoriality rejects any extraterritorial effect of bankruptcy adjudication and requires the administration of bankruptcy proceedings in every jurisdiction where assets of the debtor are located. This theory is defended on the basis of unavoidable territorial limitations on execution measures, protection of local creditors, variation in the bankruptcy laws of each jurisdiction, and the simplicity and certainty of local proceedings.¹³

The concepts of universality and territoriality are solely jurisdictional in nature. In their purest form, both approaches avoid complex conflict of laws issues. If the universality theory is followed, the *lex fori* of the domiciliary court will govern the entire proceedings. If the territoriality approach is followed, the local bankruptcy adjudication will not have extraterritorial effect.¹⁴

From an international practitioner's standpoint, the principle of universality is most compatible with the goal of equal treatment of all creditors, debtors, assets and liabilities, and the swift and effective

¹¹ 1 J. DALHUISEN, *supra* note 6, § 2.03[3], at 3-186 to -188.

¹² *Id.* at 3-190.2.

¹³ *Id.* at 3-188.

¹⁴ By their nature, the jurisdictional principles of universality and territoriality avoid complex conflict of laws issues. The bankruptcy laws applied by the adjudicating court under *lex fori* could restrict the international recognition of its extraterritorial jurisdictional claims, if the bankruptcy laws being applied are contrary to the public policy of the recognizing forum. Consequently, the adjudicating court cannot apply *lex fori* simply because of necessity, logic or convenience.

Lex fori must instead be modified, if necessary, to take into account the concern of the foreign recognizing forum regarding avoidable, preferential and fraudulent transfers, exempt assets, provability and allowability of claims, distribution of assets and rank of claims, and the dischargeability of the debtor, all of which may greatly vary by jurisdiction. Without such modifications the universal philosophy will never gain acceptance. At the very least the adjudicating forum must take into account the foreign elements of the bankruptcy proceedings, and it must make adjustments to its foreign decrees in a manner compatible with its own bankruptcy laws and public policy.

Without making adjustments for these concerns, the laws applied by an adjudicating bankruptcy court under the doctrine of *lex fori* may be ineffective and subject to attack, even if universal jurisdiction is accepted in principle, whenever the status of the adjudication and its effects on foreign property and interests have been determined elsewhere. For a discussion of these conflict of laws principles, see Honsberger, *Conflict of Laws and the Bankruptcy Reform Act of 1978*, 30 CASE W. RES. L. REV. 631 (1980).

administration of the estate. Otherwise, under the principle of territoriality, the property of a debtor located outside the domestic jurisdiction is subject to attachment and execution by creditors in the country where the assets are located.

III. Protecting the U.S. Debtor's Foreign Assets from Foreign Creditors

Primary concerns of the U.S. Debtor with assets located outside the United States include protecting such assets from creditors and ensuring that the assets will be preserved, collected, and equitably administered for the estate. Most foreign jurisdictions fail to recognize the universal jurisdiction asserted by U.S. courts over the estate of the U.S. Debtor.¹⁵ Consequently, action must be taken promptly by the U.S. Debtor to protect assets located in foreign countries.

A. Actions in the United States to Protect Foreign Assets

Time is of the essence in many foreign jurisdictions where prompt actions by creditors to seize the U.S. Debtor's assets may preclude administration of such assets under the U.S. Bankruptcy Code. Consequently, the U.S. Debtor should act quickly to perform several tasks. First, the U.S. Debtor and its attorney should compile and file promptly the required list of creditors, schedule of assets and liabilities, and statement of the U.S. Debtor's financial affairs with the original petition for relief.¹⁶ Concurrently, the U.S. Debtor should complete records and documentation concerning foreign assets to facilitate immediate action in the foreign jurisdictions.¹⁷

Immediately after the order for relief is granted under the U.S. Bankruptcy Code, the U.S. Debtor should verify the legal status of the representative of the estate pursuant to actions taken in foreign jurisdictions.¹⁸ In addition, the U.S. Debtor should seek the neces-

¹⁵ See *infra* text accompanying notes 11-14.

¹⁶ 11 U.S.C. § 521(1) (1982). If such compilation is not completed at the time of filing the petition for relief, the U.S. Debtor also should take immediate steps to compile "any recorded information, including books, documents, records and papers, relating to property of the estate." *Id.* § 521(3). FED. BANKR. R. 1007 sets forth instructions for compiling and filing schedules. Official forms accompanying the Bankruptcy Rules should be used and followed as closely as possible during preparation of the schedules. See generally 3 W. COLLIER, COLLIER ON BANKRUPTCY §§ 5521.03-.14 (15th ed. 1984).

¹⁷ Considerable diligence in obtaining complete real property descriptions, full addresses of third parties abroad owing sums to the U.S. Debtor, accurate accounts of sums payable to all creditors, and similar efforts become more important when assets are located in foreign jurisdictions.

¹⁸ U.S. Bankruptcy Rules provide detailed information concerning certified evidence that may be obtained regarding the qualification of the estate representative. Once a trustee has been appointed or elected, and has filed a bond pursuant to section 322(a) or, if under a blanket bond, has filed an acceptance of election or appointment, a certified copy of the order approving the trustee's bond or the acceptance constitutes conclusive evidence of qualification of a trustee under the provisions of FED. BANKR. R. 2010. Simi-

sary orders from the bankruptcy court¹⁹ to obtain recognition of the U.S. Bankruptcy proceeding in those jurisdictions where such recognition may be available.²⁰

Once the U.S. Debtor ascertains the foreign jurisdictions where assets are located, it should establish contact with foreign counsel in each of the jurisdictions.²¹ Foreign counsel will be needed to advise as to appropriate legal action, and to represent the U.S. Debtor in any local proceedings in the respective jurisdictions.²²

larly, a certificate of the clerk of court certifying that the U.S. Debtor is a debtor in possession constitutes conclusive evidence of such fact under FED. BANKR. R. 2011.

In addition, copies of court orders or decrees certified by the clerk of court may be obtained as evidence that U.S. Bankruptcy proceedings are being conducted or that certain court orders have been handed down. All such certified documents also should have final certification as to the genuineness of the signature and official position of (1) the executing or attesting person, and (2) any official whose certificate of genuineness of signature and official position relates to the execution.

Such final certification is obtained either if: (1) the foreign jurisdiction is a Signatory of the Hague Convention Abolishing the Requirement of Legalization of Foreign Public Documents, Oct. 5, 1961, T.I.A.S. No. 10072, 527 U.N.T.S. 189 (the "Convention") by having the clerk of court affix an apostile to the document and complete it pursuant to the provisions of the Convention; or (2) if the foreign jurisdiction is not a Signatory of the Convention, by having the court-certified document legalized at the nearest U.S. Consulate of the country where such certified documents are to be presented. Local counsel in the relevant jurisdiction should be consulted regarding the particular requirements of each country.

¹⁹ 11 U.S.C. § 105(a) (1982). Section 105(a) provides that the bankruptcy court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of the U.S. Bankruptcy Code. *Id.*

²⁰ See *infra* notes 39, 118 & 138 and accompanying text.

²¹ 11 U.S.C. § 327 (1982). Section 327 of the U.S. Bankruptcy Code authorizes the employment of such counsel with the bankruptcy court's approval. *Id.*

²² Among the most important qualifications in foreign counsel are familiarity with and experience in local bankruptcy proceedings, and if possible, in multinational bankruptcies, fluency in the English language, adequate staff, communication and support systems, and promptness in responding to communications. A personal recommendation from a U.S. attorney who has associated with the foreign counsel on one or more matters in the past usually is the best basis for making a selection.

Alternatively, it may be possible to obtain the recommendation of an accountant or similar professional person who is located either in the United States or in the foreign jurisdiction where counsel is sought. If no personal references are available, a local law society or bar association in the foreign jurisdiction may make a referral. Finally, there are many professional directories and listings that may be helpful in locating foreign counsel.

4 MARTINDALE-HUBBELL LAW DIRECTORY (116th ed. 1984) includes listings of foreign counsel by jurisdiction with, in most cases, areas of practice for each firm. Also available is THE INTERNATIONAL LAW LIST (1984), published by L. Corper-Mordaunt & Co., London, in which counsel are listed by jurisdiction, and areas of practice are included for most firms. Of special interest is the listing of principal law societies and bar associations of jurisdictions throughout the world that may be contacted for assistance in locating local counsel with experience in bankruptcy or debtors' and creditors' rights.

For corporate counsel members, the American Corporate Counsel Association has published a directory listing over 1300 foreign counsel in 109 countries. Each lawyer listed has been recommended specifically by Association members. Finally, special directories for key jurisdictions are useful. One example is WHO'S WHO IN CANADIAN LAW (3d ed. 1984), in which each biography includes in large type at the end of the entry the counsel's preferred areas of law practice.

B. *Protecting the U.S. Debtor's Assets in the Foreign Jurisdiction*

Most actions necessary to protect foreign assets of the U.S. Debtor are initiated in the foreign jurisdiction where the assets are located. A U.S. Debtor may be faced with a situation in which assets are located in several jurisdictions. Such assets may be threatened by the actions of local creditors in each jurisdiction, requiring prompt and often differing responses in each foreign jurisdiction.

The effectiveness of actions by the U.S. Debtor in foreign jurisdictions to satisfy the claims of foreign creditors is linked closely to the provisions of section 508(a) of the U.S. Bankruptcy Code. This section bars a creditor from receiving any distribution from the U.S. Debtor's estate in U.S. proceedings if the creditor has received full payment as a result of a foreign proceeding. A creditor who has received partial payment as a result of a foreign proceeding will receive nothing until comparable U.S. creditors have received equivalent distributions.²³ Consequently, the U.S. Debtor is assured that actions in foreign jurisdictions that result in the satisfaction of creditors' claims will be recognized fully in U.S. bankruptcy proceedings, and that such creditors will be prohibited from receiving disproportionate or duplicate payments from the U.S. Debtor's estate.

With regard to the major trading partners of the United States, the discussion below includes: (1) basic principles of bankruptcy law; (2) what the U.S. Debtor can do to protect assets prior to actions taken by foreign creditors; and (3) what actions foreign creditors may take to obtain foreign assets of the U.S. Debtor, and what the U.S. Debtor can do in response to such foreign creditors' actions.²⁴

1. *Brazil*

a. *Bankruptcy Law*

Bankruptcy includes only commercial insolvency under Brazilian law and is governed by Decree-Law No. 7.661/45 known as *Lei de Falencias* (Brazilian Bankruptcy Law).²⁵ Only merchants, corpora-

²³ See 3 W. COLLIER, *supra* note 16, § 508.02.

²⁴ Each foreign jurisdiction is treated independently, assuming in each case that the foreign assets of the U.S. Debtor are located solely in the foreign jurisdiction under discussion, and that the foreign creditors likewise are located solely in the jurisdiction where the foreign assets are located. For the sake of brevity, certain issues have not been addressed, such as the more complex interjurisdictional problems arising when assets and creditors are located in several foreign jurisdictions and, in particular, when foreign creditors seek to obtain assets located in a third country which is neither that of the foreign creditor nor that of the U.S. Debtor and the bankruptcy proceeding. Although in theory such issues may arise, it is more likely that a foreign creditor will try simply to seize those assets of the U.S. Debtor located in the creditor's own jurisdiction.

²⁵ For a summary of Brazilian bankruptcy statutes in English, see Baptista, Carvalho Tess & Christino Netto, *The Commercial Laws of Brazil*, I DIGEST OF COMMERCIAL LAWS OF THE WORLD 31-33 (1983) [hereinafter cited as *Commercial Laws of Brazil*]. See generally PINHEIRO NETO-ADVOGADOS, *DOING BUSINESS IN BRAZIL* ch. 11 (1979). The authors ex-

tions, and other business debtors can be adjudicated bankrupt under Brazilian Bankruptcy Law. The basis for bankruptcy proceedings in Brazil is either a proven default of the debtor with regard to payment of a liquidated and certain debt that already has fallen due, or an insolvency presumption of law based on seven specified criteria.²⁶

Three types of proceedings are available in Brazil: (1) bankruptcy leading to liquidation; (2) *concordata suspensiva* in which the debtor enters into a composition agreement with general creditors²⁷ during the bankruptcy proceeding offering cash payment of at least thirty-five percent of claims, or installment payments of at least fifty percent within two years; and (3) *concordata preventiva*, which is available to a debtor not yet in bankruptcy who offers general creditors a composition agreement to pay either fifty percent of amounts due if paid immediately, or between sixty to one hundred percent in installments over a period no longer than two years.²⁸ Once granted, both the *concordata suspensiva* and the *concordata preventiva* bind all general creditors, civil or commercial, whether or not they reside in Brazil, and whether or not they appear on the debtor's statement of liabilities.²⁹ Payments or transfers of assets made by the debtor with intent to defraud creditors may be subject to recovery in the bankruptcy proceedings.³⁰

press their thanks to Pinheiro Neto-Advogados, São Paulo, for their assistance in preparing this section.

²⁶ The seven grounds for bankruptcy or insolvency presumptions of law are:

- (1) failing to pay an indebtedness at maturity which gives the creditor a right of attachment, or failure to pay or deposit the amount of a judgment within twenty-four hours after service of execution;
- (2) resorting to precipitate liquidation or to fraudulent or ruinous methods to make payments;
- (3) calling a meeting of creditors and proposing to them delay, remission of credits, or transfer of property;
- (4) attempting to transfer or actually transferring assets to a third party, whether or not a creditor, by contracting simulated debts, concealing or diverging property, retarding payments, or defrauding creditors;
- (5) transferring or assigning the business to third parties without authorization from creditors and without having reserved assets sufficient to liquidate liabilities;
- (6) granting mortgages, pledges, or other security, preference, or privilege in favor of any creditor without retaining free and unencumbered property sufficient to pay all other debts;
- (7) absenting or concealing oneself without leaving a representative to administer the business and pay creditors.

Commercial Law of Brazil, *supra* note 25, at 32.

²⁷ The "general creditor" or "ordinary creditor" under the Brazilian Bankruptcy Law is one not holding an "in rem guarantee" (or security interest) or other special privilege. See Furquim & Rosenberg, *Questionnaire on Creditors' Rights Against Business Debtors (Brazil)*, 1983 A.B.A. INST. ON INT'L WORKOUTS & BANKR. 33.

²⁸ For a more complete description of the *concordata suspensiva* and the *concordata preventiva*, see *id.* at 32-39.

²⁹ A *concordata* is binding whether or not the creditor is present before the court, and whether or not the creditor has appealed the *concordata* ruling. *Id.* at 35. For a discussion of the effects in U.S. proceedings, see also *infra* notes 35, 41 and accompanying text.

³⁰ Furquim & Rosenberg, *supra* note 27, at 60-61. If losses result to the creditors

Jurisdiction to declare bankruptcy is territorial in nature, and thus may be exercised by the Brazilian court where the debtor has its principal business establishment.³¹ If the debtor is a foreign entity, jurisdiction exists where the principal Brazilian branch is located. If the foreign debtor has no commercial domicile or business establishment in Brazil, the debtor is ineligible for relief under the Brazilian Bankruptcy Law.³²

Jurisdiction of the proper Brazilian court is complete to the extent that a single bankruptcy adjudication is contemplated by the Brazilian Bankruptcy Law. Authority of the court exists to hear all complaints and administer all matters regarding the business of the debtor. Brazilian courts, however, administer only assets in Brazil and do not purport to have power over assets located outside Brazil.³³ The only substantive law that is applied by courts in Brazil is the Brazilian Bankruptcy Law; no foreign substantive law will be applied in any bankruptcy proceedings in Brazilian courts.³⁴

b. Protecting Assets in Brazil

If the U.S. Debtor has a business establishment in Brazil, the U.S. Debtor may protect its assets in Brazil either by declaring bankruptcy voluntarily or seeking a *concordata preventiva*.³⁵ By declaring bankruptcy, a full disposition of Brazilian creditors' claims can be obtained, and if a *concordata preventiva* is granted, the U.S. Debtor may remain as administrator of its local business. In theory, if the provisions of Chapter 11 of the U.S. Bankruptcy Code and the provisions governing the *concordata* are complied with fully, the *concordata* may function as part of a Chapter 11 reorganization plan.³⁶

An appointed official of a U.S. bankruptcy court, such as the trustee of an estate, may obtain recognition in Brazil by granting a power of attorney to local counsel who then may act on behalf of the U.S. Debtor as to claims in Brazil.³⁷ The U.S. Debtor should discuss

because of the debtors' fraudulent action, the debtor may be imprisoned for up to four years. *Id.*

³¹ Brazil shares with a number of Latin American countries the commercial domicile basis of jurisdiction in its bankruptcy law. See Nadelmann, *Discrimination in Foreign Bankruptcy Laws Against Non-Domestic Claims*, 47 AM. BANKR. L.J. 147, 152 (1973).

³² With regard to court actions other than bankruptcy against a foreign party with no domicile or residence in Brazil, however, suit may be brought in the plaintiff's domicile. See Furquim & Rosenberg, *supra* note 27, at 24.

³³ *Id.* at 65.

³⁴ *Id.*

³⁵ For a discussion of the binding effect of the *concordata* on all creditors, see *supra* note 29 and accompanying text. Any foreign currency claims included in a *concordata* are converted into Brazilian cruzeiros on the date the *concordata* is granted so any foreign exchange risk is allocated to the creditor. See Furquim & Rosenberg, *supra* note 27, at 50.

³⁶ For a discussion of contents and requirements of a Chapter 11 plan, see generally 5 W. COLLIER, *supra* note 16, §§ 1122.03-1123.02.

³⁷ See Furquim & Rosenberg, *supra* note 27, at 64. Such procedure is available to any "appointed official of a bankruptcy court in a foreign jurisdiction." Thus, it is available, in

in detail with Brazilian counsel whether counsel, as attorney-in-fact, will be able to accomplish the U.S. Debtor's purposes in Brazil.

Generally, judgments and orders in foreign bankruptcy proceedings are not recognized by Brazilian courts.³⁸ Even if the U.S. Debtor does business in Brazil through a branch office, a bankruptcy order issued by a U.S. bankruptcy court will not be effective against the assets of the Brazilian branch. It is possible to obtain ratification of a foreign composition agreement by the Federal Supreme Court of Brazil, but usually such adjudication will not be effective against assets owned by the U.S. Debtor in Brazil and will bind only Brazilian creditors when they have been duly notified by court order.³⁹

As a consequence of the territorial basis of jurisdiction under the Brazilian Bankruptcy Law, Brazilian courts will not recognize pending U.S. proceedings. For instance, the automatic stay provision of the U.S. Bankruptcy Code is ineffective to stop local Brazilian proceedings by creditors, and the Brazilian court also may hear the case.⁴⁰

Liquidating the U.S. Debtor's assets in Brazil may be a lengthy process depending on the complexity of the proceedings involved. Even if foreign assets are liquidated and the proceeds are available for remittance to the U.S. Debtor, other problems may arise. For example, the exportation of foreign currency to the United States may be limited severely by Brazilian foreign exchange controls. Thus, special action may be required by the U.S. Debtor to obtain the necessary permission to export capital to the United States for the central administration of the estate.⁴¹

c. Seizure of Assets by Foreign Creditors and the U.S. Debtor's Response

Certain prejudgment remedies are available to a creditor of the U.S. Debtor prior to the filing of a petition in bankruptcy in Brazil. Among the devices available are: seizure of the property by attach-

principle, to the debtor in possession who can produce certified evidence of appointment by the court to such capacity, and an opinion of U.S. counsel as to the power of the court over the debtor in possession in such capacity. See *supra* note 18 and accompanying text for a discussion of U.S. certification generally.

The power of attorney should be drafted initially in English, using advice of Brazilian counsel as to its content, then must be notarized and legalized at the nearest Brazilian Consulate. After the document is transmitted to Brazil, local counsel will arrange to have it translated by a sworn public translator. See Furquim & Rosenberg, *supra* note 27, at 23.

³⁸ Although a procedure exists for recognition of foreign judgments generally, the domiciliary basis for bankruptcy proceedings in Brazil precludes recognition of foreign bankruptcy court orders or judgments. See Furquim & Rosenberg, *supra* note 27, at 28-29, 63-64.

³⁹ *Commercial Laws of Brazil*, *supra* note 25, at 33.

⁴⁰ Furquim & Rosenberg, *supra* note 27, at 49.

⁴¹ See, e.g., *Latin America's Control of Foreign Currency Outflows*, III INT'L FIN. L. REV. 9, 10-11 (1984).

ment, sequestration of property, certain discovery proceedings, protection against property waste or disposal by the U.S. Debtor, and a summons to the payment of credit instruments. A failure to pay a credit instrument may provide the creditor with adequate evidence to commence bankruptcy proceedings against the U.S. Debtor. No creditor "self-help" is available, however, and the creditor must always act through the Brazilian courts. The U.S. Debtor's potential responses to prejudgment actions by creditors include denying the existence of the debt, showing no intent to leave or default on obligations, and showing that no actions to leave or default have been taken.

Upon petition of a creditor to have the U.S. Debtor declared bankrupt, the U.S. Debtor must respond quickly.⁴² The U.S. Debtor may put forth defenses such as (1) proof of falseness of the binding instrument; (2) the statute of limitations; (3) nullity of the obligation or the respective instrument; (4) payment of the debt prior to filing for bankruptcy proceedings; (5) filing for *concordata preventiva* prior to service of process; (6) proof that deposit in court has been duly made; (7) cessation of business activities for more than two years, duly documented; and (8) any reason extinguishing or suspending performance of an obligation or excluding the U.S. Debtor from bankruptcy proceedings.⁴³

Once a petition for bankruptcy has been filed by the Brazilian creditor, the U.S. Debtor has only twenty-four hours to respond after receiving service of process. If the U.S. Debtor fails to respond, it may be declared bankrupt.⁴⁴ Such procedural requirements may make it preferable in some cases for the U.S. Debtor to file for *concordata preventiva* and thereby avoid the need to meet restrictive deadlines triggered by the actions of foreign creditors. Alternatively, after the bankruptcy has been declared, the U.S. Debtor may propose a *concordata suspensiva* to arrange payment of the creditors.⁴⁵

2. Canada

a. Bankruptcy Law

Under the Canadian Constitution, bankruptcy is within the jurisdiction of the government. The Bankruptcy Act, (Canadian Bankruptcy Act)⁴⁶ the Winding-Up Act,⁴⁷ provisions of certain provincial

⁴² See *supra* text accompanying notes 16-22.

⁴³ *Commercial Laws of Brazil*, *supra* note 25, at 32.

⁴⁴ See *supra* note 28 and accompanying text.

⁴⁵ Furquim & Rosenberg, *supra* note 27, at 54.

⁴⁶ Bankruptcy Act, ch. 7, 1949 Can. Stat. 23 (codified as amended at CAN. REV. STAT. ch. B-3 (1970)). See generally 1 & 2 L. HOULDEN & C. MORAWETZ, Q.C., BANKRUPTCY LAW OF CANADA (1984). This article focuses on the Canadian Bankruptcy Act and is confined to the common-law provinces (provinces other than Quebec). The authors express thanks to Fraser & Beatty, Toronto, for their assistance in preparing this section.

⁴⁷ Winding-up Act, CAN. REV. STAT. ch. W-10 (1970). Provisions of the Act are re-

statutes in relation to winding up, and the Companies' Creditors Arrangement Act⁴⁸ govern bankruptcy actions in Canada. In addition, each of the provinces of Canada has enacted statutes regarding security interests in real and personal property that may affect bankruptcy cases.⁴⁹

Proceedings in bankruptcy normally are commenced in the province where the debtor resides or, if a corporation, where it has its principal place of business. A Canadian trustee in bankruptcy has control over assets of the debtor throughout Canada and must locate and recover such assets for the benefit of the estate. In most instances, the validity and enforcement of secured claims will depend upon the laws of the province where the assets are located. It is important, therefore, not only to distinguish between the provinces, but also to determine where the assets are located within the province to handle court proceedings.

Most corporations and individuals, including foreign debtors residing or conducting business in Canada, may be subject to the Canadian Bankruptcy Act. Simply owning property in Canada is not a sufficient basis for jurisdiction under the Canadian Bankruptcy Act. This factor, however, may be considered in determining whether the foreign debtor resides or conducts business in Canada.⁵⁰

Proceedings under the Canadian Bankruptcy Act are based on any of ten acts of bankruptcy set out in the Act.⁵¹ Proceedings under

stricted to certain corporations, principally those incorporated under Acts of the federal government.

⁴⁸ Companies' Creditors Arrangement Act, CAN. REV. STAT. ch. C-25 (1970).

⁴⁹ Courts in the provinces also have been granted jurisdiction with respect to proceedings under the Canadian Bankruptcy Act. McKinlay & Mann, *Creditors' Rights Against Business Debtors (Canada)*, 1983 A.B.A. INST. ON INT'L WORKOUTS & BANKR. 1.

⁵⁰ *Id.* at 18.

⁵¹ If a debtor commits any of the following acts it is deemed to have committed an act of bankruptcy for purposes of the Canadian Bankruptcy Act:

- (1) assigns property for the benefit of creditors;
- (2) fraudulently conveys property;
- (3) transfers property that is void as a fraudulent preference;
- (4) departs Canada intending to defeat or delay creditors;
- (5) allows an execution to remain unsatisfied until four days before sale or for a period of fourteen days after seizure;
- (6) presents to a creditors' meeting a statement of assets and liabilities evidencing insolvency or admits inability to pay debts;
- (7) disposes or hides goods, or is about to do so, with intent to defeat or delay creditors;
- (8) provides notice to creditors that payment of debts is suspended or about to be suspended;
- (9) fails to meet liabilities as they are due;
- (10) defaults as to an arrangement or proposal.

Canadian Bankruptcy Act § 24. See generally I L. HOULDEN & C. MORAWETZ, *supra* note 46, § 8.1, at D-20 to D-25. For a discussion of the action of bankruptcy most frequently relied upon ("ceases to meet liabilities as they become due"), see Honsberger, *Failure To Pay One's Debts Generally As They Become Due: The Experience of France and Canada*, 54 AM. BANKR. L.J. 153 (1980).

the Canadian Bankruptcy Act and similar statutes may consist of (1) a petition in bankruptcy filed by a creditor; (2) an assignment by the debtor of its assets to a trustee in bankruptcy; (3) a proposal by the debtor for a compromise with its unsecured creditors; (4) an application by a creditor to wind up a corporate debtor; (5) a proposal by a corporation in certain circumstances under the Companies' Creditors Arrangement Act for an arrangement with its creditors; and (6) proceedings by a secured creditor to obtain the appointment of a receiver or a receiver and manager if such a remedy is available under the security that is held.⁵²

The debtor must make separate arrangements with secured creditors because the Canadian Bankruptcy Act recognizes the right of a secured creditor to enforce its liens by appropriate proceedings outside the bankruptcy proceedings.⁵³ A trustee in bankruptcy can require a secured creditor to value its security. If funds are available, the trustee may acquire the security at that value.

The Canadian Bankruptcy Act applies to foreign debtors residing or conducting business in Canada on the same terms as it does to Canadians. Certain problems of adequate service of process, however, may result with respect to a debtor domiciled outside Canada. Jurisdiction of the court under the Canadian Bankruptcy Act extends to all assets of the debtor, wherever located. The authority of the court with respect to assets located outside Canada is limited by the relevant laws of the foreign jurisdiction where the assets are located, and by Canadian conflict of laws rules.⁵⁴

The Canadian Bankruptcy Act provides that certain payments and transfers of assets are reviewable transactions, and part or all of the payments or assets transferred may be recoverable by the estate.⁵⁵ In addition, certain settlements and assignments made by the debtor prior to the proceedings may be voidable.⁵⁶

A trustee in bankruptcy appointed under the Canadian Bankruptcy Act takes possession of the property subject to any rights of secured creditors. If the trustee considers that the realizable value of the property is insufficient to protect against possible loss occasioned by carrying on the business of the bankrupt, the trustee is not required to carry on business unless the creditors secure him against possible loss. If the debtor makes a proposal under the Canadian Bankruptcy Act that is accepted by the creditors, the debtor will re-

⁵² McKinlay & Mann, *supra* note 49, at 11-12, 19. The appointment of a receiver by a secured creditor may either be informal (if provided for in the security) or pursuant to a court order. *Id.* at 4.

⁵³ *Id.* at 14-15.

⁵⁴ *Id.* at 29. See also *supra* note 14 and accompanying text.

⁵⁵ McKinlay & Mann, *supra* note 49, at 24.

⁵⁶ *Id.*

tain possession of its property and can carry on its business unless and until there is a default under the proposal.

The effect of the Canadian Bankruptcy Act with regard to the U.S. Debtor soon may be affected by the proposed United States-Canada Bankruptcy Treaty.⁵⁷ Under the terms of the draft treaty, bankruptcy jurisdiction would be conferred on the jurisdiction where the greater portion in value of the debtor's assets is located, resulting in a single administration of the debtor's estate. Concerning choice of law, the draft indicates that the laws of the state having jurisdiction over the case, including its choice of law rules, would apply.⁵⁸

b. Protecting Assets in Canada

A Canadian court will not recognize a U.S. bankruptcy court order or the effects of Chapter 11 proceedings with respect to assets of a U.S. Debtor in Canada.⁵⁹ The Canadian Bankruptcy Act does not provide for the effects of an assignment of property to a trustee in foreign bankruptcy proceedings.⁶⁰ In common-law provinces, however, the right of a foreign trustee in bankruptcy to deal with personal or movable property in Canada probably will be recognized,⁶¹ the Canadian court probably will not recognize such rights as to real property located in Canada.⁶² This corresponds to the general principle that Canadian courts usually will apply the laws of the foreign jurisdiction with respect to personal property, but will apply the law of the situs with regard to real property.⁶³

⁵⁷ Oct. 29, 1979 Draft of United States of America-Canada Bankruptcy Treaty (1979), reprinted in 2 J. DALHUISEN, *supra* note 6, at app. D-6A-1.

⁵⁸ See generally *infra* text accompanying notes 263-87.

⁵⁹ But see McKinlay & Mann, *supra* note 49, at 27-28.

⁶⁰ *Id.* at 26-27.

⁶¹ See Riesenfeld, *The Status of Foreign Administrators of Insolvent Estates: A Comparative Survey*, 24 AM. J. COMP. L. 288, 299 (1976). A U.S. trustee in bankruptcy, who seeks to deal with personal property of the estate but is opposed by the Canadian court, should present a certified copy of the order for appointment as trustee and an opinion of U.S. counsel as to the authority of the U.S. bankruptcy court over the U.S. Debtor. In dealing with real property, it probably would be necessary to seek appointment of a Canadian trustee by the Canadian court because the U.S. trustee would not be appointed or recognized with regard to real property.

⁶² McKinlay & Mann, *supra* note 49, at 27. See also *supra* note 54. Some precedent exists, however, for appointment of a foreign trustee as receiver for real property located in Canada. See generally Riesenfeld, *supra* note 61, at 299-300.

⁶³ McKinlay & Mann, *supra* note 49, at 28. A further corollary of this principle is that if a foreign (*i.e.*, U.S.) trustee's control over personal property is recognized by Canadian courts, it may be possible to stay the actions of secured creditors in Canada with regard to such property. Although a U.S. adjudication in bankruptcy passes title in personal property or movables to the U.S. trustee, the same is not true in Canada with respect to a Canadian trustee and, in at least one Ontario case, such U.S. adjudication did not bar successful suit by a Canadian creditor on a note made by the U.S. Debtor. *Marine Trust Co. v. Weinig*, 1935 Ont. W.N. 150, 152 (Ont. H.C. 1935). See also Riesenfeld, *supra* note 61, at 299 & n.54.

In considering whether to recognize a foreign trustee in bankruptcy, a number of factors will be considered, making the results in any particular instance uncertain.⁶⁴ If recognition of the foreign trustee is unavailable, a U.S. Debtor may obtain protection of assets in Canada either by proposing a compromise with its unsecured creditors to be filed under the Canadian Bankruptcy Act or, if available, formulating a plan under the Companies' Creditors Arrangement Act. If approved by the Court, a proposal under the Canadian Bankruptcy Act binds only unsecured creditors. Separate agreements would have to be reached with secured creditors.⁶⁵ A plan under the Companies' Creditors Arrangement Act, however, if approved by each class of creditors, would bind all creditors. This course of action is available only to corporations that have outstanding bonds or debentures issued under a trust deed.

The U.S. Debtor may make an assignment of its assets in bankruptcy under the Canadian Bankruptcy Act. In the case of concurrent bankruptcies, Canadian courts probably will support the administration of assets in each jurisdiction by the appropriate court and the trustee in that jurisdiction.⁶⁶

c. Seizure of Assets by Foreign Creditors and the U.S. Debtor's Response

The actions that a Canadian creditor may take against a U.S. Debtor depend on whether the creditor is secured or unsecured. An unsecured creditor can initiate proceedings to obtain a judgment, levy execution by seizing assets of the U.S. Debtor, and subsequently sell them to satisfy the judgment.

The right of a secured creditor depends upon the nature of its security. If a creditor holds an assignment of receivables, the account debtor will be liable to make payment upon request by the creditor.⁶⁷ This is the case both before and after bankruptcy of the U.S. Debtor is declared. If the creditor holds security in the form of a mortgage or charge upon an asset, it can enforce its security by taking the appropriate steps under the statute that authorized the original grant of the security. These steps may include possession and sale in the case of chattels, or sale under a statutory power of sale in the case of real and immovable property.

If the secured creditor holds a secured interest in all the assets

⁶⁴ Among factors to be considered are: (1) whether the U.S. bankruptcy court has proper jurisdiction by the standards of laws of the Canadian forum; (2) whether personal or real property is the subject of the action; (3) Canadian conflict of laws rules; (4) principles of comity; and (5) principles of public policy. *Id.* at 28.

⁶⁵ See *supra* notes 52-53 and accompanying text.

⁶⁶ McKinlay & Mann, *supra* note 49, at 27. See also Riesenfeld, *supra* note 61, at 299.

⁶⁷ For a discussion of the potential effect of recognition of U.S. trustee's control over personal property of the estate, see generally *supra* note 63 and accompanying text.

of the U.S. Debtor in the form of a floating charge, the secured creditor could appoint a receiver-manager who would take possession of the assets subject to the secured claims for the benefit of the secured creditor.⁶⁸ In such circumstances, it is possible that the receiver-manager could carry on the business of the U.S. Debtor in Canada with a view toward selling the business as a going concern.

While a trustee in bankruptcy has the right to obtain possession of the bankrupt's property, its rights are subject to the prior rights of secured creditors. As a general principle, however, orders and assignments made pursuant to the Canadian Bankruptcy Law take precedence over preexisting injunctions, garnishments, attachments, or other remedies, subject to certain rights of the secured creditor.⁶⁹ Consequently, to defend against such actions, the U.S. Debtor may seek to set aside the seizure of assets on the basis of recognition of the powers of a U.S. trustee in bankruptcy although such effort is unlikely to be successful. Alternatively, the U.S. Debtor may propose an agreement for payment of the creditors, or declare bankruptcy voluntarily to ensure a full disposition of the Canadian estate.

A creditor also may petition the U.S. Debtor into bankruptcy any time within six months of an act of bankruptcy by the U.S. Debtor. In response, the U.S. Debtor may dispute the petition or make a proposal for payment of creditors, which must be examined and approved by the creditors. A secured creditor, having the appropriate security, also may take action to have a receiver or a receiver-manager appointed, and such measures may be similarly disputed.⁷⁰ Any actions by creditors, except for those of secured creditors to obtain collateral,⁷¹ are stayed upon execution of a bankruptcy order or the making of a proposal by the U.S. Debtor.⁷²

3. *England*⁷³

a. *Bankruptcy Law*⁷⁴

Although bankruptcy and company liquidations currently are

⁶⁸ McKinlay & Mann, *supra* note 49, at 17.

⁶⁹ *Id.* at 23.

⁷⁰ *Id.* at 20.

⁷¹ Generally, under the Canadian Bankruptcy Act, creditors may not commence or continue actions or proceedings for recovery of their claims outside of the bankruptcy proceedings without consent of the court. Secured creditors are exempted from this general rule and may take action to enforce their security. See generally McKinlay & Mann, *supra* note 49, at 4, 14-16.

⁷² See *supra* note 53 and accompanying text.

⁷³ This section deals only with the insolvency law of England and Wales. Scotland and Northern Ireland are separate legal jurisdictions and have their own insolvency legislation, although to a certain extent it is very similar. The authors express thanks to Jonathan Rushworth—Slaughter and May, London, for his assistance in preparing this section.

⁷⁴ The administration of the insolvent estates of individuals, which includes traders as well as nontraders and members of partnerships, is termed "bankruptcy" in England. The

governed in England by two distinct statutory regimes, the law relating to liquidations incorporates many of the bankruptcy rules. Bankruptcy is regulated primarily by the Bankruptcy Act,⁷⁵ the Bankruptcy (Amendment) Act⁷⁶ and the Bankruptcy Rules,⁷⁷ as amended. Company liquidation is regulated by the Companies Act⁷⁸ and the Companies (Winding-Up) Rules,⁷⁹ as amended. Both regimes have been supplemented by case law. There is currently before the United Kingdom Parliament an Insolvency Bill⁸⁰ that, if enacted, will change substantially many aspects of English insolvency law.

Proceedings in bankruptcy may be commenced in England if the debtor⁸¹ has committed one of the eight statutory acts of bankruptcy.⁸² A creditor may file a petition in bankruptcy if the debt

administration of the insolvent estates of limited companies and corporations comes under the general heading of "liquidation" or "winding up." For purposes of consistency, the authors have retained the title "Bankruptcy Law" for this subsection and have used the term "bankruptcy" occasionally, in a broad sense to cover bankruptcy and/or winding-up proceedings. There are occasions when associations of more than seven members can be wound up under the legislation relating to companies, but this rarely occurs. See generally C. LIVADAS, *THE WINDING-UP OF INSOLVENT COMPANIES IN ENGLAND AND FRANCE* (1983); Graham, *Questionnaire on Creditors' Rights Against Business Debtors (England)*, 1983 A.B.A. INST. ON INT'L WORKOUTS & BANKR. 1.

⁷⁵ Bankruptcy Act, 1914, 4 & 5 Geo. 5, ch. 59.

⁷⁶ Bankruptcy (Amendment) Act, 1926, 16 & 17 Geo. 5, ch. 7.

⁷⁷ Bankruptcy Rules, 1952, STAT. INST. No. 2113.

⁷⁸ Companies Act, 1948, 11 & 12 Geo. 6, ch. 38. The various Companies Acts currently in effect will be consolidated as of July 1, 1985. Thereafter, all references to Companies Act, 1948 will change.

⁷⁹ Companies (Winding-Up) Rules, 1949, STAT. INST. No. 330 (L. 4). See also the Powers of Criminal Courts Act, 1973, ch. 62, (which has provisions relating to criminal bankruptcy orders), and the Insolvency Act, 1976, ch. 60 (which has provisions affecting both bankruptcy and liquidation).

⁸⁰ The bill was printed on Dec. 10, 1984 and is based on a Government White Paper entitled "A Revised Framework for Insolvency Law." DEPT OF TRADE AND INDUSTRY, CMD., No. 9175 (1984) [hereinafter cited as Insolvency Bill]. References in this section to the Insolvency Bill are to the text as originally published on Dec. 11, 1984. It is expected that the Insolvency Bill will be amended while it is considered by Parliament and that it will become law by early 1986.

⁸¹ A debtor includes any person, who at the time of committing the act of bankruptcy (a) was present personally; (b) ordinarily resided or had a place of residence; (c) carried on business either personally or by an agent; or (d) was a member of a firm or partnership carrying on business in England. English Bankruptcy Act § 1(2). See generally 3 HALSBURY'S LAWS OF ENGLAND ¶ 213 (4th ed. 1973); the Insolvency Bill, *supra* note 80, at cl. 100. This definition must be read in light of the EEC Convention on Bankruptcy when it is brought into effect, which provides criteria to determine which Member State (as defined in the Convention) shall have exclusive jurisdiction to administer the estate of a bankrupt having a presence in more than one such State. See *infra* note 276 and accompanying text.

⁸² The acts of bankruptcy are:

- (1) a conveyance or assignment of property to a trustee or trustees for the benefit of creditors;
- (2) a fraudulent conveyance, gift or other disposition of property;
- (3) a conveyance or transfer or charge on property that would be void as a fraudulent preference if the debtor were adjudged bankrupt;
- (4) a departure from England (or, being out of England, remaining out of of England) with intent to defeat or delay creditors;

owed to the creditor and its co-petitioners is a liquidated sum in excess of 750 pounds sterling. The act of bankruptcy must have occurred within three months of the presentation of the petition.⁸³

An English court is not deprived of jurisdiction to adjudicate a bankrupt on the grounds that it has been adjudicated a bankrupt by a foreign court. The fact that a debtor has been declared insolvent abroad, however, is a reason for an English court not to exercise its jurisdiction.⁸⁴

After the creditor files a bankruptcy petition, the court may stay all actions against the debtor and place his property in the care of an official receiver. The debtor is then the subject of a public examination.⁸⁵ The final step is the adjudication of bankruptcy and the vesting, with a few exceptions, of all the debtor's property in a trustee for the benefit of the creditors.⁸⁶ At any time after adjudication, the debtor may be discharged from bankruptcy either by his own application or, subject to certain conditions, on the fifth anniversary of its adjudication.⁸⁷

The property vested in the trustee is defined as property of every description, "whether real or personal and whether situated in England or elsewhere."⁸⁸ An English adjudication, therefore, purports to have universal effect as an assignment to the trustee.⁸⁹ In

- (5) execution against the debtor has been levied by seizure of goods and the goods have been sold or held by the sheriff for twenty-one days;
- (6) the filing in court of a declaration of the inability to pay debts or the presentation by a debtor of a bankruptcy petition;
- (7) failure by the debtor to comply with a bankruptcy notice issued by a judgment creditor requiring the debtor to pay the judgment debt;
- (8) the giving of notice by the debtor to any of his creditors that he has suspended or is about to suspend payment of his debts.

English Bankruptcy Act § 1. The most common act is failing to pay a judgment debt, (7) above. The Insolvency Bill, *supra* note 80, at pt. III, ch. II, as currently drafted, abolishes the concept of acts of bankruptcy and puts petitions for bankruptcy on much the same basis as those for compulsory winding up. *Id.*

⁸³ English Bankruptcy Act § 4; *see also* Insolvency Bill, *supra* note 80, at cls. 101-02.

⁸⁴ *Ex parte McCulloch*, 14 Ch. D. 716, 719 (1880). *See also infra* text accompanying notes 115-26.

⁸⁵ *See* English Bankruptcy Act § 15.

⁸⁶ It is the duty of the trustee, subject to the rights of secured creditors, to realize the assets and distribute the net proceeds to creditors in the following order of priority: (a) administration costs; (b) pre-preferential debts, such as funeral expenses; (c) preferential debts, such as tax and certain outstanding wages; (d) unsecured creditors; and (e) deferred creditors, for example, under a loan at interest varying with profits. Any surplus should be returned to the debtor. For the proposed new bankruptcy procedure *see* Insolvency Bill, *supra* note 80, at pt. III.

⁸⁷ *Compare infra* notes 95-98 and accompanying text. This section discusses company liquidation where the ultimate objective is dissolution, rather than discharge.

⁸⁸ English Bankruptcy Act § 167. *See also* Insolvency Bill, *supra* note 80, at cls. 110, 133.

⁸⁹ In general, foreign property passes subject to any charges that are recognized as affecting it by local law. *In re Somes, ex parte De Lemos*, [1896] 3 Mans. 313. A judgment in rem, even after the commencement of the English bankruptcy, probably will defeat the title of the English trustee. *Cf. Minna Craig Steamship Co. v. Chartered Mercantile Bank*, [1897] 1 Q.B. 460.

practice, however, whether foreign assets pass to the English trustee depends on the law of the jurisdiction where they are situated.⁹⁰

To maintain an equal distribution of assets, an English court may enjoin an English creditor from commencing an action against the debtor abroad.⁹¹ The court will not restrain a nonresident creditor unless that creditor seeks to prove its claim in the English proceedings.⁹² If a creditor receives any part of the bankrupt's property abroad, the creditor will not be able to prove a claim under the English proceedings unless it brings that property into account.⁹³ The extent to which an English court may compel a creditor to return property of the bankrupt situated abroad, where the creditor does not seek to prove its claim in the English proceedings, is unclear. It has been suggested that the court is empowered to do so if the creditor resides in England.⁹⁴

The liquidation of a company on the grounds of insolvency may be commenced either by a resolution of the members of the company,⁹⁵ or by a winding-up order issued by the court based on a petition filed by a party having standing to petition.⁹⁶ In corporate insolvency proceedings, there is no equivalent to the eight acts of bankruptcy. The most common ground for issuing a winding-up order is the inability to pay debts.⁹⁷ A company is deemed unable to pay its debts if, for example, it does not pay a debt exceeding 750 pounds sterling within three weeks after demand.⁹⁸

Winding up does not deprive the company of its assets, but ef-

⁹⁰ In practice this difficulty sometimes is diminished by the fact that under English Bankruptcy Act § 22(2), the debtor may be ordered to execute such power of attorney, conveyances, deeds, and instruments as may reasonably be required by the trustee and must help in the realization of his property. The debtor, however, would have to be within the jurisdiction of the English court for this section to be invoked. Failing this, the trustee will have to commence proceedings in the relevant foreign jurisdiction. *Id.* See also Insolvency Bill, *supra* note 80, at cl. 149.

⁹¹ *Ex parte Ormiston, In re Distin*, [1871] 24 L.T.R. (n.s.) 197.

⁹² *In re Tait*, [1872] 30 L.R.-Eq. 311.

⁹³ *Selkraig v. Davis*, [1814] 2 Rose 291, 318.

⁹⁴ 2 J. MORRIS, DICEY AND MORRIS ON THE CONFLICT OF LAWS 706 (10th ed. 1980).

⁹⁵ Companies Act §§ 211, 278. This process is known as voluntary winding up because the winding up is under the control of the creditors, through a committee of inspection, rather than by the court. It is also currently possible for a creditor or other person having standing to petition for the compulsory winding up of the company during the course of a voluntary winding up. This is termed winding up subject to the supervision of the court. It is rarely found in practice, and the Insolvency Bill abolishes it. See Insolvency Bill, *supra* note 80, at cl. 70. As to the availability of a winding up subject to the supervision of the court and a voluntary winding up in the case of unregistered companies, see *infra* note 102.

⁹⁶ Companies Act §§ 211, 222. This is known as compulsory winding up.

⁹⁷ Companies Act § 222. Section 222 lists other grounds on which a company may be wound up by the court. For example, a company may be wound up where the court is of the opinion that it is just and equitable. *Id.*

⁹⁸ Companies Act § 223. Compulsory winding up commences on the date on which the petition is presented, although no winding-up order by the court will be made until some time later.

fectively makes the company a statutory trustee of those assets for its creditors.⁹⁹ In compulsory winding up, any disposition of the company's property after the commencement of the winding up, without the consent of the court, is void.¹⁰⁰ The liquidator manages the company and carries on the company's business with a view to winding up and distributing assets to the creditors.¹⁰¹ When the company's affairs are wound up, the company is dissolved.

An English court has jurisdiction to wind up companies incorporated outside the United Kingdom¹⁰² if the company has assets situated in England, and persons exist who would benefit from the issuance of a winding-up order.¹⁰³ As with bankruptcy, the jurisdiction of the court is unaffected by a liquidation that already has commenced in the country of incorporation.¹⁰⁴ Although the liquidator is charged with taking control of all the assets of the company wherever located, the court may order the liquidator not to recover assets situated outside England, or not to settle creditors other than English creditors without court direction.¹⁰⁵

English law provides that after a winding-up order has been issued, no proceeding against the company may be commenced or continued without the approval of the court.¹⁰⁶ Although this provision does not apply to foreign proceedings, the court may exercise

⁹⁹ *Ayerst v. C & K (Construction) Ltd.*, 1976 A.C. 167, 178. "Trustee" is used here in its broad sense and not in its bankruptcy sense. *Id.*

¹⁰⁰ Companies Act § 227.

¹⁰¹ Subject to the rights of secured creditors, a liquidator must make payments in the following order out of the assets he receives: (a) costs of the liquidation; (b) preferential debts, such as rates, taxes, and certain outstanding wages; and (c) unsecured debts. Companies Act § 267, 309, 319.

¹⁰² Companies Act § 399(5). Such jurisdictional claim is formulated on the basis that (a) the company has been dissolved or ceased to carry on business, or is carrying on business only for the purpose of winding up its affairs; (b) the company is unable to pay its debts; or (c) the court believes that it is just and equitable that it should be wound up. *Id.* See also *In re Matheson Bros.*, [1884] 27 Ch. D. 225. An unregistered company may not be wound up voluntarily or subject to the supervision of the court. Companies Act § 339(4).

¹⁰³ 2 J. MORRIS, *supra* note 94, at 734; *Banque des Marchands de Moscou v. Kindersley*, [1951] Ch. 112, 126. A right of action with a reasonable possibility of success would be a sufficient "asset" for these purposes. *In re Allobrogia Steamship Corp.*, [1978] 3 All E.R. 423, 430. It has been held that even where there are not assets in England and the company has no place of business there, it may be wound up if that would benefit the petitioning creditors. *In re Eloc Electra-Optieck and Communicatie B.V.*, [1982] Ch. 43 (petition by unfairly dismissed employees who might receive payments from government redundancy fund if the debtor company was ordered to be wound up). As with bankruptcy, the provisions of the EEC Bankruptcy Convention (which extend to corporate insolvency) would have to be taken into account in determining jurisdiction. See also *infra* note 276 and accompanying text.

¹⁰⁴ 27 Ch. D. at 225.

¹⁰⁵ *In re Hibernian Merchants Ltd.*, [1958] Ch. 76. An English court would be reluctant to adjudicate on title as to assets situated abroad, and a liquidator, therefore, normally would institute proceedings in the relevant foreign jurisdiction. Graham, *supra* note 74, at 24.

¹⁰⁶ Companies Act § 231. For the position between presentation of petition and the making of the order, see Companies Act § 226.

its inherent power to stay foreign proceedings to prevent creditors subject to its jurisdiction from obtaining an inequitable share of the assets.¹⁰⁷ Similarly, a creditor who levies execution on assets situated abroad after the commencement of the winding up may be compelled to surrender the fruits of the execution for the general benefit of all creditors if the creditor is subject to the English court's jurisdiction.¹⁰⁸

Winding up must be distinguished from corporate receivership, in which a debenture holder¹⁰⁹ appoints a receiver to take possession of the debtor company's assets with the aim of satisfying the debenture holder's claim.¹¹⁰ After paying his own expenses and fees, the costs of the appointing debenture holder, preferential claims, and the debt due under the debenture itself, the receiver will pay any remaining surplus to the company, or to any second mortgagee if one exists and thereafter to the liquidator if one has been appointed.¹¹¹

In the case of both individual and corporate debtors, it is possible to make formal arrangements with creditors short of bankruptcy or liquidation.¹¹² Because of the requirements imposed by law, however, these procedures are used rarely.¹¹³ In addition, the Insolvency Bill would allow the court, on the application of the debtor or its creditors, to appoint an administrator upon showing that the debtor is insolvent or likely to become insolvent. The court would have to be satisfied that there was a reasonable prospect of rehabilitating the company, or that the interests of all concerned would be better served by this form of insolvency procedure. Upon the appointment of an administrator, the rights of the creditors are suspended, except with leave of the court.¹¹⁴

¹⁰⁷ *In re North Carolina Estate Co.*, 5 T.L.R. 328 (Ch. 1889).

¹⁰⁸ *In re Oriental Inland Steam Co.*, 9 L.R.-Ch. App. 557 (1874) (at least where he seeks to prove in the liquidation for other sums due to him).

¹⁰⁹ A debenture is a document that either creates or acknowledges a debt. Usually it is accompanied by the creation of security. The security is either a fixed charge over specific assets of the debtor (for instance, real property or book debts) or a floating charge over the whole of the undertaking of the debtor including present and future assets. A "debenture holder" is the secured creditor who holds a debenture. Graham, *supra* note 74, at 2-6.

¹¹⁰ If appointed manager and receiver, the receiver-manager also will carry on the debtor's business with the aim of satisfying the debenture holder's claim.

¹¹¹ See generally R. WALTON, *KERR ON THE LAW AND PRACTICE AS TO RECEIVERS* (16th ed. 1983); Insolvency Bill, *supra* note 80, at pt. II, ch. III.

¹¹² For example, the debtor may make an assignment for the benefit of creditors under the Deeds of Arrangement Act, 1914, 4 & 5 Geo. 5, ch. 47, or a scheme of arrangement under the Companies Act § 206. See also Insolvency Bill, *supra* note 80, at pt. III, ch. I and *infra* note 114 and accompanying text.

¹¹³ Graham, *supra* note 74, at 11. See also "Insolvency Law and Practice." DEP'T OF TRADE AND INDUSTRY, CMD., No. 8558, ¶¶ 358, 400 (1983).

¹¹⁴ See Insolvency Bill, *supra* note 80, at pt. II, ch. II.

b. *Protecting Assets in England*

Numerous possibilities are available to the U.S. Debtor to protect its assets located in England. The success of each course of action depends, however, on the particular facts of each case and thus is not easily predicted.¹¹⁵ No formal steps are necessary for the U.S. Debtor to be recognized as the legal representative or "foreign trustee" of the estate to establish standing to collect assets located in England.¹¹⁶ As a general principle, English law recognizes a trustee serving under a foreign bankruptcy proceeding¹¹⁷ and the general assignment of assets to the foreign trustee where this is the effect in the foreign jurisdiction.¹¹⁸

Success of the foreign trustee in collecting assets may depend on whether creditors previously have attached, garnished, or otherwise seized assets. Thus, prompt action by the U.S. Debtor is critical.¹¹⁹ Even real property may be collected by the U.S. Debtor, although no direct assignment is recognized, if the U.S. Debtor holds rights to the property arising from an in personam judgment.¹²⁰ In certain cases, the powers of the foreign trustee may be recognized as an "auxiliary receivership" assisting in a foreign execution.¹²¹ English courts also will recognize the authority of a foreign liquidator, if appointed under the jurisdiction of the company's incorporation.

¹¹⁵ See, e.g., Riesenfeld, *supra* note 61, at 296-99 and cases cited therein; Nadelmann, *Codification of Conflicts Rules for Bankruptcy*, XXX ANNUAIRE SUISSE DE DROIT INTERNATIONAL 57, 83-84 (1975).

¹¹⁶ It may be necessary, however, to have certified evidence of appointment by the U.S. bankruptcy court available for presentation. See *supra* note 18.

¹¹⁷ *Solomons v. Ross*, 126 Eng. Rep. 79 (Ch. 1764); Riesenfeld, *supra* note 61, at 296-98.

¹¹⁸ Such assignment will be recognized with regard to "movables" or personal property but not with regard to "immovables" (including, for instance, leaseholds and real property) situated in England. In addition, assignment will be recognized only if the foreign court had proper jurisdiction based on English law (*i.e.*, debtor's domicile, carrying on business there, or voluntary submission to jurisdiction). Finally, the assignment will be recognized only if foreign law provides for extraterritorial reach over the worldwide assets of the debtor. See 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-138 to 3-140.

¹¹⁹ The test in such a case is: could the bankrupt have assigned to the trustee, at the date when the foreign trustee's title accrued, the assets or debts in question situated in England? *Galbraith v. Grimshaw*, 1910 A.C. 508, 511. Note, however, that in a foreign proceeding comparable to a compulsory winding up, attachment by a creditor in England may be valid, even if subsequent to the foreign proceeding. *In re Suidair Int'l Airways, Ltd.*, [1951] Ch. D. 165.

¹²⁰ 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-141. English courts may authorize the appointment of a foreign trustee as a receiver of the proceeds from sale of real property to be held in trust for the estate. *In re Kooperman*, [1982] 13 B. & C.R. 49.

¹²¹ 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-142. This principle is similar to the basis for a § 304 proceeding under the U.S. Bankruptcy Code. An English court can, by its own order, set up an auxiliary receivership in England where a foreign receiver has been appointed for a debtor's property. This will be done only if there is sufficient connection between the debtor and the jurisdiction where the foreign receiver was appointed to justify recognition of the foreign court's receivership order, based on English conflict of laws principles. *Schemmer v. Property Resources Ltd.*, [1975] Ch. 273.

Alternatively, the U.S. Debtor may petition for a winding up in England and request that such action be treated as ancillary to the U.S. bankruptcy proceeding. Such action, if successful, will stall the action of individual creditors, provide time to formulate a plan for the disposition of assets in England, and ensure that all debts ultimately are discharged.¹²²

Finally, if a winding-up petition as ancillary to a U.S. action is unavailable, the U.S. Debtor may present a petition for winding up as a separate administration. The English liquidator probably will not seek to collect assets outside England for the satisfaction of creditors.¹²³ It also is possible to conduct a multiple administration in which the English liquidator pools assets with the U.S. Debtor to provide for a ratable distribution of the estate to all creditors.¹²⁴

The practitioner should be aware of additional problems that may arise for the debtor in removing assets from England. Counsel should be prepared particularly to handle claims of English tax authorities or the intervention of a secured English creditor¹²⁵ seeking appointment of a receiver for collateral located in England.¹²⁶

c. Seizure of Assets by Foreign Creditors and the U.S. Debtor's Response

Prior to any bankruptcy proceeding, the secured creditor, in particular a debenture holder,¹²⁷ may appoint a receiver-manager over the assets that are security for the amounts owed.¹²⁸ Immediately upon appointment, the receiver takes control of all applicable property and, in some instances, the U.S. Debtor's business, to ensure that the debt is paid. There is little the U.S. Debtor can do to counter the appointment of a receiver, and such appointment remains effective even after a winding-up petition is filed.¹²⁹

¹²² Graham, *supra* note 74, at 23.

¹²³ *Id.* at 24.

¹²⁴ 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-144 & n.70a. This principle also applies to bankruptcy.

¹²⁵ See *supra* note 109.

¹²⁶ Graham, *supra* note 74, at 22-23.

¹²⁷ See *supra* note 109.

¹²⁸ See Graham, *supra* note 74, at 12-14. Such appointment may occur even after a winding-up order is granted by the English court; however, the receiver must apply to the court (or liquidator) to take possession of property of which he has not already taken possession.

¹²⁹ For a discussion of the powers of, and procedures followed by, the receiver and manager appointed by a debenture holder, see Graham, *supra* note 74, at 12-14. The U.S. Debtor can ascertain, however, whether the charge under which the receiver was appointed was valid. As a result of the application of section 320 of the Companies Act (relating to fraudulent preference), or section 322 of that Act (relating to the possible invalidity of floating charges), a winding-up order may have the effect of invalidating either the whole, or part, of the charges in respect to which the receivers have been appointed. As a result, the appointment may be either pro tanto or wholly invalidated.

Section 320 relates to charges given within six months of the date of presentation of

The unsecured creditor may freeze the U.S. Debtor's assets upon proof that the U.S. Debtor may hide or remove its assets from England to the detriment of the creditor.¹³⁰ The U.S. Debtor may defend against this assertion by a showing that no such action has been taken and no such intent exists.

Despite a pending bankruptcy in the United States, English courts will allow English or foreign creditors to enforce judgments against the debtor.¹³¹ With regard to movables or personal property, control will pass to the U.S. trustee subject to charges created prior to the bankruptcy adjudication. The U.S. Debtor may respond to the creditor's actions by petitioning for winding up in England to ensure a complete disposition of all claims.

A creditor also might be in a position to regain possession of goods in respect of which payment has not been made by the U.S. Debtor where those goods have been supplied under a contract containing a "Romalpa" clause.¹³² If the liquidator or receiver wrongly disposes of the goods, a cause of action will exist for damages.

The creditor also may petition for the winding up of the U.S. Debtor by the court with proper jurisdiction based on either doing business in England, or simply having assets in England.¹³³ The U.S. Debtor may raise defenses such as maliciousness, abuse of process, or substantial solvency. Alternatively, the U.S. Debtor may petition the court to recognize the English proceedings as ancillary to the U.S. bankruptcy court proceedings to coordinate administration and discharge all debts.

4. France

a. Bankruptcy Law

French bankruptcy law has been restructured and modified significantly by two recent laws. The first law, known as Prevention and Amicable Settlement of Difficulties Experienced by Business Con-

the petition, and section 322 relates to floating charges given within twelve months of that date. Companies Act § 320, 322. Furthermore, if the charge under which the receiver was appointed was registrable under section 95 of the Companies Act but was unregistered, it would be void against a liquidator, and therefore, would have the effect of invalidating the appointment of the receiver. Companies Act § 95.

¹³⁰ A relatively recent development in English law, known as "Mareva" jurisdiction, has led to the availability of an injunction that allows the creditor "to freeze the assets of a debtor where there is credible evidence that prior to obtaining a judgment, he might surreptitiously make away with or conceal his assets." See Graham, *supra* note 74, at 7-8.

¹³¹ *Id.* at 23.

¹³² The exact circumstances in which the Romalpa clause will be effective is a matter of some debate. Such clauses sometimes are treated as void against the liquidator for want of registration under the Companies Act § 95. The latest judicial authority on such clauses is *Clough Mill Ltd. v. Martin*, [1984] 3 All E.R. 982.

¹³³ Graham, *supra* note 74, at 15.

cerns (the 1984 Law), became effective March 2, 1985.¹³⁴ The 1984 Law provides for a new out-of-court settlement procedure for debtors and creditors and certain internal corporate procedures to monitor the activities of French businesses.¹³⁵

The second law, the Judicial Recovery and Liquidation of Business Concerns (the 1985 Law), becomes effective no later than January 1, 1986.¹³⁶ The 1985 Law substitutes a single procedure for the three procedures that existed under the 1967 bankruptcy laws.¹³⁷ Under the 1985 Law, judicial recovery of a business concern is divided into two stages: a preliminary observation stage, which includes the preparation of a restructuring plan, and a second stage during which either the restructuring plan is enforced or the company is liquidated. The 1985 Law also provides for a simpler procedure for small business concerns. Generally, France and other civil law countries equate bankruptcy with a judgment, thereby providing the legal foundation for applying the French system of recognition of judgments to foreign bankruptcy proceedings.¹³⁸

Judicial reorganization and liquidation proceedings may be instituted for both French individuals and companies. Proceedings also may be initiated for foreign entities that have an established branch, regularly carry on business, or possess assets in France. Jurisdiction also may be assumed over a foreign entity engaged in commercial activity.¹³⁹ Furthermore, the broad jurisdictional reach of article 14 of the French Civil Code allows a French creditor to initiate bankruptcy proceedings against any foreign entity, based upon the right of French nationals to bring actions in French courts.¹⁴⁰ French bankruptcy proceedings assert universal jurisdiction over assets of the debtor,¹⁴¹ although in certain instances multiple administrations in bankruptcy may be recognized.¹⁴²

Judicial recovery or liquidation of assets is initiated by a court determination of cessation of payment by the debtor.¹⁴³ The debtor, a creditor, or the appropriate court or prosecutor may commence proceedings leading to a court declaration of cessation of pay-

¹³⁴ 1984 JOURNAL OFFICIEL DE LA REPUBLIQUE FRANCAISE 751. The authors express thanks to White & Case, Paris, for their assistance in preparing this section.

¹³⁵ See Lorotte, *France—Bankruptcy*, 2 WEST'S INT'L L. BULL. 28 (1984).

¹³⁶ 1985 JOURNAL OFFICIEL DE LA REPUBLIQUE FRANCAISE 1097.

¹³⁷ For a summary of the 1967 bankruptcy laws of France in English, see Pichard & Cie, *The Commercial Laws of France*, III DIGEST OF COMMERCIAL LAWS OF THE WORLD 37-43 (1978).

¹³⁸ 1 J. DALHUISEN, *supra* note 6, § 2.01[1], at 3-100, and § 2.01[2], at 3-114 to 3-115. See *infra* text accompanying note 147.

¹³⁹ 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-134.2 n.19.

¹⁴⁰ See Nadelmann, *supra* note 115, at 93.

¹⁴¹ See Riesenfeld, *supra* note 61, at 301.

¹⁴² See, e.g., 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-134.2 n.18.

¹⁴³ BOUSSARD, LEVIN & BIGBIE, *Creditor's Rights Against Business Debtors—France*, 1983 A.B.A. INST. ON INT'L WORKOUTS & BANKR. 56, 61.

ment.¹⁴⁴ The procedure can be initiated when the debtor has not fulfilled his obligations under an amicable settlement concluded in conformity with the 1984 Law. Furthermore, the 1985 Law provides that the employees' committee or representatives confidentially may inform the court of any evidence of cessation of payments.

Cessation of payment often is referred to as the "state of cessation of payment" and is similar to an equity-insolvency test.¹⁴⁵ Although complex in definition, and often determined on a case-by-case basis, cessation of payment usually was defined as failure to pay one or more liquidated debts while experiencing financial difficulties that cannot be remedied.¹⁴⁶ The concept is defined now in the 1985 Law as the inability to pay current liabilities with current assets.

In addition to declaring a cessation of payment, the court establishes the date of cessation, which may not be more than eighteen months prior to the bankruptcy adjudication. When the court has decided to initiate judicial recovery, a three-month observation period, which may be extended to a maximum of one year, begins as of the date of the court's judgment.

The court appoints three parties necessary to the recovery procedure: (i) a commissary-judge ("*juge-commissaire*") who is responsible for supervising the proceedings; (ii) a trustee ("*administrateur*") who is responsible for preparing a report on the business concern, supervising the management of the concern during the observation period, and submitting the restructuring plan to the court; and (iii) a creditors' representative ("*representant des creanciers*") who represents the interests of all the creditors. In addition, a representative of the employees, appointed through the employees' committee or representatives or directly by the employees, participates in the procedure.

During the observation period, the trustee prepares a report on the economic, corporate, and labor situation of the concern. Based on the report, the trustee proposes to the court that either the business be liquidated or that a restructuring plan be adopted. The restructuring plan is adopted by the court after hearing the debtor, the trustee, and the creditors' and employees' representatives. The objective of such a plan is the continuation of the debtor's business.

The recent laws primarily will affect domestic concerns in France and reflect a continuing concern for the survival of French businesses during difficult economic periods. Although it is too soon to determine the real impact of the two new laws on French business concerns, some elements already may be emphasized. First, the rather lengthy proceedings that the new laws require and the in-

¹⁴⁴ *Id.* at 60-61.

¹⁴⁵ See generally Honsberger, *supra* note 51, at 154.

¹⁴⁶ Boussard, Levin & Bigbie, *supra* note 143, at 62.

volvement of a greater number of parties in the restructuring or work-out process might reduce the effectiveness of the new laws. Second, the increased importance given to the employees' representatives may impede the saving of distressed companies. On the positive side, the new monitoring procedures should forewarn certain companies of difficulties early enough to solve their problems, and should improve the chances of survival of a business concern within a judicial recovery procedure.

Generally, a foreign debtor may be declared bankrupt in French courts and will be treated in a manner similar to a French debtor. On the other hand, if the foreign debtor is involved in a foreign bankruptcy proceeding, it may seek recognition and enforcement of the foreign proceeding through a procedure known as *exequatur*.¹⁴⁷ No special proceeding ancillary to a foreign bankruptcy proceeding exists under French law.¹⁴⁸ It may be possible, however, to obtain recognition of a foreign trustee without *exequatur* for certain limited purposes, such as collecting debts owed to the debtor or obtaining an attachment lien to preserve property for the estate.¹⁴⁹

To secure the broad power to collect assets in France, however, formal recognition through the *exequatur* is necessary. Although partial *exequatur* may be obtained for limited purposes, it cannot be relied upon for power beyond its defined scope.¹⁵⁰ Thus, full *exequatur* power usually is sought. *Exequatur* may not be available to the foreign debtor, however, if a French creditor already has acted to attach, garnish, or otherwise seize assets or to declare the debtor bankrupt in France.

b. *Protecting Assets in France*

Prompt action by the U.S. Debtor is critical when assets are located in France. The initiatives of French creditors to freeze or obtain assets, or to have the U.S. Debtor declared bankrupt in France, may prevent or obstruct the U.S. Debtor from protecting assets that are located in France.

If the assets located in France consist of debts owed by third parties, immediately the U.S. Debtor should seek to collect the debts as the foreign representative of the estate. Under general principles of French recognition of the powers of foreign bankruptcy trustees, formal recognition is not necessary.¹⁵¹ Such action, without *exequatur*, may forestall the action of creditors that would occur while obtaining *exequatur* in court. Chapter 11 reorganization proceedings

¹⁴⁷ See 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-134.1; Nadelmann, *supra* note 115, at 93.

¹⁴⁸ Boussard, Levin & Bigbie, *supra* note 143, at 73.

¹⁴⁹ Riesenfeld, *supra* note 61, at 301.

¹⁵⁰ See Nadelmann, *supra* note 115, at 93.

¹⁵¹ See, e.g., 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-134.1.

are recognized automatically in French courts without *exequatur*.¹⁵²

Alternatively, a partial *exequatur* may be sought by the U.S. Debtor to obtain formal recognition by the French court for the U.S. Debtor to perform certain specified actions, ancillary to the U.S. bankruptcy proceeding, to protect and marshal French assets. Particular care must be taken, however, to define the parameters of the partial *exequatur* broadly enough to cover all conceivable actions that the U.S. Debtor may wish to institute in France.¹⁵³

When assets in France are more varied and substantial, the U.S. Debtor should initiate *exequatur* proceedings in the French court to obtain formal recognition of the foreign bankruptcy proceeding and of the U.S. Debtor's status to act in France. *Exequatur* is not retroactive, however, and seizure of assets by creditors prior to *exequatur* may be upheld by French courts.¹⁵⁴ If this occurs, there is some possibility of seeking a local bankruptcy declaration that removes such preferences.¹⁵⁵

Finally, the U.S. Debtor may seek declaration of a separate, concurrent bankruptcy proceeding in France, resulting in multiple administrations of the estate. Some amount of commercial activity or the presence of assets in France usually will suffice to confer jurisdiction.¹⁵⁶ Substantial benefits may be derived by the U.S. Debtor in following this course of action. First, if only partial *exequatur* can be obtained, a bankruptcy declaration will be of broader scope, bringing all assets and creditors before the court. Second, the proceeding in bankruptcy invalidates all existing attachments and ensures an equitable administration of assets and the satisfaction of all French creditors.

c. Seizure of Assets by Foreign Creditors and the U.S. Debtor's Response

Numerous remedies outside bankruptcy proceedings are available to the French creditor wishing to seize assets of the U.S. Debtor located in France.¹⁵⁷ For example, the following remedies generally are available as provisional or execution remedies: (1) attachment of movables; (2) garnishment of debts owed to the U.S. Debtor or of U.S. Debtor's goods held by third parties; (3) lien on contents or

¹⁵² Boussard, Levin & Bigbie, *supra* note 143, at 95. Such automatic recognition is available for certain preventive measures that protect the debtor, and thus applies to Chapter 11 proceedings but not to Chapter 7 proceedings under the U.S. Bankruptcy Code. *Id.*

¹⁵³ See 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-134; Nadelmann, *supra* note 115, at 93.

¹⁵⁴ 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-134.1.

¹⁵⁵ Nadelmann, *supra* note 115, at 93.

¹⁵⁶ See *supra* text accompanying note 142.

¹⁵⁷ For a more detailed discussion of remedies for French creditors and the effects, see 1 J. DALHUISEN, *supra* note 6, § 2.01[2], at 3-105 n.10.

proceeds of leased property; (4) judgment lien on real property; and (5) order preventing valid transfer of movable property.¹⁵⁸

Once the French creditor has taken such an action, obtaining *exequatur* to recognize the foreign bankruptcy proceeding is unlikely to affect rights of the creditors.¹⁵⁹ The U.S. Debtor's best response is to declare bankruptcy in French courts, which serves to invalidate the effect of many rights under such prior actions.¹⁶⁰

The creditor also may seek the appointment of an administrator by the Commercial Court temporarily to manage the U.S. Debtor's assets in France. The creditor must show that the U.S. Debtor's management may misuse assets to the creditor's detriment or for its own benefit. Such a showing is difficult, and many creditor-initiated appointments have been overturned.¹⁶¹

Finally, a creditor may seek a declaration of cessation of payment, placing the U.S. Debtor into bankruptcy proceedings in France. The U.S. Debtor may defend by showing that no cessation of payment has occurred. Once the French proceeding is formally underway, it is unlikely that *exequatur* may be obtained.¹⁶² French bankruptcy declared concurrently with U.S. proceedings may be limited to French assets, although the scope of bankruptcy proceedings in such cases is uncertain. Finally, a foreign composition or a U.S. Chapter 11 reorganization proceeding may be a defense in French bankruptcy proceedings.¹⁶³

5. Germany

a. Bankruptcy Law

Two types of relief are available in Germany for the insolvent debtor, and each is governed by a separate statutory framework. The debtor or a creditor may seek to have the debtor declared bankrupt, which leads to liquidation of the debtor's business. Such action is governed by the Bankruptcy Law of 1877, as amended.¹⁶⁴ Alternatively, the debtor may propose a composition where creditors waive up to sixty-five percent of their claims and the debtor continues business. Such judicial arrangements, often involving a moratorium, are governed by the Composition Law of 1935.¹⁶⁵ A debtor

¹⁵⁸ *Id.*

¹⁵⁹ See *supra* text accompanying note 154. But see *supra* text accompanying note 155.

¹⁶⁰ See 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-134.2 to 3-134.3.

¹⁶¹ Boussard, Levin & Bigbie, *supra* note 143, at 52-53.

¹⁶² *Id.* at 95.

¹⁶³ 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-134.2 n.17.

¹⁶⁴ Konkursordnung, 1877 Reichsgesetzblatt [RGBL] S 351 (W. Ger.). For a synoptical translation of the Konkursordnung in English, see M. PELTZER, GERMAN INSOLVENCY LAWS 26-130 (1975). The authors express thanks to Westrick & Eckholdt, Frankfurt, for their assistance in preparing this section.

¹⁶⁵ Vergleichsordnung, 1935 RGBL I 321 (W. Ger.). For a synoptical translation of the Vergleichsordnung in English, see M. PELTZER, *supra* note 164, at 131-206.

must apply for composition or relief in bankruptcy if it cannot satisfy its liabilities or if its liabilities exceed its assets.¹⁶⁶ Both proceedings protect the debtor from actions of creditors and are effective as to the debtor's assets outside Germany if the foreign jurisdiction respects and recognizes the German proceedings—a rare situation.¹⁶⁷

In bankruptcy proceedings, the court appoints an administrator who is responsible for selling the debtor's assets to satisfy outstanding claims. An established statutory order of priority exists for the satisfaction of claims in a liquidation action. Foreign creditors may obtain satisfaction on an equal basis with domestic creditors.¹⁶⁸ Certain transfers of assets or payments by the debtor prior to bankruptcy, such as those creating a preference for one or more creditors to the detriment of others, those made for inadequate consideration, or those by the debtor acting in conspiracy with others to damage creditors, may be recoverable for the debtor's estate.¹⁶⁹

During composition proceedings, the court will take whatever actions are necessary to ensure that the debtor's assets are not dissipated and that the financial status of the debtor is not altered to the detriment of creditors. A composition agreement may not require creditors to waive more than sixty-five percent of their claims. If upon examination of the debtor's business, the court finds that the debtor is unable to pay at least thirty-five percent of its claims, the court will deny composition and initiate bankruptcy proceedings.¹⁷⁰ If composition proceedings are opened by the court, the debtor will remain as manager of its business under the supervision of a court-appointed administrator. The composition agreement is subject to approval by the majority of the creditors present at the meeting (including written votes delivered in advance) and, further, by three-fourths of all the outstanding claims by monetary value, which latter majority increases to four-fifths if the debtor offers a settlement providing for a return to creditors of less than fifty percent.

Bankruptcy in Germany generally is considered a creditor's remedy and an enforcement device, unlike the French view, which perceives bankruptcy as a judgment.¹⁷¹ This general approach to bankruptcy in Germany provides no framework for the recognition of foreign bankruptcy proceedings, foreign judgments, or the powers of foreign trustees.¹⁷² Even if a foreign proceeding is pending, German creditors may obtain executions on the debtor's assets in

¹⁶⁶ See generally H. WURDINGER, *GERMAN COMPANY LAW* 118-20 (1975).

¹⁶⁷ Minton & Westrick, *Creditors' Rights Against Business Debtors (Germany)*, 1983 A.B.A. INST. ON INT'L WORKOUTS & BANKR. 21.

¹⁶⁸ *Id.* at 18-20.

¹⁶⁹ *Id.* at 22-23.

¹⁷⁰ *Id.* at 8-9.

¹⁷¹ J. DALHUISEN, *supra* note 6, § 2.01[2], at 3-114. See also *supra* note 138 and accompanying text.

¹⁷² J. DALHUISEN, *supra* note 6, § 2.01[2], at 3-114.

Germany.¹⁷³ Furthermore, a foreign trustee in bankruptcy might not be recognized, leaving the bankrupt debtor in control of the estate in Germany.¹⁷⁴

In general, foreign compositions and discharges will have no effect in Germany.¹⁷⁵ Consequently, except in limited situations, the debtor must submit to, or initiate, actions in German courts to protect its German assets. The debtor's final obstacle is establishing jurisdiction to come before the German courts. Mere presence of assets in Germany does not appear to be sufficient for declaration of bankruptcy in Germany.¹⁷⁶ A branch or office located in Germany, or the leasing of property in Germany, however, may be sufficient to confer jurisdiction.¹⁷⁷

b. Protecting Assets in Germany

Only in limited circumstances will the U.S. Debtor be able to obtain the recognition necessary to protect its assets in Germany. A foreign trustee in bankruptcy may be able to recover debts owed to the U.S. Debtor by third parties in Germany.¹⁷⁸ To accomplish virtually anything other than the collection of debts, however, the U.S. Debtor should file for bankruptcy in German courts if jurisdiction can be established. If jurisdiction is conferred, concurrent German proceedings may be limited to the assets located in Germany.¹⁷⁹ Foreign trustees have been recognized by German courts as having powers to file for bankruptcy relief in Germany, and then to negotiate with the German trustee concerning matters related to the disposition of the estate.¹⁸⁰

Perhaps it is more critical in Germany than in other foreign jurisdictions for the U.S. Debtor to act promptly either to obtain recognition of the U.S. bankruptcy proceeding or to declare bankruptcy. German creditors may obtain executions against assets that will be upheld or given preference, notwithstanding composition or bankruptcy proceedings pending in foreign jurisdictions.¹⁸¹ Similarly,

¹⁷³ See Minton & Westrick, *supra* note 167, at 25.

¹⁷⁴ Nadelmann, *supra* note 115, at 88. Earlier decisions were more favorable than recent decisions to the recognition of foreign trustees of bankrupt corporations. See, e.g., Riesenfeld, *supra* note 61, at text accompanying notes 86, 88.

¹⁷⁵ Nadelmann, *supra* note 115, at 95.

¹⁷⁶ *Id.* at 82-83.

¹⁷⁷ See 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-135 n.38.

¹⁷⁸ *Id.* at 3-134.5; Riesenfeld, *supra* note 61, at 304-05.

¹⁷⁹ 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-134.7 n.38.

¹⁸⁰ Riesenfeld, *supra* note 61, at 305; 1 J. DALHUISEN, *supra* note 6, § 2.02[1], at 3-134.5 to 3-134.6. The basis for such recognition is not clear in most authorities, and thus, whether such recognition might be extended to the debtor in possession in Chapter 11 proceedings is uncertain.

¹⁸¹ Nadelmann, *supra* note 115, at 80, 82. There is a tendency developing in German jurisprudence, however, to pay more attention to foreign bankruptcy proceedings when it comes to execution against assets located in Germany.

preexisting liens, attachments, or garnishments exercised in Germany remain in effect, even though bankruptcy in Germany is declared, and are valid until the claim is settled. Also subject to challenge are those attachments that have taken place ten days before bankruptcy filing has occurred or within ten days before the debtor generally has ceased to pay its debts. Only attachments or other similar actions of creditors after the German bankruptcy or composition filing are ineffective.¹⁸² The principle of "first in time" is upheld vigorously in German proceedings and may therefore give local creditors a significant advantage in obtaining satisfaction for their claims from the U.S. Debtor's assets in Germany.

c. Seizure of Assets by Foreign Creditors and the U.S. Debtor's Response

The primary remedy for the German creditor attempting to seize German assets to satisfy its claim is a device known as the *din-glicher Arrest*. The *Arrest* is a general order that is the basis for a relatively unified system of attachment and garnishment of movable, immovable, and intangible property. The *Arrest* sets forth the amount and nature of the creditor's claim, without specifying assets or allowing the seizure itself. The creditor then obtains another order based on the *Arrest* that identifies assets to be seized and authorizes the creditor to seize them. Thereafter, the parties proceed with an action on the merits.¹⁸³ The *Arrest* is available as a remedy to creditors only if an *Arrestgrund* or *Arrest* reason exists. Although an imminent or expected insolvency would not be an *Arrest* reason, such *Arrestgrund* would exist if a creditor had grounds to believe, and could confirm by affidavit, that the debtor was about to dissipate assets of the estate to the detriment of the creditors.

Other than denying the existence of the claim or showing solvency, there is little the U.S. Debtor can do to protect its German assets once the creditor acts to seize them. Thus, the U.S. Debtor's action prior to initiatives by German creditors is very important. To minimize the dissipation of assets to local creditors, the U.S. Debtor should respond by seeking bankruptcy or composition relief in Germany immediately after filing for relief under the U.S. Bankruptcy Code. Such action at least will forestall any subsequent actions of creditors.

¹⁸² 1 J. DALHUISEN, *supra* note 6, § 2.01[2], at 3-110 n.10.

¹⁸³ *Id.* Note that the *Arrest* and succeeding seizure order may be used as either provisional or execution remedies.

6. Japan

a. Bankruptcy Law

Bankruptcy proceedings in Japan include straight bankruptcy, arrangement or composition, and reorganization. The basis for a straight bankruptcy proceeding, which is governed by Bankruptcy Law,¹⁸⁴ is insolvency of the debtor. For a corporate debtor, liabilities in excess of assets is sufficient to show insolvency. Straight bankruptcy is voluntary when initiated by the debtor and involuntary when filed by a creditor.

Reorganization proceedings are governed by certain provisions of the Commercial Code¹⁸⁵ and the Corporate Reorganization Law.¹⁸⁶ A sufficient basis for reorganization relief exists if the debtor's liabilities exceed assets or if insolvency is impending.¹⁸⁷ At least two-thirds of unsecured creditors and up to four-fifths of secured creditors must approve the plan. Like bankruptcy, reorganization may be voluntary or involuntary.

Arrangements and compositions are governed by Composition Law,¹⁸⁸ and such actions may be initiated only by the debtor. At least seventy-five percent in known value of creditors must approve a plan for composition.¹⁸⁹

Jurisdiction in Japanese bankruptcy or related proceedings is generally territorial in scope, and actions are effective only as to assets located in Japan.¹⁹⁰ As long as assets are located in Japan, regardless of whether they are related to the claims of creditors, there is jurisdiction for straight bankruptcy relief.¹⁹¹ Foreign entities are treated on an equal basis with domestic debtors if reciprocity exists between the two countries.¹⁹²

Once bankruptcy proceedings have been initiated, the Japanese court plays an active role. For example, in reorganizations the court may play a substantial role in drafting the plan of reorganization. The court also appoints a receiver who supervises and approves the disposition of assets in bankruptcy proceedings. If the debtor peti-

¹⁸⁴ For a summary of Japanese bankruptcy and creditors' remedies law in English, see Logan, Okamoto & Takashima, *The Commercial Laws of Japan*, IV DIGEST OF COMMERCIAL LAWS OF THE WORLD 21-25 (1982) [hereinafter cited as *Commercial Laws of Japan*]. The authors express thanks to Koji Takeuchi—Kawai, Takeuchi, Nishimura & Inoue, Toyko, for his assistance in preparing this section.

¹⁸⁵ *Id.*

¹⁸⁶ *Id.*

¹⁸⁷ See Takeuchi & Butler, *Creditors' Rights and Bankruptcy Law in Japan*, 1983 A.B.A. INST. ON INT'L WORKOUTS & BANKR. 52.

¹⁸⁸ See *Commercial Laws of Japan*, *supra* note 184.

¹⁸⁹ See *id.* at 22.

¹⁹⁰ Takeuchi & Butler, *supra* note 187, at 62.

¹⁹¹ As to reorganization relief, establishment of an office is required.

¹⁹² See *Commercial Laws of Japan*, *supra* note 184, at 21-22; but see Takeuchi & Butler, *supra* note 187, at 58-59, 61.

tions for composition during a bankruptcy proceeding, the court must approve the composition plan. If the creditors do not approve the composition plan, the court proceeds with bankruptcy action. The length of time involved in a proceeding in Japan varies widely from an average of two years for a straight bankruptcy proceeding to as much as ten or more years in a reorganization.

Foreign orders in bankruptcy are void as to the debtor's property in Japan by provisions of both the bankruptcy and reorganization statutes.¹⁹³ Similarly, a discharge in the foreign proceeding is ineffective against creditors in Japan. Once the debtor has been declared bankrupt in a foreign jurisdiction, however, a Japanese creditor may petition to declare the debtor bankrupt in Japan, using the foreign adjudication as the basis of his petition without setting forth proof of an act of bankruptcy by the debtor as required under Japanese law.¹⁹⁴

b. Protecting Assets in Japan

Japanese bankruptcy law does not recognize foreign bankruptcy proceedings.¹⁹⁵ Thus, the best protective action the U.S. Debtor can take is to seek relief through bankruptcy, reorganization, or composition proceedings in Japan. One of the basic principles of U.S. bankruptcy law is that all creditors shall be treated equally.¹⁹⁶ This constitutes a basis for proof that reciprocity exists in the United States, and thereby provides access to the Japanese courts for the U.S. Debtor.¹⁹⁷

c. Seizure of Assets by Foreign Creditors and the U.S. Debtor's Response

The creditor in Japan may use prejudgment attachment, garnishment, injunctions, or seizure orders to obtain the U.S. Debtor's assets in Japan. In certain situations, collateral may be repossessed by a creditor without action of the court as long as the creditor's ownership rights are clearly recognized. All types of property are subject to such action by creditors.¹⁹⁸

Under Japanese law, prejudgment remedies do not give rise to a judicial lien; therefore, other creditors may attach the same assets

¹⁹³ See Takeuchi & Butler, *supra* note 187, at 62.

¹⁹⁴ *Commercial Laws of Japan*, *supra* note 184, at 23.

¹⁹⁵ See *supra* note 193 and accompanying text.

¹⁹⁶ Equity of distribution among all creditors is a fundamental premise of U.S. bankruptcy law. See, e.g., *Sampson v. Imperial Paper & Color Corp.*, 313 U.S. 215, 219 (1941); *Buchanan v. Smith*, 83 U.S. 277, 301 (1872); *In re Iowa Premium Serv. Co.*, 12 Bankr. 597, 599 (Bankr. S.D. Iowa 1981), *aff'd*, 676 F.2d 1220, *rev'd on other grounds*, 695 F.2d 1109 (8th Cir. 1982).

¹⁹⁷ See *supra* text accompanying note 192.

¹⁹⁸ Takeuchi & Butler, *supra* note 187, at 45-46.

during a specified period and become entitled to equal distribution of proceeds with prior creditors who have attached the property. Consequently, such actions may be as effective as bankruptcy proceedings with regard to equal distribution of assets among creditors.

The U.S. Debtor may reacquire seized property pending a disposition on the merits by posting a bond in the amount of the creditor's claim. Because foreign bankruptcy orders are not recognized, the U.S. Debtor either should file voluntary bankruptcy in Japan, or seek relief under the composition or reorganization statutes. This ensures that assets are equitably allocated and that all claims in that jurisdiction are satisfied.

Although security interests can be enforced outside a proceeding in bankruptcy, unsecured claims or existing executions are void. No claims are enforceable outside a reorganization plan adopted pursuant to the Corporate Reorganization Law.¹⁹⁹ Japan's territorial basis for bankruptcy jurisdiction allows for multiple administrations with each jurisdiction's court affecting only the assets within its territorial limits.

7. Mexico

a. Bankruptcy Law

Bankruptcy proceedings in Mexico are governed by federal statutes adopted in 1943 (Mexican Bankruptcy Law) that incorporate much of the bankruptcy procedure of Spain.²⁰⁰ The Mexican Bankruptcy Law has been highly criticized because of its age and its inconsistencies, which have led to ambiguity in its interpretation.²⁰¹ In addition, many procedures and substantive principles under Mexican Bankruptcy Law are difficult to implement and are used so rarely that they are virtually unavailable.²⁰² Generally, litigation in Mexico is time-consuming and expensive and requires careful attention to complicated procedures.²⁰³ Such problems become magnified for the foreign debtor attempting to protect its assets in Mexico.

Three types of proceedings exist in Mexico: (1) involuntary bankruptcy leading to liquidation or reorganization; (2) voluntary bankruptcy initiated by the debtor and leading to liquidation or reorganization; and (3) suspension of payments with subsequent reor-

¹⁹⁹ *Id.* at 62-63.

²⁰⁰ For a summary of Mexican bankruptcy law in English, see Lic. Federico Martinez Montes de Oca, *The Commercial Laws of The Republic of Mexico*, V DIGEST OF COMMERCIAL LAWS OF THE WORLD 22-28 (1978) [hereinafter cited as *Commercial Laws of Mexico*]. See also generally Romo, *Questionnaire on Creditors' Rights Against Business Debtors (Mexico)*, 1983 A.B.A. INST. ON INT'L WORKOUTS & BANKR. 1-68. The authors express thanks to Miguel Angel Hernandez Romo, Mexico City, for his assistance in preparing this section.

²⁰¹ Romo, *supra* note 200, at 24-25.

²⁰² See, e.g., *infra* text accompanying notes 204, 213.

²⁰³ Romo, *supra* note 200, at 66-67.

ganization and continuation of the debtor's business. As a practical matter, however, successful reorganizations are extremely rare, and nearly all proceedings result in liquidation of the company.²⁰⁴

Corporations, partnerships, or individuals engaged in commercial activities may be declared bankrupt upon a showing of cessation of payment by the debtor. A presumption of cessation of payment exists if one of nine statutorily prescribed events occurs.²⁰⁵ Either a creditor or the district attorney may seek to have the debtor declared bankrupt. Although a single creditor may file, at least two creditors must exist to adjudicate the debtor bankrupt.²⁰⁶

Proceedings are brought in the civil and commercial courts, which can play a relevant role depending on the nature of the case.²⁰⁷ A *sindico* is appointed by the court to manage the liquidation of the debtor under the supervision of the court. The creditors appoint an "intervenor" who oversees the *sindico* on behalf of the creditors.²⁰⁸ In general, all actions by creditors are stayed upon the initiation of bankruptcy proceedings.²⁰⁹ The Mexican Bankruptcy Law provides various tests for recovery of preferential or fraudulent transfers to some creditors resulting in the detriment of other creditors.²¹⁰

Mexico has a domiciliary basis for jurisdiction; if the debtor has

²⁰⁴ Very few reorganizations have been successfully concluded without resulting in liquidation, though reorganization is available under Mexican law. Some estimates show that only ten companies in the past twenty years have been reorganized pursuant to a suspension of payments and stayed in business. See Romo, *supra* note 200, at 26.

²⁰⁵ A suspension of payment is presumed in the following cases:

- (1) nonfulfillment, in general, of payment of any liquid and due obligations;
- (2) insufficient property of merchant exists to satisfy claim of creditor when execution has been levied;
- (3) concealment or absence of the merchant without leaving in charge of the company a person legally qualified to meet company obligations;
- (4) under the same circumstances as above, actual closing of the business of the company and branches;
- (5) assignment of properties in favor of certain creditors;
- (6) proceeding, fraudulent or false, meant to avoid complying with any obligations;
- (7) asking to be declared bankrupt;
- (8) requesting stoppage of payments and not doing so, or when such cessation is granted, making no agreement with creditors;
- (9) nonfulfillment of obligations contracted in the agreement, made within the assignment of payment proceedings.

See *Commercial Laws of Mexico*, *supra* note 200, at 23.

²⁰⁶ See also Romo, *supra* note 200, at 43.

²⁰⁷ *Id.* at 28. The court has the power to direct, supervise, and manage the bankruptcy and the estate of the debtor. *Id.* at 28-29.

²⁰⁸ The intervenor may be more than one person; three or five persons commonly serve together in this capacity.

²⁰⁹ Three exceptions exist to this general rule. Foreclosure proceedings on pledged real or personal property may be continued with approval of the court hearing the bankruptcy proceeding. Mexican governmental authorities also may continue to pursue tax liabilities of the debtor. Finally, claims of laborers may receive a separate hearing in a labor court. See generally Romo, *supra* note 200, at 37-38.

²¹⁰ See *id.* at 51.

its domicile or its main office in Mexico, courts have bankruptcy jurisdiction. If the domicile is different from the principal place of business, the main office of the principal place of business is deemed to be the domicile for jurisdiction purposes in declaring bankruptcy. Based on this domiciliary principle, the Mexican branch of a foreign company may be declared bankrupt. Such proceedings will have jurisdiction only over property of the debtor located in Mexico and claims of creditors arising from transactions with the branch in Mexico.²¹¹ This is contrary to the jurisdictional scope of bankruptcy for a Mexican debtor, which reaches assets worldwide. No basis for bankruptcy exists when a foreign corporation has property located in Mexico without the additional presence of a branch or main office.²¹²

No proceeding ancillary to a foreign bankruptcy is available in Mexico. Article 14 of the Mexican Bankruptcy Law generally provides that a foreign bankruptcy decree will not be recognized in Mexico. In theory, however, if the foreign court has proper jurisdiction under Mexican law, the foreign adjudication fully complies with substantive Mexican bankruptcy law. If all applicable procedures are followed to recognize the proceeding in Mexican courts, the decree may be enforced in Mexico.²¹³ The difficulties of obtaining such recognition make this option elusive and the foreign debtor should not consider it seriously.

Similarly, recognition of a foreign trustee in bankruptcy is available in theory if the trustee can show that a right exists under Mexican law to perform whatever actions are proposed. Decisions are made on a case-by-case basis, however, and such showing may be difficult in light of Mexican legal standards.²¹⁴ The prevailing principle regarding bankruptcy procedures is that Mexican law governs proceedings in Mexico,²¹⁵ and only in rare instances will foreign law be applied. More importantly, it is clear that substantive bankruptcy law of a foreign jurisdiction will not apply in Mexican courts.

b. Protecting Assets in Mexico

The U.S. Debtor may take the same steps to protect its assets located in Mexico that a Mexican debtor may take. To strengthen its position, the U.S. Debtor immediately should associate Mexican counsel to evaluate the likelihood that U.S. bankruptcy proceedings or a U.S. trustee or debtor in possession will be recognized in Mexican courts. Because such recognition is unlikely in Mexico,²¹⁶ the

²¹¹ *Commercial Laws of Mexico*, *supra* note 200, at 25; Romo, *supra* note 200, at 40; *see also* Nadelmann, *supra* note 115, at 73.

²¹² Romo, *supra* note 200, at 40-41.

²¹³ *Id.* at 38, 54; *Commercial Laws of Mexico*, *supra* note 200, at 25.

²¹⁴ *See generally* Romo, *supra* note 200, at 54-55.

²¹⁵ *Id.* at 56.

²¹⁶ *See supra* text accompanying note 214.

next step is to determine whether the U.S. Debtor has sufficient presence in Mexico to voluntarily declare bankruptcy in Mexico. Voluntary bankruptcy, in theory, would bring all creditor actions into the bankruptcy proceeding and result in the equitable disposition of all Mexican assets and claims.²¹⁷

If jurisdiction does not exist to voluntarily declare bankruptcy in Mexico, the best alternative may be for the U.S. Debtor to liquidate the assets in Mexico and seek to have the proceeds remitted to the United States for distribution under the U.S. bankruptcy proceeding. Of course, if Mexican creditors have claims against the U.S. Debtor, they are likely to seek a distribution of the assets in Mexico to satisfy local claims. At that point, the U.S. Debtor may defend itself, negotiate with creditors, or offer a bond.

c. Seizure of Assets by Foreign Creditors and the U.S. Debtor's Response

Under provisions of the Federal Commercial Code, prejudgment remedies of attachment and garnishment are available to creditors in Mexico.²¹⁸ Attachment may be had if there is reason to believe that the U.S. Debtor will leave the jurisdiction or conceal or waste its assets. A creditor also may file to have the U.S. Debtor declared bankrupt in Mexico if jurisdiction exists for the Mexican court to adjudicate such claim.²¹⁹ Attachment and garnishment actions may be instituted along with the bankruptcy proceeding if proper evidence of jurisdiction is presented.

The U.S. Debtor's response to a creditor's action must be initiated promptly by Mexican counsel with full power of attorney to act in Mexican court for the U.S. Debtor. The U.S. Debtor may defend by showing solvency, denying the creditor's claim, negotiating for payment of the creditor, or offering a bond. If numerous creditors are involved, the U.S. Debtor must file a petition for agreement that details a plan for distributing assets in satisfaction of all outstanding claims. As mentioned previously, it is unlikely that recognition of a U.S. bankruptcy proceeding will be available to stay or consolidate the Mexican bankruptcy proceedings.

If jurisdiction for bankruptcy does not exist, the creditor will seek to satisfy its claims by proceeding directly against the U.S. Debtor's assets. Since both the voluntary declaration of bankruptcy and the recognition of a foreign proceeding are unlikely, the U.S. Debtor must retain Mexican counsel familiar with debtor-creditor law to respond to such claims in Mexican courts.

²¹⁷ Romo, *supra* note 200, at 29.

²¹⁸ *Id.* at 10; *Commercial Laws of Mexico*, *supra* note 200, at 29-31.

²¹⁹ See *supra* text accompanying notes 211-12.

IV. The U.S. Model: Section 304 Proceedings

A. Background

Protecting assets in foreign countries can be time consuming, costly, and inconvenient. By contrast, the U.S. Bankruptcy Code provides a model designed to complement a principal proceeding abroad.²²⁰ Under section 304 of the Bankruptcy Code, the foreign representative²²¹ voluntarily may file a case ancillary to a foreign proceeding²²² without the commencement of a separate U.S. bankruptcy proceeding.²²³ This allows the foreign representative to administer the assets of the foreign estate located in the United States and to prevent the dismemberment of such assets by local creditors.²²⁴

Section 304 represents a shift toward the recognition of universal jurisdiction and the extraterritorial effect of the foreign bankruptcy laws.²²⁵ The section permits the commencement of a purely ancillary case to assist qualifying foreign estates and to protect the U.S. assets of the foreign estate without requiring a full and duplicate U.S. administration.²²⁶

Section 304(c) prescribes the criteria to which foreign proceed-

²²⁰ See *infra* note 223 and accompanying text.

²²¹ Section 101(20) defines the foreign representative as a "duly selected trustee, administrator, or other representative of an estate in a foreign proceeding." 11 U.S.C. § 101(20) (1982).

²²² Section 101(19) defines a foreign proceeding as a "proceeding, whether judicial or administrative and whether or not under bankruptcy law, in a foreign country in which the debtor's domicile, residence, principal place of business, or principal assets were located at the commencement of such proceeding, for the purpose of liquidating an estate, adjusting debts by composition, extension, or discharge, or effecting a reorganization." 22 U.S.C. § 101(19) (1982).

²²³ See H.R. REP. NO. 595, 95th Cong., 1st Sess. 324 (1977); S. REP. NO. 989, 95th Cong., 2d Sess. 35 (1978).

²²⁴ The foreign representative may file the petition under Section 304 and make an appearance in the case without subjecting himself to the jurisdiction of the United States for any other purpose. 11 U.S.C. § 306 (1982).

²²⁵ This has not always been the case. U.S. courts traditionally rejected the doctrine of universality in the operation of bankruptcy laws and rarely recognized the claims asserted by foreign trustees over the U.S. assets of foreign debtors. See, e.g., *Ogden v. Saunders*, 25 U.S. (12 Wheat.) 213 (1827); *Harrison v. Sterry*, 9 U.S. (5 Cranch) 289 (1809). After these initial decisions, the pendulum swung toward recognition of foreign bankruptcy proceedings based on the principle of comity among nations, at least until the adoption of section 304. See, e.g., cases cited *supra* note 2. For a discussion of this history, see *Riesenfeld, supra* note 61, at 290-96; *Gallagher & Hartje, The Effectiveness of § 304 in Achieving Efficient and Economic Equity in Transnational Insolvency*, 1983 ANN. SURV. BANKR. L. 1 (1983).

²²⁶ See *supra* note 223. The legislative history of section 304 provides that it had no compatible provisions under the Bankruptcy Act of 1898 (the "Bankruptcy Act"). 11 U.S.C. § 304 (1982). Under sections 301 and 303(b)(4) there is still a possibility of a full U.S. case to administer the U.S. assets of a foreign estate. *Id.* §§ 301, 303(b)(4). A full U.S. case previously was provided for by section 2(a)(22) of the Bankruptcy Act, which contemplated the creation of full U.S. cases in international bankruptcies which could then be suspended in favor of foreign proceedings. Section 305 of the Bankruptcy Code permits the suspension of such cases in favor of the foreign proceedings if those foreign proceedings qualify for protection under section 304. *Id.* § 305.

ings must conform to qualify for this ancillary judicial assistance: (1) just treatment of all claimants; (2) protection of U.S. claimholders against prejudice and inconvenience; (3) prevention of preferential or fraudulent transfers; (4) distribution of proceeds of the estate substantially in accordance with the U.S. Bankruptcy Code; (5) comity; and (6) if possible, the provision of the opportunity for a fresh start for the foreign debtor (in the case of an individual).²²⁷ It has been held that the bankruptcy court's ultimate determination is whether the relief sought will afford equality of distribution of available assets and an economical and expeditious administration.²²⁸

If the foreign representative satisfies the qualification criteria, the bankruptcy court may order any relief necessary to prevent the dismemberment of the assets of the foreign estate located within the United States. This relief includes transferring assets to the foreign representative for central administration and worldwide distribution.²²⁹

B. Commencement of the Section 304 Case

A foreign representative may commence an ancillary case under section 304 by filing a verified petition with the bankruptcy court.²³⁰ Subject to the exceptions below, the petition is to be filed in the dis-

²²⁷ 11 U.S.C. § 304(c)(1)-(6) (1982). All the factors listed in section 304(c) historically have been considered within the court's determination whether to afford comity to a proceeding in a foreign nation. *In re Culmer*, 25 Bankr. 621, 629 (Bankr. S.D.N.Y. 1982). Comity historically has been defined as

the recognition which one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citizens or of other persons who are under the protection of its laws.

Hilton v. Guyot, 159 U.S. 113, 164 (1895).

Comity is to be accorded a decision of a foreign court as long as that court is of competent jurisdiction, and as long as the laws and public policy of the foreign state are not violated. *Id.* at 202-03; *Clarkson Co. v. Shaheen*, 544 F.2d 624, 629 (2d Cir. 1976); *Cornfeld v. Investors Overseas Serv., Ltd.*, 471 F. Supp. 1255 (S.D.N.Y.), *aff'd*, 614 F.2d 1286 (2d Cir. 1979). For a discussion of the development of the doctrine of comity in international insolvency proceedings prior to the enactment of the Bankruptcy Code, see *Gallagher & Hartje, supra* note 225.

²²⁸ *Culmer*, 25 Bankr. at 628.. The Court cited *Israel-British Bank (London), Ltd. v. FDIC*, 536 F.2d 509, 513 (2d Cir.), *cert. denied*, 429 U.S. 978 (1976), to enunciate the principle that the theme of the Bankruptcy Code is equality of distribution of assets among creditors and avoidance of preferences. *Id.*

²²⁹ 11 U.S.C. § 304(b) (1982). The legislative history of § 304 articulates the flexibility available to a court in applying these factors to the specific circumstances in each case in order to arrive at a fair result. *See Culmer*, 25 Bankr. at 628.

²³⁰ 11 U.S.C. § 304(a) (1982). FED. BANKR. R. 1003(3) provides the procedure with respect to commencing a case under section 304, and provides:

(e) *Case Ancillary to Foreign Proceeding.*

(1) *Petition; Number of Copies.* An original and one copy of a petition commencing a case ancillary to a foreign proceeding shall be filed with the bankruptcy court.

(2) *Service of Petition and Summons.* On the filing of a petition pursuant to the preceding paragraph, the clerk shall forthwith issue a summons for service on all parties against whom relief is sought pursuant to § 304(b) of the

trict in which the principal U.S. assets of a foreign debtor are located.²³¹ If the foreign administrator is seeking to enjoin the commencement or continuation of litigation, or to enjoin the enforcement of a judgment, the petition must be filed in the bankruptcy court for the district in which the litigation is pending.²³² If the administrator is attempting to enjoin the enforcement of a lien against the U.S. property of the foreign debtor, the petition must be filed in the bankruptcy court for the district in which such property is located.²³³ The petition must specify the form of relief requested under section 304(b).²³⁴

Unlike other voluntary cases under the U.S. Bankruptcy Code, an order for relief is not granted automatically upon the filing of a petition under section 304.²³⁵ First, interested parties are allowed to challenge the petition on the grounds of the fraudulent nature of the foreign proceeding or appointment of the foreign representative, or the failure of the foreign proceeding to meet the criteria set forth in section 304(c).²³⁶ If the petition is not challenged, the bankruptcy court may enter its order for relief without a hearing.²³⁷

Because a section 304 ancillary proceeding does not constitute a full bankruptcy proceeding, the stay of section 362 does not apply automatically to restrain actions against the foreign debtor or its U.S. assets.²³⁸ If the foreign representative anticipates seizure of the foreign debtor's assets, he may apply for a temporary restraining order under section 304 or section 105 to maintain the status quo pending the outcome of the litigation.²³⁹

Code and on such other parties as the court may direct. FED. BANKR. R. 1010 applies to the manner of service of the summons and petition.

(3) *Responsive Pleadings and Motions*. FED. BANKR. R. 1011(a), (b), (c) and (e) applies to responsive pleadings and motions.

(4) *Contested Petition*. FED. BANKR. R. 1018 applies when a petition filed under this rule is contested.

Id.

²³¹ 28 U.S.C. § 1410(c) (1982).

²³² *Id.* § 1410(a).

²³³ *Id.* § 1410(b).

²³⁴ Section 304 authorizes the bankruptcy court to enter interim or permanent relief and specifically provides for injunctions against (a) actions against debtors with respect to property involved in the foreign proceeding; (b) suits against such property; (c) the enforcement of a judgment against such property; (d) the enforcement of a judgment against the debtor with respect to such property; and (e) a proceeding to create or enforce a lien against the assets of the estate. The court also may turn over the property of such estate to the foreign representative for foreign administration abroad and, where appropriate, provide for other equitable relief. 11 U.S.C. § 304 (1982).

²³⁵ *Cf.* 11 U.S.C. §§ 301, 302(a) (1982).

²³⁶ FED. BANKR. R. 1018 applies when a petition filed under section 304 is contested. For a discussion of the procedural aspects of section 304 litigation, see Given & Vilaplana, *Comity Revisited: Multinational Bankruptcy Cases under Section 304 of the Bankruptcy Code*, 1983 ARIZ. ST. L.J. 325, 329-37; Gallagher & Hartje, *supra* note 225, at 7-8.

²³⁷ 11 U.S.C. § 304(b) (1982).

²³⁸ See *supra* note 223 and accompanying text.

²³⁹ See 2 W. COLLIER, *supra* note 16, § 105.02; FED. BANKR. R. 7065.

It has always been contemplated that U.S. ancillary proceedings may be used by foreign representatives to avoid U.S. preferences and protect assets for foreign administration.²⁴⁰ Furthermore, it has been suggested that attachment by local creditors of the U.S. assets of a foreign debtor will not survive once a bankruptcy court has determined that the foreign proceeding has met the necessary statutory criteria for relief.²⁴¹

Upon determination that the foreign proceeding qualifies for U.S. recognition and assistance under section 304, the court may provide various forms of relief.²⁴² The court may enjoin the commencement, continuation, or enforcement of any U.S. action, judgment, or lien against a foreign debtor with respect to its U.S. assets.²⁴³ The court also may order the turnover of such U.S. assets to the foreign representative for distribution in the foreign proceeding.²⁴⁴ Instead of establishing inflexible rules, the legislative history of section 304 permits the bankruptcy court to make appropriate orders under the circumstances of each case.²⁴⁵ Finally, a foreign representative may petition the bankruptcy court to dismiss or suspend any existing U.S. bankruptcy proceeding against a foreign debtor if a foreign proceeding qualifies for ancillary relief under section 304.²⁴⁶

C. Court Decisions

Very few cases have interpreted section 304 since its enactment in 1978.²⁴⁷ The cases that have interpreted section 304 are inconsistent. Some bankruptcy courts have applied powers of equity to assist a qualifying foreign administration in ensuring the worldwide equal-

²⁴⁰ *Culmer*, 25 Bankr. at 633 (citing *Banque de Financement, S.A. v. First Nat'l Bank of Boston*, 568 F.2d 911 (2d Cir. 1977)).

²⁴¹ See Gallagher & Hartje, *supra* note 225, at 14 (citing *Banque de Financement*, 568 F.2d at 918-20, and *Israel-British Bank (London), Ltd.*, 536 F.2d at 511). These commentators further argue that if section 304 was to be meaningful or add anything to the prior practice, it must be necessary for attachments in place to be vacated in an ancillary proceeding. *Id.* Accord *Culmer*, 20 Bankr. at 633.

²⁴² 11 U.S.C. § 304(b), (c) (1982).

²⁴³ *Id.* § 304(b)(1).

²⁴⁴ *Id.* § 304(b)(2).

²⁴⁵ See *supra* note 223. Accord *Culmer*, 25 Bankr. at 627-28.

²⁴⁶ 11 U.S.C. § 305(a)(2) (1982).

²⁴⁷ See *In re Egeria Societa Per Azioni De Navigazione*, 26 Bankr. 494 (Bankr. E.D. Va. 1983), *rev'd on other grounds*, *Ciel v. Cia S.A. v. Nereide Societa De Navigazione*, 28 Bankr. 378 (E.D. Va. 1983); *Culmer*, 25 Bankr. at 621; *In re Toga Mfg. Ltd.*, 28 Bankr. 165 (Bankr. E.D. Mich. 1983); *Angulo v. Kedzep Ltd.*, 29 Bankr. 417 (S.D. Tex. 1983); *RBS Fabrics Ltd. v. G. Beckers & Le Hanne*, 24 Bankr. 198 (Bankr. S.D.N.Y. 1982); *In re Egeria Societa Per Azioni De Navigazione*, 20 Bankr. 625 (Bankr. E.D. Va. 1982); *In re Comstat Consulting Servs. Ltd.*, 10 Bankr. 134 (Bankr. S.D. Fla. 1981); *In re Stuppel*, 17 Bankr. 413 (S.D. Fla. 1981); *In re Lineas Aereas de Nicaragua S.A.*, 10 Bankr. 790 (Bankr. S.D. Fla. 1981); *In re Lineas Aereas de Nicaragua S.A.*, 13 Bankr. 779 (Bankr. S.D. Fla. 1981). For an in-depth discussion of the foregoing cases and an analysis of section 304, see Gallagher & Hartje, *supra* note 225; Given & Vilaplana, *supra* note 236, at 329-37.

ity of creditor treatment in an efficient and economical manner.²⁴⁸ Other courts have insisted on a U.S. ancillary administration under the substantive and procedural laws of the U.S. Bankruptcy Code.²⁴⁹

The two most significant decisions to date, *In re Culmer*²⁵⁰ and *In re Toga Manufacturing Ltd.*,²⁵¹ determined the question whether to grant the relief requested in the section 304 petition. Other cases decided to date have ruled only on requests for preliminary relief.²⁵²

Culmer represents as pure an application of section 304 as its drafters could have intended. The case arose from the voluntary liquidation of Banco Ambrosiano Overseas Limited (BAOL) in the Bahamas. Its Italian parent, Banco Ambrosiano SPA, was unable to support its Bahamian banking subsidiary, and certain creditors attempted to attach the U.S. assets of BAOL. BAOL filed a section 304 petition and pending its hearing, the court temporarily restrained the continuation of previously commenced actions against BAOL, the commencement of any further action by any other BAOL depositors or creditors, and the creation, perfection, or enforcement of any lien, set-off, or any other claim against the property of BAOL.²⁵³

After a review of section 304 and its legislative history, the court concluded that it must determine whether the relief sought would afford equality of distribution of the available assets.²⁵⁴ The court analyzed Bahamian liquidation law and found it to be similar to the U.S. Bankruptcy Code in providing for a comprehensive procedure for the orderly and equitable distribution of assets among all creditors.²⁵⁵ Other factors that the court found relevant were that the Bahamas had the greatest interest in BAOL's liquidation, and that the two largest creditors of the estate supported the Bahamian proceeding. The court also noted that preclusion of relief would provide some creditors with preferences to which they were not entitled under a Bahamian liquidation. On the other hand, the court found that granting the requested relief would not prejudice or inconvenience creditors in processing claims, because the Bahamian proceeding substantially was in accord with the order and priority in the U.S. Bankruptcy Code.²⁵⁶

Combining these considerations with traditional notions of com-

²⁴⁸ See, e.g., *Culmer*, 25 Bankr. at 621.

²⁴⁹ See, e.g., *Comstat Consulting Services*, 10 Bankr. at 134; *Lineas Aereas de Nicaragua*, 10 Bankr. at 790; *Egeria Societa Per Azioni De Navigazione*, 20 Bankr. at 625.

²⁵⁰ *Culmer*, 25 Bankr. at 621.

²⁵¹ *Toga Mfg.*, 28 Bankr. at 165.

²⁵² See *Comstat Consulting Services*, 10 Bankr. at 134; *Stuppel*, 17 Bankr. at 413; *Lineas Aereas de Nicaragua*, 10 Bankr. at 790; *RBS Fabrics*, 24 Bankr. at 198; *Egeria Societa Per Azioni De Navigazione*, 20 Bankr. at 625; *Angulo*, 29 Bankr. at 417.

²⁵³ *Culmer*, 25 Bankr. at 623.

²⁵⁴ *Id.* at 628.

²⁵⁵ *Id.*

²⁵⁶ *Id.* at 628-29.

ity,²⁵⁷ the court permanently enjoined all persons from commencing or continuing attempts to obtain, create, or enforce any set-off or lien against any of BAOL's assets located within the United States. The court also ordered the turnover of all funds and assets of BAOL located in the United States to the foreign administrators for administration in the foreign proceeding, and directed U.S. claimants to the Bahamian liquidation for resolution of substantive issues.²⁵⁸

In contrast, the court in *Toga* denied relief, dismissing an ancillary case.²⁵⁹ Essentially, the court held that although the U.S. Bankruptcy Code and Canadian bankruptcy laws provide for equality of distribution among creditors, the Canadian proceeding could not qualify for ancillary assistance under section 304(c). Although Canada was not an inconvenient forum, Canadian law was found to accord a lesser priority to the objecting U.S. creditor.²⁶⁰ In addition, comity was lacking because of the unavailability of a treaty between the United States and Canada providing for the mutual recognition of each country's bankruptcy laws.²⁶¹

Toga has been criticized severely for restricting section 304 to only those countries that either adopt U.S. bankruptcy law principles or conclude treaties with the United States.²⁶² A requirement for reciprocity in the application of section 304, however, could serve well as an incentive for major trading partners to implement legislation authorizing ancillary relief for foreign debtors in their own countries.

V. Proposal for Reciprocity

Because true international bankruptcy proceedings are rare, there is no immediate need to achieve the goal of full international bankruptcy compatibility in one ratification. Indeed, commentators have suggested that insights into the requirements for the development of a true international bankruptcy system currently are lacking.²⁶³ Yet, because of increased integration of the global economy and the corresponding increase in international economic interdependence, a policy for the treatment of international insolvency proceedings must be developed.

Although an awareness of the need for international agreement on bankruptcy proceedings has existed for centuries,²⁶⁴ recent inter-

²⁵⁷ *Id.* at 629.

²⁵⁸ *Id.* at 634.

²⁵⁹ *Toga Mfg.*, 28 Bankr. at 170.

²⁶⁰ *Id.*

²⁶¹ *Id.*

²⁶² See Gallagher & Hartje, *supra* note 225, at 21; Comment, *Section 304 of the Bankruptcy Code: Has It Fostered the Development of an "International Bankruptcy System?"*, 22 COLUM. J. TRANSNAT'L L. 541, 566 (1984).

²⁶³ I. J. DALHUISEN, *supra* note 6, § 2.05[7], at 3-440.

²⁶⁴ Efforts to enact treaties or otherwise reach agreements between nations to resolve

national economic development has resulted in the formulation of two major proposals that currently are receiving widespread recognition as precursors of more general multinational agreements to resolve conflicts in international bankruptcy proceedings. The Draft United States-Canada Bankruptcy Treaty (Draft Treaty)²⁶⁵ is a bilateral proposal, while the European Economic Community (EEC) Bankruptcy Convention (Draft Convention)²⁶⁶ is regional in scope.

The Draft Treaty is still in preliminary form and subject to ratification by the Parliament of Canada and the U.S. Senate. This treaty provides for the single administration of the estate of a debtor,²⁶⁷ conferring jurisdiction on the contracting state within whose territory the greater portion in value of the debtor's property is located.²⁶⁸ The laws of the state having jurisdiction, including conflict of laws rules, are to apply, and the trustee or debtor in possession will have all attendant powers in both states.²⁶⁹ Orders of courts having jurisdiction are to be recognized and enforced in courts of the nonadjudicating state.²⁷⁰

No new substantive law of bankruptcy is proposed in the Draft Treaty; rather, rules are set forth regulating the choice of law in international bankruptcy proceedings.²⁷¹ The Draft Treaty has been criticized for not recognizing the differences in the substantive bankruptcy law of the United States and Canada and failing to acknowledge that in certain instances, the law of the nonadjudicating state

conflicts in international bankruptcy have a long and largely unsuccessful history, dating back to agreements on bankruptcy entered into between Medieval Italian city-states in the Thirteenth Century. Nadelmann, *Bankruptcy Treaties*, 93 U. PA. L. REV. 58, 59 (1944).

In addition to numerous efforts at bilateral treaties, the Fifth Conference on Private International Law held at the Hague in 1925 adopted a model treaty on bankruptcy which has had considerable influence on subsequent efforts, although it was never submitted for multilateral adoption. The 1925 model treaty is reprinted in English translation. *Id.* at 94-97. Regional agreements on bankruptcy have been adopted in Latin America, including certain provisions in the Montevideo Treaty on International Commercial Law, first adopted in 1889, and the Bustamante Code of Private International Law, adopted at Havana in 1928. *See generally id.* at 68-71; Nadelmann, *supra* note 31, at 150-53.

²⁶⁵ Draft of United States of America-Canada Bankruptcy Treaty, Oct. 29, 1979 [hereinafter cited as the Draft Treaty], reprinted in 2 J. DALHUISEN, *supra* note 6, app. D-6A, at D-6A-1 to D-6A-13. *See generally Explanatory Notes on the Draft Treaty*, 2 J. DALHUISEN, *supra* note 6, app. D-6A, at D-6A-18 to D-6A-24; 2 L. HOULDEN & C. MORAWETZ, *supra* note 46, at 70; Nadelmann, *A Reflection on Bankruptcy Jurisdiction: News from the European Common Market, the United States and Canada*, 27 REVUE DE DROIT DE MCGILL 541, 550-55 (1982).

²⁶⁶ Preliminary Draft of A Convention on Bankruptcy, Winding-Up, Arrangements, Compositions and Similar Proceedings, June 1979, Commission of the European Communities [hereinafter cited as Draft Convention], reprinted in 2 J. DALHUISEN, *supra* note 6, app. C-1A2, at C-1A2-1 to C-1A2-60. *See generally* 1 J. DALHUISEN, *supra* note 6, § 2.05[7], at 3-428 to 3-439; C. LIVADAS, *supra* note 74, at 12-14.

²⁶⁷ Draft Treaty, *supra* note 265, at art. 3, reprinted in 2 J. DALHUISEN, *supra* note 6, at app. D-6A-4.

²⁶⁸ *Id.* at art. 6, reprinted in 2 J. DALHUISEN, *supra* note 6, at app. D-6A-5 to D-6A-6.

²⁶⁹ *Id.* at art. 15, reprinted in 2 J. DALHUISEN, *supra* note 6, at app. D-6A-10.

²⁷⁰ *Id.* at art. 16, reprinted in 2 J. DALHUISEN, *supra* note 6, at app. D-6A-10.

²⁷¹ 2 L. HOULDEN & C. MORAWETZ, *supra* note 46, at 70-71.

should govern.²⁷² Creditors may be uncertain as to which substantive bankruptcy law would apply at a future date with regard to a debtor having assets in both the United States and Canada.²⁷³

The other major extant proposal is the Draft Convention²⁷⁴ which has been proposed for members of the EEC. The proposal anticipates an increase in bankruptcies, reorganizations, and related proceedings involving businesses with establishments or activities in two or more of the EEC jurisdictions.²⁷⁵ The Draft Convention provides for unity of the bankruptcy proceeding and grants jurisdiction to the courts of the state where the center of administration of the debtor is located.²⁷⁶

The substantive law of the adjudicating state determines the requirements for commencing a bankruptcy proceeding and the procedure to be followed.²⁷⁷ Preferences and the rights of secured creditors, however, are governed by the substantive law of the jurisdiction where the assets were located at the time of the commencement of the bankruptcy proceeding.²⁷⁸

Criticisms of the Draft Convention have included: (1) lack of flexibility in conflict of laws rules; (2) inadequate treatment of preventive proceedings such as reorganizations; (3) insufficient protec-

²⁷² Nadelmann, *supra* note 265, at 551. The author also critiques the "location of the greater portion of the assets" test as a basis for jurisdiction. In addition, he critiques such provisions as the determination of location of intangible property, Draft Treaty, *supra* note 265, at art. 8, and the limitation on applicability of the Draft Treaty to those debtors whose "principal property," as defined therein, is in either the United States or Canada or both. *See generally id.* at 550-51.

²⁷³ *See id.* at 551.

²⁷⁴ The first draft of the Draft Convention was made in 1968, followed by new texts in 1970 and 1979, with work still proceeding on the project. For text of the 1970 draft, see 2 J. DALHUISEN, *supra* note 6, at apps. C-1A-1 to C-1A-51.

²⁷⁵ The theoretical basis for the anticipation of an increase in international bankruptcies in the EEC is the increasing movement of goods and services between the EEC jurisdictions as a result of the economic integration of EEC states. It has been observed that such an increase in international bankruptcies has yet to become evident. *See* 1 J. DALHUISEN, *supra* note 6, § 2.05[7], at 3-428.

²⁷⁶ Draft Convention, *supra* note 266, at art. 3(1), *reprinted in* 2 J. DALHUISEN, *supra* note 6, at app. C-1A-3. The center of administration is defined as "the place where the debtor usually administers his main interests," and is presumed in the case of companies to be the registered office. *Id.* at arts. 3(2)-(3), *reprinted in* 2 J. DALHUISEN, *supra* note 6, at app. D-6A-4.

If no center of administration exists in the EEC, jurisdiction may be asserted by the courts of any EEC state where the debtor has an establishment or "place where an activity of the debtor comprising a series of transactions is carried on by him or on his behalf." *Id.* at art. 4(1)-(2), *reprinted in* 2 J. DALHUISEN, *supra* note 6, at app. D-6A-5. The definitions of "centre of administration" and "establishment" may be sufficiently broad to result in concurrent jurisdictions. *See* 1 J. DALHUISEN, *supra* note 6, § 2.05[7], at 3-432, 3-430 to 3-431 n.125.

²⁷⁷ Draft Convention, *supra* note 266, at arts. 17-18, *reprinted in* 2 J. DALHUISEN, *supra* note 6, at apps. C-1A-7 to C-1A-8.

²⁷⁸ *Id.* at arts. 45-46, *reprinted in* 2 J. DALHUISEN, *supra* note 6, at app. C-1A-19. The law of the jurisdiction where the assets are situated also is determinative as to excluded property. *Id.* at art. 34(3), *reprinted in* 2 J. DALHUISEN, *supra* note 6, at app. C-1A-13.

tion of third party interests; (4) lack of accounting provisions for concurrent proceedings;²⁷⁹ and (5) failure to deal adequately with assets of the debtor located outside the EEC.²⁸⁰

Neither the Draft Treaty nor the Draft Convention is in final form, and further negotiations and refinements are anticipated. It is clear already from the criticisms of both proposals, however, that formulating an effective bilateral or regional accord on international bankruptcy in the near future will be difficult.

Therefore, it appears that if a system of rules of international bankruptcy recognition is to be developed, it must be done through the cooperation of the adjudicating bankruptcy court and the recognizing bankruptcy court in international proceedings. The recognizing foreign court, guided by the *forum non conveniens* approach, would concede jurisdiction to the adjudicating bankruptcy court having better contacts with the case. The adjudicating bankruptcy court, while being guided by principles of *lex fori*, should make necessary adjustments that take into account the concerns of the foreign recognizing forum to obtain the cooperation of the foreign court.²⁸¹

This procedure has been implemented in the United States under section 304 of the U.S. Bankruptcy Code,²⁸² which allows foreign administrators to commence a case ancillary to a foreign insolvency proceeding. As evidenced by the survey of foreign bankruptcy laws, the major trading partners of the United States are not willing at this time to reciprocate.

The successful implementation of section 304 by U.S. bankruptcy courts should encourage the major trading partners of the United States to provide for similar ancillary relief under their bankruptcy laws. If foreign jurisdictions do not follow the lead of the United States, it may be necessary for U.S. bankruptcy courts, in implementing section 304, to follow the approach in *Toga*²⁸³ to elicit the cooperation necessary to protect the foreign assets of the U.S. Debtor. As a prerequisite to applying comity under section 304(c), the courts could insist on a showing that reciprocity is available to the U.S. Debtor with assets located in the foreign jurisdiction of the foreign representative seeking ancillary relief under section 304.²⁸⁴

²⁷⁹ See generally 1 J. DALHUISEN, *supra* note 6, § 2.05[7], at 3-430 n.125.

²⁸⁰ Nadelmann, *supra* note 265, at 544 n.14. See also Nadelmann, *The Common Market Bankruptcy Convention Draft: Foreign Assets and Related Problems*, in CONFLICT OF LAWS: INTERNATIONAL AND INTERSTATE SELECTED ESSAYS 340 (1972). In addition to the criticisms cited herein, other difficulties plague the Draft Convention, including for instance, the problem of integrating Great Britain and its three jurisdictions into the Draft Convention regime, particularly with regard to the concept of single administration. Nadelmann, *supra* note 31, at 148.

²⁸¹ See generally *supra* note 14 and accompanying text.

²⁸² See generally *supra* and text accompanying notes 220-62.

²⁸³ *Toga Mfg.*, 28 Bankr. at 165. See *supra* notes 259-62 and accompanying text.

²⁸⁴ Because of the extraordinary circumstances surrounding an ancillary proceeding

Alternatively, a legislative basis for such a requirement could be provided by amending section 304 to add reciprocity as a requisite factor to be considered in granting relief under section 304.²⁸⁵

Once foreign courts involved in international insolvency proceedings realize that the United States requires reciprocal treatment before authorizing relief under section 304, enactment of similar laws providing for ancillary proceedings in such foreign jurisdictions may follow.²⁸⁶ The ultimate result would be a network by which assets of the debtor could be preserved and distributed equally among creditors in a centrally administered bankruptcy proceeding.²⁸⁷ At that time, it will be proper to assess whether the availability of the ancillary proceeding in the U.S. and foreign jurisdictions is sufficient, or whether it would be desirable to propose the adoption of bilateral or multilateral treaties on bankruptcy among major trading partners. Perhaps by that time, the Draft Treaty will be polished sufficiently to provide a model for new treaty proposals.

The existence of the section 304 proceeding under the U.S. Bankruptcy Code provides the United States with a vehicle for stimulating the development of reciprocity in international bankruptcy proceedings. Thus, the work to develop a system of rules of international bankruptcy recognition must begin with U.S. bankruptcy courts in their implementation of section 304.

VI. Conclusion

The present formulation of international bankruptcy law is in-

under section 304, the relief provided, and the availability to the foreign debtor of a full United States bankruptcy case under sections 301 and 303(b)(4) to administer the U.S. assets of the foreign estate, the authors do not believe that such a requirement of reciprocity would offend traditional notions of fair play and substantial justice, emasculate section 304, or overturn legal precedent.

Without such action the logjam that haunts the development of rules of international bankruptcy law will never be broken. The burden of proof as to the availability of satisfactory reciprocal relief should be placed on the foreign representative. For a heated criticism of this concept, see Gallagher & Hartje, *supra* note 225, at 21; Comment, *supra* note 265, at 556 (stating that "[r]eciprocity type legislation, while encouraging the use of similar procedures, may exacerbate existing differences and lead to increased tensions and political stalemates rather than increased international cooperation"). Comment, *supra* note 262, at 556.

²⁸⁵ This concept has significant support. See *Bankruptcy Act Revision: Hearings on H.R. 31 and H.R. 32 Before the Subcomm. on Civil and Constitutional Rights of the House Comm. on the Judiciary*, 94th Cong., 2d Sess. 1516 (1976) (statement of Prof. Stefan A. Reisenfeld). See also *id.* at 1445 (statement of Prof. Kurt H. Nadelmann, supporting a provision which gave the executive branch the power to demand reciprocity); Nadelmann, *supra* note 2, at 34.

²⁸⁶ This expectation is not without merit. Canada's bankruptcy law now contains provisions for relief in cases ancillary to foreign proceedings that are similar to section 304. See *supra* notes 61-64 and accompanying text. See also Honsberger, *supra* note 14, at 671-74.

²⁸⁷ At the present time, it appears that should similar statutes be enacted in the jurisdiction of the major trading partners of the United States surveyed in this article, the U.S. Debtor would, in most cases, qualify for ancillary relief.

consistent and incomplete. More effort must be dedicated to the task of increasing the effectiveness of international insolvency laws before international bankruptcy proceedings become commonplace. The current techniques for protecting the foreign assets of the U.S. Debtor, for the most part, are ineffective and expensive. The United States, however, has provided a model by which an action ancillary to a foreign bankruptcy proceeding can be instituted to protect the assets of a foreign debtor from dismemberment and to effectuate the principle of equality of distribution of assets among creditors in the most efficient manner.

The major trading partners of the United States, as well as other foreign jurisdictions, are encouraged to follow this U.S. model and adopt similar legislation. A demand for reciprocity by U.S. bankruptcy courts in section 304 proceedings may be necessary to provide the catalyst to initiate legislation instituting ancillary bankruptcy procedures in foreign jurisdictions.

If the major trading partners of the United States adopt such legislation, the first step toward the establishment of international rules regarding bankruptcy proceedings will have been accomplished. It will then be necessary to examine whether these ancillary proceedings are sufficient to accomplish the goals in international bankruptcy proceedings of protection of estates from dismemberment and efficient, equitable distribution of assets among all creditors, or whether international treaties regarding bankruptcy will have to be adopted.

