

# CROSS-BORDER INSOLVENCY LAW IN THE UNITED STATES AND ITS APPLICATION TO MULTINATIONAL CORPORATE GROUPS

*Lesley Salafia\**

## INTRODUCTION

Ever since corporations began expanding across national borders, countries throughout the world have struggled with the question of how to manage cross-border insolvency, or, in other words, an insolvent debtor with assets and liabilities in more than one country. On the one hand, the need to manage the debtor's assets under one coherent bankruptcy plan to benefit the creditors and maximize the value of the estate. On the other hand, no nation wishes to give up control over assets within its own borders to the jurisdiction of a foreign court. This issue becomes more difficult when a debtor is not merely liquidating a bankrupt estate but rather applies for a reorganization of its debts and liabilities. In today's global economy, multinational corporate groups with numerous subsidiaries are faced with the prospect of addressing insolvency issues under multiple, and sometimes conflicting, foreign jurisdictions.

The United States became the first nation in the world to codify a policy that foregoes a bit of its own sovereign jurisdiction to the order of a foreign court concerning the U.S. assets of a foreign debtor's bankrupt estate.<sup>1</sup> In the Bankruptcy Reform Act of 1978, the U.S. Congress passed section 304, recognizing cases in bankruptcy courts ancillary to foreign proceedings.<sup>2</sup> Under this statute, if a U.S. bankruptcy judge felt a foreign bankruptcy proceeding met certain procedural requirements, just treatment and comity, she could grant ancillary jurisdiction to the foreign proceeding and allow the debtor's U.S. assets to be controlled and distributed under the order of the foreign bankruptcy proceeding.<sup>3</sup>

Section 304 was the first attempt at achieving universalism, or international coherence, to cross-border bankruptcy proceedings. Like all first attempts, however, it also produced a multitude of litigation in the interpretation and application of the statute. Although ancillary proceedings under section 304

---

\* J.D. Candidate, University of Connecticut School of Law, 2006; B.A., Tulane University, 2003. I would like to thank Professor Blumberg for his encouragement and guidance with this work. I would also like to extend my gratitude to my husband and parents for their relentless support. Finally, to the members of the *Connecticut Journal of International Law* for their constant editing, advice, and friendship.

1. Jay Lawrence Westbrook, *Theory and Pragmatism in Global Insolvencies: Choice of Law and Choice of Forum*, 65 AM. BANKR. L.J. 457, 471 (1991).

2. Bankruptcy Reform Act of 1978, §304, 11 U.S.C. §304 (2005) (repealed 2005).

3. *Id.*

became more accepted,<sup>4</sup> the results of petitions for ancillary jurisdiction also became more random and unpredictable. Success varied not merely due to the status of the parties arguing for and against the petition, but also due to the judge's discretion.<sup>5</sup>

Two essential problems arose in section 304 litigation. The first problem involved the six statutory criteria used by courts to determine whether or not deference to the foreign proceedings was appropriate for the facts at hand.<sup>6</sup> Because of the wide discretion afforded to judges and the lack of concrete rules, cases varied widely as to the application of the six criteria and the substantive law that would be considered by the courts. The sole guiding principle emerging from the case law was that a foreign proceeding, that did not place a secured creditor in a position equal to the position that would be afforded under U.S. bankruptcy law, would not be granted ancillary relief.

The second problem centered around the question of which types of proceedings involving a debtor in foreign courts constituted "foreign proceedings" under section 304.<sup>7</sup> Even within the singular jurisdiction of the Southern District of New York, an uncertainty was forming as to whether voluntary reorganization proceedings that did not involve insolvency would constitute "foreign proceedings" under section 304.<sup>8</sup>

In April of 2005 Congress passed the Bankruptcy Reform Act of 2005, also known as the Abuse Prevention and Consumer Protection Act of 2005.<sup>9</sup> It went into effect 180 days later, on October 18, 2005. In the process of adopting the new bankruptcy code, Congress repealed Section 304. The new bankruptcy act codified the Model Law on Cross-Border Insolvency into United States Code sections 1501 through 1532.<sup>10</sup> This, in effect, is the new "Chapter 15." Chapter 15 takes many steps to amend those questions and codify case law that has evolved from section 304. The extent to which it resolves the problems of the former section 304 will have to be determined by future scholars.

This paper will discuss whether Chapter 15 of the new Bankruptcy Reform Act of 2005 addresses the problems that arose under section 304 in the quest to bring universalism to foreign bankruptcy proceedings involving assets located in the United States. It will consider Chapter 15 in light of the reality that multinational corporate groups impact bankruptcy proceedings involving parent and subsidiary

---

4. As far back as 1984, scholars were noting, "During the past decade, U.S. case law has increasingly reflected a growing movement away from decisions based on an overt nationalistic bias favoring American creditors. The new trend favors recognizing foreign proceedings and judgments in international insolvencies, as well as the rights of foreign debtors under U.S. law." Stacy Allen Morales & Barbara Ann Deutsch, *Bankruptcy Code Section 304 and U.S. Recognition of Foreign Bankruptcies: The Tyranny of Comity*, 39 BUS. LAW. 1573, 1579 (1984).

5. Todd Kraft & Allison Aranson, *Transnational Bankruptcies; Section 304 and Beyond*, 1993 COLUM. BUS. L. REV. 329, 339 (1993).

6. *Id.* at 340.

7. *In re Bd. of Dirs. of Hopewell Int'l Ins. Ltd.*, 275 B.R. 699, 706-07 (S.D.N.Y. 2002); *In re Rose*, 318 B.R. 771, 774-76 (Bankr. S.D.N.Y. 2004).

8. *Id.*

9. Pub. L. No. 109-8 (2005).

10. Abuse Prevention and Consumer Protection Act of 2005, 11 U.S.C. §§1501-1532 (2005).

corporations in ways not previously found in traditional bankruptcy law. Multinational corporate groups cause a solution to cross-border insolvency even more complex to attain.

Part I of this paper will briefly discuss the concept of universalism as applied to cross-border insolvencies. As part of this discussion, the paper will give an overview into the concept of comity established by the United States Supreme Court. Part I will then discuss early attempts by U.S. courts to grant comity to foreign bankruptcy proceedings.

Part II of this paper will discuss section 304 and the specific problems that arose under it. The first problem involved the application of the statutory criteria considered by a court when adjudicating a petition for ancillary jurisdiction. The second problem arose with the question of which types of proceedings in a foreign court amounted to “foreign proceedings” applicable for relief under section 304 the U.S. Bankruptcy Code.

Part III will look in depth into the new Chapter 15. It will discuss in particular how the new sections of Chapter 15 clarify recognition of foreign proceedings and attempt to make distinctions between main and non-main foreign proceedings. It will also discuss the wide and varied steps that Chapter 15 takes to guarantee coordination and cooperation between U.S. and foreign bankruptcy proceedings, both in cases in which the U.S. bankruptcy courts handle a plenary proceeding along with another jurisdiction and those cases in which the United States is asked to grant ancillary jurisdiction to foreign proceedings. Finally, Part III will discuss ways that Chapter 15 has amended some of the problem litigation that arose under Section 304.

Part IV will apply what has been learned from section 304 and Chapter 15 to the problem of insolvent multi-tiered corporations. After providing an overview of the debate between entity versus enterprise corporate structures, this Part will discuss substantive consolidation and the solutions suggested by the American Law Institute. It will then look into the path taken by judges when faced with the complex problems of insolvent multinational corporations prior to Chapter 15 and the possible guidance that the new Chapter 15 may give in the future to navigating these complex issues. In conclusion, it will consider possible other paths that commentators have suggested to guide the insolvency proceedings of multinational corporations.

## I. UNIVERSALISM IN U.S. BANKRUPTCY PROCEEDINGS

### *A. The Universalism versus Territorialism Debate*

Traditionally when it came to the bankruptcy proceedings of a debtor with assets in multiple countries, each state had jurisdiction over the debtor’s assets within its own borders. Under this “territorial system,” each nation was left to distribute the debtor’s assets in its jurisdiction as it saw fit. Each nation in turn

distributed assets mostly to the local creditors.<sup>11</sup> This process is also known as the “grab rule” for the competing efforts of creditors to appear before local jurisdictions to seize assets and initiate insolvency proceedings as quickly as possible.<sup>12</sup>

Rather than leave creditors to the “grab rule” and insolvent multinational corporations completely unable to receive the benefits of reorganization, practitioners and commentators began to envision a system of coordinated cross-border bankruptcy. In this system, all assets of the debtor, regardless of location or jurisdiction, would be administered under one bankruptcy plan.<sup>13</sup> This idea became known as universalism.

The universalism system would achieve fairness and equity among the competing claimholders. Because all of the debtor’s property would be subject to a single adjudication, irrespective of the property’s location, creditors have a chance of uniform distribution.<sup>14</sup>

But what does it mean to bring universalism to international bankruptcy?<sup>15</sup> “Universality is considered by many as the ideal of international insolvency proceedings. To achieve complete universality, however, would require the unification of the substantive and procedural insolvency laws and other economic legislation of all the world’s countries. This is no more realistic than attempting to unify the world’s currencies.”<sup>16</sup> Another flaw of universalism exists because different nations have different perceptions of fairness concerning the rights of creditors to the distribution of assets.<sup>17</sup> Complete universalism in both procedural and substantive bankruptcy law would necessitate the substitution of one nation’s values for those of another. Finally, coordination of an international bankruptcy code would force individual nations to forego their individual sovereignty with regard to bankruptcy.

Recently, a third approach to the handling of international insolvencies has come into discussion. This approach, known as contractualism, allows a corporation to “specify in its charter the jurisdiction that will administer its bankruptcy.”<sup>18</sup> Commentators argue that this approach is merely an extension of the current contractual abilities of creditors to secure their claims with a security

---

11. Kraft & Aranson, *supra* note 5, at 337. See also Harold S. Burman, *International Insolvencies: Colloquium: Harmonization of International Bankruptcy Law: A United States Perspective*, 64 *FORDHAM L. REV.* 2543, 2551 (1996).

12. Westbrook, *supra* note 1, at 460.

13. Kraft & Aranson, *supra* note 5, at 336.

14. *Id.*

15. See Thomas M. Gaa, *Harmonization of International Bankruptcy Law and Practice: Is it Necessary? Is it Possible?*, 27 *INT'L LAW.* 881 (1993) (questioning whether “harmonization” of international bankruptcy means coordinating the various state bankruptcy laws, forming bankruptcy treaties between nations that allocate jurisdiction, or forming an international bankruptcy court that overrules the sovereign state’s bankruptcy laws).

16. Shoichi Tagashira, *Intraterritorial Effects of Foreign Insolvency Proceedings: an Analysis of “Ancillary” Proceedings in the United States and Japan*, 29 *TEX. INT'L L.J.* 1, 37 (1994).

17. Westbrook, *supra* note 1, at 466.

18. *In re Treco*, 240 F.3d 148, 154 n.2 (2d Cir. 2001).

interest or a pledge of lender priority.<sup>19</sup> They further posit that this approach would give the greatest benefit to multinational corporations, as some corporations would benefit from a single, unified international insolvency proceeding, while others might prefer to have insolvency issues of their corporate subsidiaries administered by the separate individual jurisdictions of incorporation.<sup>20</sup> Contractualism has yet to be tested in practice.

*B. The Concept of Comity in the United States*

The seminal United States Supreme Court case discussing the concept of comity and its application is *Hilton v. Guyot*.<sup>21</sup> A French glove manufacturer received a judgment in France against an American merchant with stores in both New York and Paris. When the merchant conveniently closed up shop in Paris before paying the ordered sum, the French manufacturer petitioned a U.S. court for a judgment. A full jury trial was held in the Southern District of New York with a directed verdict against the American merchant for a sum equivalent to the amount ordered by the French court plus interest.<sup>22</sup> Appeal was then taken. The decision produced by the United States Supreme Court contained the standard definition of comity that has since been used by all U.S. courts:

‘Comity,’ in the legal sense, is neither a matter of absolute obligation, on the one hand, nor of mere courtesy and good will, upon the other. But it is the recognition which one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citizens, or of other persons who are under the protection of its laws.<sup>23</sup>

After a lengthy discussion of writings from prior scholars and English, American colonial and state case law, the *Hilton* Court first concluded that when the proceedings essentially have been fair, the defendant should not be allowed to contest the validity of the judgment.<sup>24</sup> The court then questioned whether France would grant reciprocity to decisions rendered by U.S. courts. After analyzing the laws of many foreign nations, the Court concluded, “It appears, therefore, that there is hardly a civilized nation on either continent which, by its general law, allows conclusive effect to an executory foreign judgment for the recovery of money.”<sup>25</sup> Therefore, because French courts would not grant full comity to a U.S. decision

---

19. Robert K. Rasmussen, *Resolving Transnational Insolvencies Through Private Ordering*, 98 MICH L. REV. 2252, 2258 (2000). Rasmussen admits contractualism might result in the creation of debtor havens. *Id.* at 2264. However, he does not feel that this should outweigh the benefits of contractualism and suggests ways around the negative aspects of debtor havens. *Id.* at 2264 -73.

20. *Id.* at 2260.

21. 159 U.S. 113, 114 (1895).

22. *Id.* at 120, 122.

23. *Id.* at 163-64.

24. *Id.* at 202-03.

25. *Id.* at 227.

without review, the decision of the French court in this case should serve only as prima facie evidence in the U.S. trial.<sup>26</sup> In the absence of a statute or treaty giving full comity to the decisions of other nations, "The judgment is not entitled to be considered conclusive."<sup>27</sup>

The *Hilton* decision, while acknowledging the validity of the judgment by the French judiciary, ultimately found that the wiser course would be to protect U.S. citizens by reviewing in full the judgment of the foreign court because the foreign court would do the same in a like situation. A decade after *Hilton*, the U.S. Supreme Court characterized the decision as one that advocated a case-by-case approach to complaints brought by foreign creditors and cemented the notion that international comity does not require "prejudice" to local creditors and superior claims against property located in the United States.<sup>28</sup> Thus, later questions of comity were left to the courts with guidance that, while comity might be a wise concept, the effects of comity upon a U.S. citizen must be taken into consideration. *Hilton v. Guyot* has been used to fuel both the notion that U.S. courts should respect the judgments of foreign courts and the notion that U.S. courts should not defer to the judgments of foreign courts if those foreign courts would not defer equally to U.S. proceedings.

For example, in *In re Toga Manufacturing Limited*,<sup>29</sup> a case in which a U.S. creditor sought to prevent ancillary jurisdiction to a Canadian bankruptcy proceeding, the bankruptcy court cited two Canadian cases, both from the late nineteenth and early twentieth century, in which the Canadian court refused to grant comity to U.S. bankruptcy proceedings.<sup>30</sup> Before discussing these Canadian cases and the concept of comity under *Hilton*, the court had already found that the U.S. creditor would not be treated as a secured creditor in violation of the criteria necessary for a grant of ancillary relief.<sup>31</sup> The court went on to discuss the

---

26. *Id.*

27. *Id.* at 228. The case was remanded in order to hold a new, full trial. *Id.* at 229. The dissent, written by Chief Justice Fuller and joined by Justices Harlan, Brewer and Jackson, would under the principles of res judicata grant full effect to the French decision absent a treaty or Congressional ruling. *Id.* "In any aspect, it is difficult to see why rights acquired under foreign judgments do not belong to the category of private rights acquired under foreign laws." *Id.* at 233.

28. *Disconto Gesellschaft v. Umbreit*, 208 U.S. 570, 579 (1908).

In the elaborate examination of the subject in that case many cases are cited and the writings of leading authors on the subject extensively quoted as to the nature, obligation, and extent of comity between nations and states. The result of the discussion shows that how far foreign creditors will be protected and their rights enforced depends upon the circumstances of each case, and that all civilized nations have recognized and enforced the doctrine that international comity does not require the enforcement of judgments in such wise as to prejudice the rights of local creditors and the superior claims of such creditors to assert and enforce demands against property within the local jurisdiction.

*Id.* The U.S. Supreme Court in *Disconto* affirmed a Wisconsin state court's decision to place the claims of local creditors above those of foreign creditors, citing that foreign nations and other states would do the same. *Id.* at 580.

29. 28 B.R. 165 (Bankr. E.D. Mich. 1983).

30. *Id.* at 170. The cases cited were *Macdonald v. Georgian Bay Lumber Co.*, 2 S.C.R. 364 (Can. Sup. Ct. 1878) and *Williams v. Rice & Rice Knitting Mills Ltd.*, [1926] 3 D.L.R. 225 (Can. 1926).

31. *Id.* at 169. The court found that distribution of the bankrupt's estate under Canadian law would be in violation of 11.U.S.C. §304(c)(4), distribution of proceeds of such estate substantially in

criterion of comity and found that *Hilton*, the Canadian cases and *Clarkson Co., Ltd. v. Shaheen*,<sup>32</sup> a case that granted comity on the specifications that the U.S. creditors would not be subject to injustice or prejudice, all called for a denial of ancillary relief because the creditors would not be treated equally under U.S. and Canadian bankruptcy law.<sup>33</sup> As one commentator later wrote, “Though in *Toga* the application and interpretation of comity was not crucial because relief could (and had to) be denied on other grounds, a potential threat to creditor equality is inherent in an attitude like that of the *Toga* court.”<sup>34</sup>

The idea of comity being linked to reciprocity has not become the majority view.<sup>35</sup> Early in section 304 litigation, one bankruptcy court found that comity is the overriding consideration guiding the other criteria found in section 304.<sup>36</sup> “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 forum state are not violated.”<sup>37</sup> This decision, while including an analysis of *Hilton v. Guyot*, failed to mention the concept of reciprocity that was so determinative in *Hilton*. Later, in the case of *Cunard S.A. Co. Ltd. v. Salen Reefer Services AB*, the Second Circuit Court of Appeals explicitly stated that “reciprocity is not an essential element in granting comity” to foreign bankruptcy proceedings.<sup>38</sup>

### C. Early U.S. Attempts at Comity in Foreign Bankruptcy Proceedings

The United States has a history of attempting to achieve universalism in its cross-border insolvency proceedings. For example, in a full case brought under the U.S. Bankruptcy Code, the Code restrains creditors subject to U.S. jurisdiction with an automatic stay against the debtor’s property located anywhere in the world.<sup>39</sup> Thus, U.S. policy seeks to prevent creditors from enticing foreign jurisdiction with a territoriality approach in an attempt to gain assets outside of U.S. jurisdiction.

Before and despite *Hilton v. Guyot*, the United States had a long history of granting comity to bankruptcy decisions of other nations. The most notable is *Canada Southern Railroad Co. v. Gebhard*.<sup>40</sup> In this case, an insolvent Canadian railroad company readjusted its bonds as part of a reorganization strategy under the

---

accordance with the order prescribed by this title. *Id.* A more complete discussion of the Section 304 criteria, including the one used to deny relief in this case, is found below.

32. 544 F.2d 624 (2d Cir. 1976).

33. *In re Toga Mfg.*, 28 B.R. at 170.

34. Ulrich Huber, *Creditor Equality in Transnational Bankruptcies: The United States Position*, 19 VAND. J. TRANSNAT’L L. 741, 759 (1986). Huber argues that *In re Toga* was decided correctly based on the application of the Section 304 criteria, regardless of the literal, and somewhat backward-thinking, approach to the definition of comity as akin to reciprocity found in *Hilton*. *Id.* at 760.

35. *Id.* at 759.

36. *In re Culmer*, 25 B.R. 621, 629 (Bankr. S.D.N.Y. 1982).

37. *Id.*

38. 773 F.2d 452, 460 (2d Cir. 1985).

39. TRANSNATIONAL INSOLVENCY PROJECT: INTERNATIONAL STATEMENT OF UNITED STATES BANKRUPTCY LAW, 109, 111 (Am. L. Inst. Tentative Draft 1997) (hereinafter AMERICAN LAW INSTITUTE US).

40. 109 U.S. 527, 538 (1883).

supervision and approval of the Canadian courts. A New York bondholder challenged the new scheme when the bonds were not paid according to the terms under which they were purchased.<sup>41</sup> The United States Supreme Court rejected the hardship to the U.S. citizen to the favor of the Canadian reorganization scheme.<sup>42</sup>

The Bankruptcy Act of 1898, section 2(a)(22), allowed the U.S. bankruptcy courts to grant comity to foreign bankruptcy provisions. Specifically, the code allowed:

When a proceeding for the purpose of the liquidation or rehabilitation of his estate has been commenced by or against a bankrupt in a court of competent jurisdiction without the United States, the court of bankruptcy may, after hearing on notice to the petitioner or petitioners and such other persons as it may direct, having regard to the rights and convenience of local creditors and other relevant circumstances, dismiss a case or suspend the proceedings therein under such terms as may be appropriate.<sup>43</sup>

The statute shows remarkable similarity to section 304 and section 305 of the Bankruptcy Reform Act of 1978, to be discussed below. The primary difference is that it does not outline the specific criteria courts are to consider when “having regard to the rights and convenience of local creditors and other relevant circumstances.”<sup>44</sup> The subsequent statutes attempt to guide the court in its considerations of the “relevant circumstances.”

Until the passage of section 304, the concept of comity with respect to foreign bankruptcy proceedings, without considerations of reciprocity, was largely the rule. Two years before the adoption of section 304 as part of the Bankruptcy Reform Act of 1978, the concept of comity alone was used to grant an injunction of U.S. proceedings to the deference of Canadian proceedings.<sup>45</sup> In *Clarkson, Co., Ltd., v. Shaheen*, trustees of a bankruptcy proceeding in Canada requested a preliminary injunction ordering the New York offices of the bankrupt corporations to turn over records and restraining them from disbursing the corporations’ property.<sup>46</sup> “We think that it would contravene the public policy of New York and the doctrine of

---

41. *Id.*

42. *Id.* at 539.

Under these circumstances the true spirit of international comity requires that schemes of this character, legalized at home, should be recognized in other countries. The fact that the bonds made in Canada were payable in New York is unimportant, except in determining by what law the parties intended their contract should be governed; and every citizen of a country, other than that in which the corporation is located, may protect himself against all unjust legislation of the foreign government by refusing to deal with its corporations.

*Id.* The dissent argued that the Canadian reorganization did not sufficiently resemble a U.S. bankruptcy in that the U.S. bondholder was not given a chance to be heard in the Canadian court. *Id.* at 543-44.

43. COLLIER ON BANKRUPTCY ¶ 304.01[2] (15th ed. revised 2005) [hereinafter COLLIER] (quoting Bankruptcy Act of 1898, §2(a)(22)).

44. *Id.*

45. *Clarkson Co., Ltd. v. Shaheen*, 544 F.2d 624, 631 (2d Cir. 1976).

46. *Id.*

comity not to recognize the Canadian judgment in these circumstances, and we therefore recognize it for present purposes.”<sup>47</sup>

## II. SECTION 304 AND ITS PROBLEMS

### A. Section 304

Section 304 of the U.S. Bankruptcy Code<sup>48</sup> is considered the first concrete step taken by any nation in the world towards universalism.<sup>49</sup> Section 304 recognized that other nations could have jurisdiction over the distribution of a debtor’s assets located in the United States.<sup>50</sup> As further explained in the house Judiciary Report for section 304,

---

47. *Id.* at 632.

48. U.S.C. §304 (2005). Cases ancillary to foreign proceedings.

(a) A case ancillary to a foreign proceeding is commenced by the filing with the bankruptcy court of a petition under this section by a foreign representative.

(b) Subject to the provisions of subsection (c) of this section, if a party in interest does not timely controvert the petition, or after trial, the court may—

(1) enjoin the commencement or continuation of—

(A) any action against—

(i) a debtor with respect to property involved in such foreign proceeding; or

(ii) such property; or

(B) the enforcement of any judgment against the debtor with respect to such property, or any act or the commencement or continuation of any judicial proceeding to create or enforce a lien against the property of such estate;

(2) order turnover of the property of such estate, or the proceeds of such property, to such foreign representative; or

(3) order other appropriate relief.

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

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

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

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

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

(5) comity; and

(6) if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns.

49. Westbrook, *supra* note 1, at 471. See also Gaa, *supra* note 14, at 893 (“Although the United States Bankruptcy Code does not confer automatic recognition and enforcement of all foreign bankruptcy adjudications, it does permit the most extensive functional harmonization of bankruptcy laws available today. In that regard it represents a functional paradigm for other states to consider in any effort to reform their municipal bankruptcy laws and thereby enhance the opportunity for harmonization of international bankruptcy cases and practices.”); Huber, *supra* note 28, at 747.

50. COLLIER, *supra* note 43, ¶ 304.03[1].

Essentially, an ancillary case means just that: it serves as a jurisdictional aid for a foreign representative to facilitate the administration of a bankruptcy or similar proceeding pending abroad. It allows a foreign representative to marshal U.S. assets and eventually repatriate them, to obtain discovery and to otherwise protect and facilitate the administration of the foreign proceeding.

where a foreign bankruptcy case is pending concerning a particular debtor and that debtor has assets in this country, the foreign representative may file a petition under this section, which does not commence a full bankruptcy case, in order to administer assets located in this country, to prevent dismemberment by local creditors of assets located here, or for other appropriate relief. The debtor is given the opportunity to controvert the petition.<sup>51</sup>

Ancillary jurisdiction is not granted automatically, but rather adjudicated on a case-by-case basis. Thus, a section 304 proceeding is considered an example of “modified universalism”<sup>52</sup> because the local courts are still given the discretion to determine whether universalism is appropriate to the situation at hand.

It is important to remember that although section 304 was revolutionary law in the field of cross-border insolvencies, it did not legitimize something that was before considered taboo or against practice. *Clarkson Co.* demonstrated that ancillary jurisdiction was available to any representative of a foreign bankruptcy proceeding who requested it and presented valid reasons for its approval.<sup>53</sup> Rather, section 304 codified *Clarkson Co.* and other common law.<sup>54</sup>

Although section 304 fell under Chapter 11 of the U.S. Bankruptcy Code, the foreign debtor was not required to be eligible for a bankruptcy proceeding in the United States as long it was subject to a foreign proceeding.<sup>55</sup> Similarly, the debtor in a section 304 proceeding need not qualify as a “debtor” under the U.S. Bankruptcy Code as long as the debtor is subject to foreign proceedings.<sup>56</sup> Unlike a plenary case in the Bankruptcy Code, it did not create a bankruptcy estate.<sup>57</sup> The foreign proceeding must be in the jurisdiction of the foreign debtor’s principal place of business or principal assets. “Thus it is clear that the willingness of the United States to defer to a foreign insolvency action is limited to the Debtor’s home-country.”<sup>58</sup> Jurisdiction of a case was limited to the district in which the proceeding against the debtor was pending or the district in which the debtor’s principal place of business, principal assets or bankrupt estate in the United States was located.<sup>59</sup>

Section 304 first provided for an injunction against any action taken by creditors against the bankrupt estate’s U.S. assets.<sup>60</sup> The second remedy allowed

---

51. S. Rep. No. 95-989, at 645, as reprinted in 11 U.S.C. §304 (2005).

52. Tagashira, *supra* note 15, at 37. See also Helmut Gerlach, *Bankruptcy in the Czech Republic, Hungary, and Poland and Section 304 of the United States Bankruptcy Code, Proceedings Ancillary to Foreign Bankruptcy Proceedings*, 22 MD. J. INT’L L. & TRADE 81, 106 (1998).

53. 544 F.2d 624, 632 (2d Cir. 1976).

54. Kraft & Aranson, *supra* note 5, at 338.

55. *In re Brierley*, 145 B.R. 151, 159 (Bankr. S.D.N.Y. 1992). See also *In re Goerg*, 884 F.2d 1562, 1567 (11th Cir. 1988).

56. *In re Goerg*, 844 F.2d at 1568.

57. COLLIER, *supra* note 43, ¶ 304.03[1].

58. AMERICAN LAW INSTITUTE US, *supra* note 39, at 110.

59. 28 U.S.C. §1410 (2005). For a more in-depth discussion, see COLLIER, *supra* note 43, ¶ 304.02[6].

60. 11 U.S.C. §304(b)(1) (2000).

under section 304 was the turnover of assets to the foreign representative to be distributed under the jurisdiction of the foreign court.<sup>61</sup> An order of turnover allowed the bankrupt estate to consolidate property in the U.S. with property located abroad.<sup>62</sup> “A turnover order is the ultimate objective of any foreign representative, and understandably, a foreign representative seeks a turnover quite frequently.”<sup>63</sup>

Apart from enforcing foreign bankruptcy judgments and relinquishing control of U.S. assets to a foreign representative, section 304 also allowed judges to grant “other appropriate relief.”<sup>64</sup> Such relief included discovery.<sup>65</sup> The court could appoint a representative “whose authority and responsibility does not extend beyond the debtor's assets and affairs in this country.”<sup>66</sup> “Other appropriate relief” might even have justified the implementation of a confidentiality order to protect the identities of investors.<sup>67</sup> Finally, under section 305<sup>68</sup> the court has the power to dismiss a case, taking into consideration the goals and criteria of section 304(c).<sup>69</sup>

Although section 304 encouraged deferral to the foreign proceedings, the property at issue in the ancillary jurisdiction was adjudicated to be property of the bankruptcy estate under the local law. According to *In re Koreag*,<sup>70</sup> a foreign debtor must first prove a valid ownership interest in the property under local law before the property can be turned over to the bankrupt estate, just as in U.S. federal

---

61. See, e.g., *In re Culmer*, 25 B.R. 621, 627 (Bankr. S.D.N.Y. 1982).

62. Gary Perlman, *The Turnover of Assets Under Section 304 of the Bankruptcy Code: The Virtues of Comity*, 12 FORDHAM INT'L L.J. 521, 527 (1989).

63. Huber, *supra* note 34, at 764.

64. 11 U.S.C. §304(b)(3) (2000).

65. *In re Gee*, 53 B.R. 891, 905 (Bankr. S.D.N.Y. 1985); *Angulo v. Kedzep, Ltd.*, 29 B.R. 417, 419 (Bankr. S.D.Tex.1983).

66. *In re Lineas Areas de Nicaragua, S.A.*, 13 B.R. 779, 780 (Bankr. Fla. 1981).

67. *In re I.G. Services Ltd.*, 244 B.R. 377, 391 (Bankr. W.D. Tex. 2000), *rev'd In re Blackwell*, 263 B.R. 505, 510 (Bankr. W.D. Tex. 2000). Although the bankruptcy court decision granting section 304 relief for enforcement of a confidentiality order was overruled by the district court, the court did not rule that such an order may never be given, just that the investors did not sufficiently prove a need for such an order in this case. *Id.*

68. 11 U.S.C. §305, before the 2005 amendments, read:

(a) The court, after notice and a hearing, may dismiss a case under this title, or may suspend all proceedings in a case under this title, at any time if—

(1) the interests of creditors and the debtor would be better served by such dismissal or suspension; or

(2)(A) there is pending a foreign proceeding; and (B) the factors specified in section 304(c) of this title warrant such dismissal or suspension.

(b) A foreign representative may seek dismissal or suspension under subsection (a)(2) of this section.

(c) An order under subsection (a) of this section dismissing a case or suspending all proceedings in a case, or a decision not so to dismiss or suspend, is not reviewable by appeal or otherwise by the court of appeals under section 158(d), 1291, or 1292 of title 28 or by the Supreme Court of the United States under section 1254 of title 28.

69. 11 U.S.C. §305. See *Interpool, Ltd. v. Certain Freights of the M/V S Venture Star*, 878 F.2d 111, 114 (3d Cir. 1989). It is not necessary for a foreign representative seeking dismissal under Section 305 to actually file for ancillary jurisdiction under section 304. *In re Gee*, 53 B.R. at 897.

70. *In re Koreag*, 961 F.2d 341, 349 (2d Cir. 1992).

bankruptcy proceedings.<sup>71</sup> This in turn produces an interesting twist of the continued application of territoriality into discussions of comity granted to legitimate foreign proceedings.

Section 304 ultimately was a statute dealing with the question of jurisdiction. It dictated how and in what circumstances a foreign representative could have control over U.S. assets, and in what circumstances the orders of a foreign court would be honored. It did not resolve the differences inherent in the bankruptcy proceedings of different nations.

Thus, the device does not solve problems created by underlying substantive differences in the laws of the various countries involved. However, it provides a structure where such differences may be traded out by the major creditors concerned, united by their common desire to conserve values available for all through accelerated termination of the proceedings.<sup>72</sup>

Although section 304 did not affect the substantive bankruptcy law of competing jurisdictions, it provided the option for a more unified cross-border proceeding that involved assets located in the United States.

#### B. *The Statutory Criteria under Section 304*

Although a section 304 petition questioned which jurisdiction would ultimately handle bankruptcy proceedings, the courts still had to consider the substantive law of the foreign jurisdiction and compare that law with the U.S. Bankruptcy Code.<sup>73</sup> Because section 304 did not automatically confer ancillary jurisdiction on a foreign representative that filed a petition, the judge had to balance the necessity of ancillary proceedings with a codified list of six criteria. These criteria are found in section 304(c).<sup>74</sup>

---

71. Robin E. Phelan & Scott W. Everett, *The Wretched Refuse – Leading the Foreign Corporation to a Fresh Start in the United States*, 59 CONSUMER FIN. L.Q. REP. 23, 39 (2005). The *Koreag* rule was followed in *In re Grandote Country Club Co.*, 208 B.R. 218, 224 (Bankr. D. Colo. 1997).

72. PHILLIP I. BLUMBERG ET AL., *BLUMBERG ON CORPORATE GROUPS* §90.07[A] (2d ed. 2005).

73. For a good illustration of thorough review of the bankruptcy laws of a foreign jurisdiction and comparison to U.S. law, see *In re Kojima*, 177 B.R. 696, 701-03 (Bankr. D. Colo. 1995).

74. 11 U.S.C. §304(c) states in relevant part:

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

- (1) just treatment of all holders of claims against or interests in such estate;
- (2) protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceeding;
- (3) prevention of preferential or fraudulent dispositions of property of such estate;
- (4) distribution of proceeds of such estate substantially in accordance with the order prescribed by this title;

As commentators have pointed out, “[t]he first two criteria appear to contradict each other.”<sup>75</sup> Protecting the claims and convenience for U.S. creditors would conflict with the just outcome of all interested parties if at least some of those parties came from foreign jurisdictions or would benefit from the bankruptcy laws of a foreign jurisdiction rather than the U.S. Bankruptcy Code. Similarly, comity is “a doctrine that accommodates jurisdictional conflicts by encouraging deference to foreign laws and judgments.”<sup>76</sup> This is in tension with factors four and six, which reflected the goals of the U.S. Bankruptcy Code but not those that might be present in foreign bankruptcy law.<sup>77</sup> As commentators have further pointed out, and courts themselves acknowledged, “[section] 304 by its terms requires an exercise of judicial discretion.”<sup>78</sup> The adoption of section 304 in 1978 began twenty-six years of litigation over these criteria.<sup>79</sup>

#### 1. Just treatment of all holders of claims against or interest in such estate

This criterion acknowledged that all creditors should be treated equally, whether they were foreign or domestic creditors or held foreign or domestic security. It also considered claims that may concern shareholders or even the debtor against the foreign representative or the administrator of the estate.<sup>80</sup> Like the other criteria considered below, a court had to consider the choice of law under which it would weigh the just treatment of claimholders. Different nations have different notions of just treatment between claim holders. Cases have found that when the foreign debtor is the United Kingdom, just treatment of all claim holders would be more likely to be found, as the United States shares the common law tradition of the United Kingdom and many similarities in the Bankruptcy Code.<sup>81</sup> For civil law countries, which treat the priority of claims very differently from the priority found in the U.S. Bankruptcy Code, this criterion required particular attention.<sup>82</sup>

#### 2. Protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceedings

Although initially U.S. creditors contesting section 304 proceedings argued that simply traveling to a foreign jurisdiction and litigating in a foreign court would

---

(5) comity; and

(6) if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns.

75. Gerlach, *supra* note 52, at 107. See also Kraft & Aranson, *supra* note 5, at 340-41.

76. COLLIER, *supra* note 43, ¶ 304.08.

77. COLLIER, *supra* note 43, ¶ 304.08[5][b].

78. *In re Treco*, 240 F.3d 148, 154-55 (2d Cir. 2001).

79. Because criteria (6) concerns only natural persons under the Bankruptcy Code, it will not be discussed in this paper. Kraft & Aranson, *supra* note 5, at 348.

80. *In re Gee*, 53 B.R. 891, 901 (Bankr. S.D.N.Y. 1985).

81. *In re Brierley*, 145 B.R. 151, 162 and n.5 (Bankr. S.D.N.Y. 1992).

82. See *In re Papeleras Reunidas, S.A.*, 92 B.R. 584, 590 (Bankr. E.D.N.Y. 1988).

satisfy this element,<sup>83</sup> subsequent cases held that the inconvenience of dealing with a foreign jurisdiction alone is not enough.<sup>84</sup> As commentators point out, “the mere fact that a claim holder has to pursue his rights abroad renders [Section 304] ineffective in any case where a foreign debtor has United States creditors.”<sup>85</sup> Recent U.S. cases under section 304 became more concerned with the procedure and treatment of creditors under the applicable foreign bankruptcy law rather than the inconvenience of processing creditors’ claims in the foreign jurisdiction.<sup>86</sup>

### 3. Prevention of preferential or fraudulent dispositions of property of such estate

A Second Circuit case characterized this criterion as permitting refusal of section 304 relief if the foreign proceeding “inadequately protects against the risk of preferential or fraudulent disposition of the estate.”<sup>87</sup> One commentator wrote, “[s]ection 304(c)(3) authorizes the court to decide only whether the law of the main proceeding sufficiently protects the estate against preferences and fraudulent transfers,” and therefore allows section 304 relief even if a preference or fraudulent transaction does exist, as long as the foreign proceeding would adequately address it.<sup>88</sup> Case law indicates that this criterion further allowed ancillary proceedings for the purposes of recovering U.S. property for the benefit of the foreign bankruptcy estate.<sup>89</sup> Conversely, this criterion has been used to deny ancillary proceedings if the court finds that the foreign proceedings would allow or tolerate disposition of property that under U.S. law could be considered preferential or fraudulent conveyances.<sup>90</sup>

---

83. *In re Lineas Areas de Nicaragua, S.A.*, 13 B.R. 779, 780 (Bankr. Fla. 1981); Kraft & Aranson, *supra* note 5, at 341. In *Lineas Areas*, the bankruptcy court did not reject the debtor’s section 304 petition. The court had previously turned over the U.S. assets to the foreign representative. *Id.* Rather, the court, at the behest of the U.S. creditors, appointed a co-trustee to represent the debtor in an attempt to preserve the debtor’s U.S. assets for the U.S. creditors so that the creditors would not “have to look to Nicaragua for payment.” *Id.*

84. *In re Culmer*, 25 B.R. 621, 632 (Bankr. S.D.N.Y. 1982) (“This result is altogether just and appropriate as these creditors dealt freely with BAOL and were undoubtedly aware that they were dealing with a bank incorporated under and subject to foreign law when they first began doing business with BAOL.”); *In re Brierley*, 145 B.R. at 163 (“But the prejudice and inconvenience of which [this U.S. creditor] complains is typical of what every U.S. creditor in a sizeable domestic case encounters when it is forced to litigate its claim.”)

85. Huber, *supra* note 34, at 751.

86. *Id.*

87. *In re Treco*, 240 F.3d 148, 158 (2d Cir. 2001).

88. Huber, *supra* note 34, at 753.

89. *In re Kojima*, 177 B.R. 696, 703 (Bankr. D. Colo. 1995). In this case, a foreign representative was allowed to attempt to recover in U.S. courts and under U.S. law property that allegedly was the subject of a fraudulent disposition in the United States for the benefit of the foreign bankrupt estate.

90. *In re Papeleras Reunidas, S.A.*, 92 B.R. 584, 592 (Bankr. E.D.N.Y. 1988). In this case, the court found that the Spanish court’s distribution of assets would amount to preferential treatment against U.S. creditors. The court was also disturbed with the lack of notice to creditors. *Id.*

4. Distribution of proceeds of such estate substantially in accordance with the order prescribed by this title.

The main question emerging from this criterion was whether secured creditors would obtain or maintain similar primacy positions in the foreign jurisdiction as under the U.S. Bankruptcy Code.<sup>91</sup> “An exact match is not required; similarity, not duplication, is the standard.”<sup>92</sup> Some cases have held that a legitimate proceeding that accords the creditors standing and primacy in court satisfies this requirement.<sup>93</sup> However, if secured creditors under U.S. law would be placed at a disadvantage in the foreign proceeding, ancillary jurisdiction would not be granted.<sup>94</sup> For example, in *Toga Manufacturing Limited*, a creditor considered a secured creditor in the United States would have lost his secured status under Canadian bankruptcy law.<sup>95</sup> This case was distinguished from *Matter of Culmer*,<sup>96</sup> which granted ancillary jurisdiction because the creditor would not have been considered a secured creditor under U.S. law and therefore would not have been placed at a disadvantage in the foreign proceedings.<sup>97</sup>

Even when a creditor would not lose his secured status, other perceived disadvantages to creditors have warranted denial of ancillary relief. For example, in *Interpool, Ltd.*, the court denied ancillary relief because creditors in the Australian proceedings would not have access to the proceedings.<sup>98</sup> The court was further disturbed with the lack of notice to all creditors and the lack of equitable subordination.<sup>99</sup> In *In re Treco*, the Second Circuit denied ancillary relief because under Bahamian bankruptcy law, a U.S. creditor’s secured claim to the funds in its account would be subordinated to other costs and expenses, such as administrative expenses.<sup>100</sup>

5. Comity

“The addition of comity (which occurred at a late stage of legislation) to the other principles of this subsection has confused the courts considering petitions of

---

91. Huber, *supra* note 34, at 756.

92. COLLIER, *supra* note 43, at ¶ 304.08[4].

93. *In re Brierley*, 145 B.R. 151, 167 (Bankr. S.D.N.Y. 1992). *But see* Kraft & Aranson, *supra* note 5, at 348 (arguing that change of creditor status from secured to unsecured should not be a sort of protectionism used by U.S. courts to deny ancillary proceedings).

94. *In re Toga Mfg. Ltd.*, 28 B.R. 165, 168-169 (Bankr. E.D. Mich. 1983).

95. Huber, *supra* note 34, at 756-757.

96. *In re Culmer*, 25 B.R. 621, 629 (Bankr. S.D.N.Y. 1982).

97. *Id.*; *see also* Huber, *supra* note 34, at 756-57.

98. *Interpool, Ltd. v. Certain Freights of M/V Venture Star*, 102 B.R. 373, 378 (Bankr. D.N.J. 1988).

99. *Id.* at 379. Note that the court does not state that equitable subordination would be specifically applicable or useful to the creditors in the case at hand; it merely discusses its absence in Australian bankruptcy law.

100. *In re Treco*, 240 F.3d 148, 158 (2d Cir. 2001).

foreign representatives rather than aided them in this process.”<sup>101</sup> As discussed above, the case shaping the concept of comity in the United States, *Hilton*, has itself caused confusion. Some decisions, such as *In re Toga Manufacturing*, used comity to protect domestic creditors from a lack of reciprocity in foreign courts to comity of U.S. decisions.<sup>102</sup> Decisions from other courts have stated that comity is most readily granted when the bankruptcy laws of the foreign jurisdiction “are in harmony with those of the United States.”<sup>103</sup> Complete harmony of all aspects of the law, however, is not necessary.<sup>104</sup> The United Kingdom is given special consideration of comity because the United States takes its bankruptcy code from the English common law tradition. The same has been said for the bankruptcy laws of Canada,<sup>105</sup> the Bahamas,<sup>106</sup> and the Cayman Islands.<sup>107</sup>

Early in the history of section 304 case law, the bankruptcy court for the Southern District of New York, with *Matter of Culmer*, set the standard that the five other section 304 criteria fall within the overarching consideration of comity.<sup>108</sup> Comity was the only section 304 criteria discussed by the Second Circuit Court of Appeals in *Cunard S.A. Co. Ltd. v. Salen Reefer Services AB*.<sup>109</sup> Then, the Second Circuit arguably changed the standard of primacy given to the criterion of comity with *In re Treco*.<sup>110</sup> The court acknowledged the view that comity was the ultimate consideration for deciding section 304 criteria but found that comity should be considered “in light of the other factors.”<sup>111</sup> This ruling is more in line with relevant legislative history. “[T]he legislative history reflects that when Representative Don Edwards introduced the final bill to the House, he stated: ‘Section 304(c) is modified to indicate that the court shall be guided by considerations of comity *in addition* to the other factors specified therein.’”<sup>112</sup>

---

101. Huber, *supra* note 32, at 760-61.

102. *In re Toga Mfg. Ltd.*, 28 B.R. 165, 170 (Bankr. E.D. Mich. 1983).

103. *In re Culmer*, 25 B.R. 621, 632 (Bankr. S.D.N.Y. 1982).

104. *In re Ward*, 201 B.R. 357, 362 (Bankr. S.D.N.Y. 1996). In this case, petitioner asserted that comity should not be granted because the Zambian legal system’s rules of ethics allowed aspects that notably would not be allowed in the United States, and that this in turn should prove that “the entire Zambian legal system is flawed.” The court admitted the actions were questionable under the American notion of ethics but did not find that to be proof that the entire Zambian legal system is repugnant or substantially unfair to the U.S. system. *Id.*

105. *In re Culmer*, 25 B.R. at 631.

106. *Id.*

107. *In re Gee*, 53 B.R. 891, 902 (Bankr. S.D.N.Y. 1985).

108. *In re Culmer*, 25 B.R. at 629 (“All of the factors listed in Section 304(c) have historically been considered within a court’s determination whether to afford comity to a proceeding in a foreign nation.”). The court looked to Second Circuit pre-section 304 case law to say that “the central examination which it must undertake in order to comply with Section 304(c) is whether the relief petitioners seek will afford equality of distribution of the available assets.” *Id.* at 628 (citing *Israel British Bank (London), Ltd. v. Federal Deposit Insurance Corp.*, 536 F.2d 509, 513 (2d Cir. 1976)).

109. 773 F.2d 452, 456 (2d Cir. 1985).

110. 240 F.3d 148, 156 (2d Cir. 2001).

111. *Id.*

112. *In re Papeleras Reunidas, S.A.*, 92 B.R. 584, 594 (Bankr. E.D.N.Y. 1988) (quoting *Bankruptcy Reform Act of 1978*, Pub.L. No. 95-598).

C. *The definition of “Foreign Proceedings”*

A second area of contention in section 304 litigation became deciding which types of judicial proceedings in foreign courts constituted “foreign proceedings” under section 304.<sup>113</sup> Although eligibility for Chapter 7 or Chapter 11 proceedings under the U.S. Bankruptcy Code is not necessary, “a foreign proceeding must have some purpose related to bankruptcy, insolvency or financial reorganization, however, for relief under section 304 to be available.”<sup>114</sup> The context of financial reorganization became difficult to discern from corporate restructuring done for purposes other than readjustment of debts.

One of the first cases to seriously analyze the question of which types of proceedings available in foreign jurisdictions would constitute “foreign proceedings” under section 304 was *In re Tam*.<sup>115</sup> The debtor, a corporation organized under the laws of the Cayman Islands, entered into a voluntary winding up of business and distribution of assets.<sup>116</sup> In debating the section 304 petition filed in the United States, the court was quick to note that the liquidators selected by the debtor in a voluntary winding up under Cayman law “operate free from the supervision and control of the Cayman Court.”<sup>117</sup> Creditors had no voice in the proceeding and little right to notice of the liquidators’ actions.<sup>118</sup> Although the liquidators must report to the government at the end of the voluntary winding up, the government, as characterized by the court in this case, played a ministerial role only.<sup>119</sup> For these reasons, the court found that the Cayman voluntary winding up did not constitute a “foreign proceeding” for the purposes of section 304.<sup>120</sup>

Two years later, the bankruptcy court for the Southern District of New York limited *In re Tam* by classifying the case as having been decided upon the factors

---

113. A foreign proceeding, as defined in 11 U.S.C. §101(23) under the prior law, is 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.

114. COLLIER, *supra* note 43, ¶ 304.02[1].

115. *In re Tam*, 170 B.R. 838 (Bankr. S.D.N.Y. 1994).

116. *Id.* at 839.

117. *Id.* at 841.

118. *Id.* at 843.

119. *Id.*

120. *Id.* at 844. The court acknowledged that prior cases dealing with laws derived from the British Companies Act have found the foreign law to be substantially the same as the U.S. Bankruptcy Code and therefore eligible for section 304 relief. In a footnote, the court distinguished many of those prior cases. *Id.* at 845, n.12. The debtor in that case was insolvent. *Id.*

It is also necessary to remember that section 304 petitions are examined on a case-by-case basis. For this reason, other Cayman Islands proceedings may be classified as “foreign proceedings,” even though the voluntary winding up was not found to be a foreign proceeding in *In re Tam*. For example, the bankruptcy court for the Southern District of New York found a provisional liquidation under Cayman law to be a “foreign proceeding” eligible for section 304 relief in *In re MMG LLC*, 256 B.R. 544, 550 (Bankr. S.D.N.Y. 2000). In this case, the debtor was “undeniably insolvent.” *Id.*

of governmental oversight and creditor voice in the proceedings.<sup>121</sup> With *In re Ward*, the court examined the voluntary winding up of a company under Zambian law and remarked that “the government plays no regulatory or supervisory role in this winding up other than to collect fees.”<sup>122</sup> There was no application to a court to commence the proceeding, and a court did not issue a final order of dissolution.<sup>123</sup> However, there was substantial creditor notice, and creditors were given the option of petitioning the court for a judicial liquidation if they could show prejudice by the voluntary winding up.<sup>124</sup> The liquidator’s role was nearly identical to that of a judicial liquidation.<sup>125</sup> The court considered the Zambian law to differ from Cayman law concerning a voluntary winding up in that there was more ready access to the court system by creditors, and creditors were allowed to participate and be heard in the proceedings equal to their rights under a judicial liquidation.<sup>126</sup> It ruled the Zambian voluntary winding up to be a foreign proceeding under section 304.<sup>127</sup>

Following the importance given to creditor voice and participation in the proceedings, the bankruptcy court for the Southern District of New York found that a Bermuda “Scheme of Arrangement” to facilitate a voluntary run-off of business constituted “foreign proceedings” in *In re Hopewell*.<sup>128</sup> It was Bermuda’s first use of a cut-off scheme of arrangement for a solvent company’s run-off.<sup>129</sup> In discussing whether the Scheme of Arrangement qualified as a “foreign proceeding” under section 304, the court began its analysis by noting that the Scheme of Arrangement did “not exist in tandem with another statutory vehicle for debt manipulation such as a voluntary liquidation, administration or court-ordered winding-up.”<sup>130</sup> The court, following *Tam*, looked to the degree of judicial involvement and supervision and the degree of access to the court available to creditors in the questioned proceedings.<sup>131</sup> After creditor approval of the Scheme by vote, the Scheme was then again sanctioned by the Bermuda court.<sup>132</sup> Creditors had the opportunity to object with their proxy forms, at the creditors’ meeting and at the sanction hearing in the Bermuda court.<sup>133</sup> Considering the high level of involvement by the court, and Hopewell’s description of the Scheme as a “prepackaged Chapter 11 plan,”<sup>134</sup> the court ruled the Scheme to qualify as a

---

121. *In re Ward*, 201 B.R. 357, 361 (Bankr. S.D.N.Y. 1996). Both *In re Tam* and *In re Ward* were decided by the same bankruptcy judge, the Honorable James L. Garrity, Jr.

122. *Id.* at 360.

123. *Id.* at 359.

124. *Id.* at 360-61.

125. *Id.* at 361.

126. *Id.* at 361-62.

127. *Id.* at 361.

128. *In re Bd. of Dirs. of Hopewell Int’l Ins. Ltd.*, 238 B.R. 25, 35 n.7 (Bankr. S.D.N.Y. 1999).

129. *Id.* at 35.

130. *Id.* at 48.

131. *Id.* at 50.

132. *Id.* at 51.

133. *Id.* at 51-52.

134. *Id.* at 52.

foreign proceeding subject to section 304 relief.<sup>135</sup> The decision was affirmed on appeal.<sup>136</sup> The district court noted the multiple appearances in front of the Bermuda court and the Bermuda court's approval of the scheme.<sup>137</sup>

In considering the question of proceedings qualifying as foreign proceedings under section 304, a California bankruptcy court characterized the determining factor in *Hopewell* to be the amount of judicial involvement and supervision.<sup>138</sup> In *In re Master Home Furniture Co.*, the court compared the amount of judicial involvement in *Hopewell* to the Southern District of New York bankruptcy court's ruling in *In re Tam*, which was conducted "without any regulatory oversight [sic] and virtually no creditor participation."<sup>139</sup> The conclusion reached in *In re Master Home Furniture* found that the Taiwanese reorganization did not meet the definition of foreign proceedings because there was no judicial supervision during the reorganization of the company petitioning for section 304 recognition of the reorganization, and the requested relief only applied to certain creditors.<sup>140</sup>

Finally, *In re Rose*, decided by the bankruptcy court of the Southern District of New York, brought back into perspective the necessity of financial reorganization. "This case tests the limits of the 'near blank check' flexibility a bankruptcy court has to fashion relief in a case under §304 of the Bankruptcy Code."<sup>141</sup> In *Rose*, thirteen British insurance and reinsurance companies sought recognition in the United States of a "Transfer Scheme" sanctioned by the High Court of Justice in England. "The Transfer Scheme proposes to effect a corporate restructuring by shifting the majority of assets and liabilities of twelve of the Corporations into the thirteenth Corporation."<sup>142</sup> These corporations also wished to run off their existing business to one company in order to lessen the amount of money the corporations were required by U.S. regulations to keep tied up in U.S. trust funds.<sup>143</sup> The section 304 petition requested an injunction to recognize the Transfer Scheme and head off any possible litigation.<sup>144</sup>

In response to the proposition that the Transfer Scheme available under English law falls under the term "reorganization" used to define a "foreign proceeding" in the U.S. Bankruptcy Code, the court found that the term "reorganization" must be understood in the context of Chapter 11.<sup>145</sup> The court noted that although solvent debtors may file bankruptcy proceedings to voluntarily distribute their assets to creditors, the proceedings here were not bankruptcy

---

135. *Id.*

136. *In re Bd. of Dirs. of Hopewell Int'l Ins. Ltd.*, 275 B.R. 699, 702 (Bankr. S.D.N.Y. 2002).

137. *Id.* at 707.

138. *In re Master Home Furniture Co. Ltd.*, 261 B.R. 671, 675 (Bankr. C.D. Cal. 2001) (quoting *In re Bd. of Dirs. of Hopewell Int'l Ins. Ltd.*, 238 B.R. 25 (Bankr. S.D.N.Y. 1999)).

139. *Id.*, quoting *In re Tam*, 170 B.R. 838, 843 (Bankr. S.D.N.Y. 1994).

140. *In re Master Home Furniture Co.*, 261 B.R. at 677. The court also found that the section 304 petitioners did not meet the definition of foreign representatives. *Id.* at 678.

141. *In re Rose*, 318 B.R. 771, 772 (Bankr. S.D.N.Y. 2004).

142. *Id.* at 773.

143. *Id.*

144. *Id.* at 776 n.8.

145. *Id.* at 774. The decision emphasized the necessity of putting words into context and quoted a passage from Lewis Carroll's *Through the Looking Glass*. *Id.*

proceedings but corporate restructuring.<sup>146</sup> Section 304 relief is simply not available for corporate reorganization absent a bankruptcy proceeding. As the court concludes,

when all is said and done, Mr. Rose is asking the court to do what it cannot – to enter an order allowing him to use the bankruptcy law to enjoin potential lawsuits in the United States so he can effect a corporate financial restructuring of a group of foreign insurance companies unrelated to any foreign insolvency proceeding.<sup>147</sup>

The case analysis did not discuss the amount of court supervision or creditor involvement in the reorganization proceedings. It based its decision solely on the view that the corporate restructuring was not needed for readjustment of debts.<sup>148</sup>

### III. THE NEW CHAPTER 15

In May of 1997 the United Nations Commission on International Trade Law (UNCITRAL) adopted the Model Law on Cross-Border Insolvency.<sup>149</sup> The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005,<sup>150</sup> adopted by Congress on April 20, 2005, adopted the Model Law on Cross-Boarder Insolvency into a new “Chapter 15” of the Bankruptcy Code.<sup>151</sup> “The Guide to Model Law emphasizes that the Model Law is intended to be incorporated directly into the law of enacting states on a statutory, rather than treaty, basis and that the effectiveness of the Model Law depends in part upon enacting states maximizing the uniformity of their enactments.”<sup>152</sup>

Chapter 15 followed the Model Law as much as possible “to promote uniformity in its adoption and application.”<sup>153</sup> It essentially expanded the “breadth

---

146. *Id.* at 775.

147. *Id.* at 776.

148. *Id.*

149. COLLIER, *supra* note 43, ¶ 304.09[1][c].

150. Pub. L. No. 109-8 (2005).

151. The Model law of Cross-Border Insolvencies was approved by the United Nations Commission on International Trade Law (UNCITRAL) in 1997. Edward T. Canuel, *United States – Canadian Insolvencies: Reviewing Conflicting Legal Mechanisms, Challenges and Opportunities for Cross-Border Cooperation*, 4 J. INT'L BUS. & L. 8, 24 (2005).

152. COLLIER, *supra* note 43, ¶ 304.09[1][c].

153. *Id.* ¶ 1501.01. As far as other nations adopted the Model Law, “Legislation based on the UNCITRAL Model Law on Cross-Border Insolvency has been adopted in Eritrea, Japan (2000), Mexico (2000), Poland, Romania (2003), South Africa (2000), Montenegro (2002) and British Virgin Islands (2005). The United Kingdom has adopted legislation enabling the Model law to be adopted by regulation. Enactment is under consideration in Argentina and Pakistan and has been recommended in New Zealand, Australia and Canada. The Spanish Insolvency Act, effective 2004, contains provisions which reflect in part the Model Law.” *Id.* ¶ 1501.01 n.2.

To show the level of conformity to the Model Law, Section 1501 includes an application of Chapter 15 to “creditors or other interested persons request in a foreign country have an interest in requesting the commencement of, or participating in, a case or proceeding under this title.” 11 U.S.C. §1501(b)(4)(2005). This has not been a problem under the U.S. Bankruptcy Code, which does not

and detail” that section 304 recognition of foreign proceedings attempted to provide cross-border insolvencies.<sup>154</sup> “Chapter 15 then envelops its mechanism for ancillary relief in a broader structure that mandates cooperation with foreign courts and foreign representatives and coordination of multiple proceedings involving a common debtor.”<sup>155</sup> The first section of Chapter 15 specifies the chapter as applying to the traditional request for ancillary jurisdiction found under the old section 304 as well as main proceedings brought in the U.S. that require assistance in a foreign country, concurrent proceedings involving the same debtor, and foreign creditors with an interest in proceedings taking place in the U.S.<sup>156</sup> It lists the objectives as including cooperation with foreign courts in dealing with such multi-jurisdictional insolvency, administration of insolvencies in the best interests of the creditors and debtor, protection of the debtor’s assets, facilitation in the reorganization of troubled business, and “greater legal certainty for trade and investment.”<sup>157</sup> Thus Chapter 15 emphasizes the resolution of procedural issues, though it does not harmonize substantive issues with the laws of foreign jurisdictions.<sup>158</sup>

A particularly notable provision appears in section 1506, named the “Public policy exception.” It reads, “[n]othing in this chapter prevents the court from refusing to take an action governed by this chapter if the action would be manifestly contrary to the public policy of the United States.”<sup>159</sup> Although UNCITRAL included this exception under the assumption it would be limited to constitutional issues, “[n]onetheless, there was a concern that the exception could be read broadly and used to undermine the Model Law. The addition of the word ‘manifestly’ was intended to insure a narrow reading of the exception.”<sup>160</sup> Chapter 15 includes a provision that the statutes do not override any treaty between the U.S. and another country.<sup>161</sup> Chapter 15 also allows a court to grant permission for a trustee to act on behalf of an estate in a foreign jurisdiction.<sup>162</sup> Section 305 continues to serve the same purpose under the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 as under the prior Bankruptcy Code in that, if the goals of ancillary proceedings or Chapter 15 would be furthered, section 305 authorizes a court to abstain from a related proceeding.<sup>163</sup>

---

discriminate against foreign creditors, but was included to conform with the Model Law. COLLIER, *supra* note 43, ¶ 1501.04.

154. 2005 BANKRUPTCY REFORM LEGISLATION WITH ANALYSIS, 84 (2005).

155. COLLIER, *supra* note 41, ¶ 1501.01.

156. 11 U.S.C. §1501.

157. *Id.*

158. BLUMBERG, *supra* note 72, §90.07[C].

159. 11 U.S.C. §1506.

160. COLLIER, *supra* note 43, ¶ 1506.02.

161. 11 U.S.C. §1503.

162. 11 U.S.C. §1505.

163. COLLIER, *supra* note 43, ¶ 1501.03. 11 U.S.C. §305 (2005) now states:

- (a) The court, after notice and a hearing, may dismiss a case under this title, or may suspend all proceedings in a case under this title, at any time if—
- (1) the interests of creditors and the debtor would be better served by such dismissal or suspension; or

### A. Recognition

Section 1509 explains how a foreign representative may petition a court for recognition of foreign proceedings.<sup>164</sup> It further states that once recognition is granted, the foreign representative has direct access to the courts and shall be granted “comity and cooperation.”<sup>165</sup> The foreign representative may sue and be sued in U.S. courts. However, the foreign representative is not subject to the jurisdiction of the U.S. courts for any other purpose outside of Chapter 15 proceedings.<sup>166</sup> Interestingly, “[i]f the court denies recognition under this chapter, the court may issue any appropriate order necessary to prevent the foreign representative from obtaining comity or cooperation from courts in the United States.”<sup>167</sup> This combats yet another weakness of the prior section 304. “Section 304 was not the exclusive vehicle for a foreign representative to seek relief nor was there a single venue for a section 304 proceeding. Thus, foreign representatives could, theoretically at least, try their luck in a variety of courts, with failure in one not precluding a second try in another.”<sup>168</sup>

The directives in filing a petition for recognition of a foreign proceeding are found in section 1515. In order to be granted recognition of foreign proceedings by U.S. courts, the statute now requires formal evidence of a foreign proceeding in existence in a foreign court.<sup>169</sup> Along with the petition and evidence of the foreign proceeding, the representative must submit “a statement identifying all foreign proceedings with respect to the debtor that are known to the foreign representative.”<sup>170</sup> Thus, Chapter 15 envisions coordination between all proceedings regarding the debtor, as indicated in section 1501. The evidence submitted by the foreign representative concerning the existence of foreign proceedings is entitled to a presumption of genuineness and authentication.<sup>171</sup>

Once a petition has been filed under section 1515, there is notice to the interested parties and a hearing.<sup>172</sup> If the foreign proceeding, the foreign representative and the petition meet the guidelines of Chapter 15, the court must

---

(2)(A) a petition under section 1515 for recognition of a foreign proceeding has been granted; and, (B) the purposes of chapter 15 of this title would be best served by such dismissal or suspension.

(b) A foreign representative may seek dismissal or suspension under subsection (a)(2) of this section.

(c) An order under subsection (a) of this section dismissing a case or suspending all proceedings in a case, or a decision not so to dismiss or suspend, is not reviewable by appeal or otherwise by the court of appeals under section 158(d), 1291, or 1292 of title 28 or by the Supreme Court of the United States under section 1254 of title 28.

164. 11 U.S.C. §1509.

165. 11 U.S.C. §1509(b).

166. 11 U.S.C. §1510.

167. 11 U.S.C. §1509(d).

168. COLLIER, *supra* note 43, ¶ 1509.02.

169. 11 U.S.C. §1515.

170. 11 U.S.C. §1515(c).

171. 11 U.S.C. §1516.

172. 11 U.S.C. §1517.

grant an order of recognition.<sup>173</sup> An order of recognition may be terminated or modified upon a change of circumstances,<sup>174</sup> and the filing of a petition places a duty upon the foreign representative to notify the court of any “change of status” concerning the foreign proceeding, the foreign representative, or other proceedings involving the debtor.<sup>175</sup> Section 1519 provides for relief during the “gap” between the filing of a Chapter 15 petition and the grant of such a petition under section 1521.<sup>176</sup> “Relief of a provisional nature,” including stays and entrustment of a debtor’s assets to a foreign representative, is available upon request after the filing of a petition under section 1515.<sup>177</sup>

Recognition grants the same administration regarding the debtor’s property that would be available in a U.S. proceeding.<sup>178</sup> Other relief that may be granted upon recognition of a foreign proceeding includes a stay of court action against a debtor’s assets, rights, or obligations, a stay of execution, entrustment of a debtor’s U.S. assets to the foreign representative, and any additional relief deemed necessary by the court.<sup>179</sup> Discovery is available.<sup>180</sup> However, recognition also limits the availability of plenary proceedings. Once recognition of a foreign main proceeding has been granted, a case under the U.S. Bankruptcy Code may be commenced only if the debtor has assets in the United States, and the case shall be restricted to those U.S. assets alone.<sup>181</sup>

#### B. *Main versus Non-main Proceedings*

Section 1502 contains definitions to be used specifically in the application of Chapter 15.<sup>182</sup> Section 1502 states that “foreign main proceedings” are “foreign proceeding pending in the country where the debtor has the center of its main interests.”<sup>183</sup> This is distinguished from “foreign non-main proceedings,” which could be brought in any country, other than the location of the business’ main interests, in which the debtor has an establishment.<sup>184</sup> Furthermore, an “establishment” must include “nontransitory economic activity.”<sup>185</sup> “By omission, a foreign proceeding that is premised only on the presence of assets in the foreign country is not eligible for recognition.”<sup>186</sup>

---

173. 11 U.S.C. §1517(a), stating in relevant part, “an order recognizing a foreign proceeding shall be entered if-”

174. 11 U.S.C. §1517(d).

175. 11 U.S.C. §1518.

176. COLLIER, *supra* note 43, ¶ 1519.01.

177. 11 U.S.C. §1519.

178. 11 U.S.C. §1520.

179. 11 U.S.C. §1521.

180. 11 U.S.C. §1521(a)(4).

181. 11 U.S.C. §1528.

182. 11 U.S.C. §1502.

183. 11 U.S.C. §1502(4).

184. 11 U.S.C. §1502(5).

185. 11 U.S.C. §1502(2).

186. COLLIER, *supra* note 43, ¶ 1517.02.

This distinction between main and non-main proceedings is taken into consideration in section 1511, “Commencement of a case under section 301 or 303.”<sup>187</sup> “Upon recognition, a foreign representative may commence (1) an involuntary case under section 303; or (2) a voluntary case under section 301 or 302, if the foreign proceeding is a foreign main proceeding.”<sup>188</sup> Thus, although Chapter 15 is intended to supplement foreign proceedings, it also allows commencement of a plenary case under another chapter of Title 11.<sup>189</sup> In addition, before a U.S. court will grant relief to a petition brought by a foreign representative of a non-main proceeding, “the court must be satisfied that the relief relates to assets that, under the law of the United States, should be administered in the foreign non-main proceeding or concerns information required in that proceeding.”<sup>190</sup>

### C. Cooperation and Coordination

Special attention is paid in Chapter 15, as it is with the Model Law on Cross-Border Insolvency, to the goal of international coordination.<sup>191</sup> The “Forms of cooperation” referred to in Chapter 15 are listed specifically in section 1527.<sup>192</sup> Cooperation referred to in sections 1525 and 1526 may be implemented by any appropriate means, including—

- (1) appointment of a person or body, including an examiner, to act at the direction of the court;
- (2) communication of information by any means considered appropriate by the court;
- (3) coordination of the administration and supervision of the debtor's assets and affairs;
- (4) approval or implementation of agreements concerning the coordination of proceedings; and

---

187. 11 U.S.C. §1511.

188. *Id.*

189. COLLIER, *supra* note 43, ¶ 1501.01.

190. 11 U.S.C. §1521(c). *See also* 11 U.S.C. §1523(b), which states, “When a foreign proceeding is a foreign non-main proceeding, the court must be satisfied that an action under subsection (a) relates to assets that, under United States law, should be administered in the foreign non-main proceeding.”

191. 11 U.S.C. §1508 (stating, “In interpreting this chapter, the court shall consider its international origin, and the need to promote an application of this chapter that is consistent with the application of similar statutes adopted by foreign jurisdictions”).

192. 11 U.S.C. §1527.

(5) coordination of concurrent proceedings regarding the same debtor.<sup>193</sup>

Reflecting back to the goals of Chapter 15 as listed in section 1501, this section amplifies the intent of the Model Law to achieve maximum efficiency of cross-border insolvencies. “Both subsections 1526(a) and (b) require that such cooperation and direct communication be subject to the supervision of the court,” although court approval is not necessary for each act of communication but rather is in general subject to court supervision.<sup>194</sup> “None of these suggestions are novel in the United States, and all can be found in various reported decisions and protocols approved in cases. The list of suggestions may be more useful to countries without the developed jurisprudence of the United States.”<sup>195</sup> Section 1529 likewise furthers the goal of coordination between foreign proceedings recognized under this chapter and other U.S. bankruptcy proceedings involving the same debtor by calling for review of relief granted under Chapter 15 in relation to other U.S. proceedings.<sup>196</sup> Section 1530 coordinates Chapter 15 relief with multiple foreign main and non-main proceedings, taking into account any relief granted by other courts with jurisdiction over the debtor.<sup>197</sup> In conclusion, section 1532 attempts to prevent creditors from collecting on the same debt through payment in a foreign proceeding and additional payment in a U.S. proceeding.<sup>198</sup>

#### *D. Steps taken by Chapter 15 to amend Section 304 problems*

##### 1. Limited use of statutory criteria

The six criteria governing the consideration of section 304 ancillary proceedings have not been discarded in the new Chapter 15. They can be found in section 1507.<sup>199</sup> However, these criteria are no longer mandatory considerations

---

193. *Id.*

194. COLLIER, *supra* note 43, ¶ 1526.01.

195. *Id.* ¶ 1527.01.

196. 11 U.S.C. §1529.

197. 11 U.S.C. §1530.

198. 11 U.S.C. §1532.

199. 11 U.S.C. §1507.

#### Additional assistance

(a) Subject to the specific limitations stated elsewhere in this chapter the court, if recognition is granted, may provide additional assistance to a foreign representative under this title or under other laws of the United States.

(b) In determining whether to provide additional assistance under this title or under other laws of the United States, the court shall consider whether such additional assistance, consistent with the principles of comity, will reasonably assure-

- (1) just treatment of all holders of claims against or interests in the debtor's property;
- (2) protection of claim holders in the United States against prejudice and inconvenience in the processing of claims in such foreign proceeding;
- (3) prevention of preferential or fraudulent dispositions of property of the debtor;
- (4) distribution of proceeds of the debtor's property substantially in accordance with the order prescribed by this title; and

for all petitions for ancillary jurisdiction. They are only to be considered if, once recognition of the foreign proceeding is granted, the court feels “additional assistance” is necessary.<sup>200</sup>

One other aspect of the criteria has changed dramatically as well; comity is no longer listed as the fifth criterion. Now comity is included as an overarching principal when considering the remaining five criteria,<sup>201</sup> a solution proposed by foreign commentator Ulrich Huber in 1986.<sup>202</sup> The wording of the remaining five criteria remains the same as that found in the former section 304. For this reason, the case law considering section 304 will continue to play a relevant part in the interpretation of section 1507 in the new Chapter 15.

Chapter 15 codifies the section 304 case law that protected the interests of U.S. creditors from foreign proceedings that would otherwise harm or subordinate their interests. It ensures that the rights of U.S. creditors are not endangered.<sup>203</sup> Section 1522 states that any action taken by the court may be taken “only if the interests of the creditors and other interested entities, including the debtor, are sufficiently protected.”<sup>204</sup> Chapter 15 also codifies the rights of foreign creditors to the U.S. court system. “Foreign creditors have the same rights regarding the commencement of, and participation in, a case under this title as domestic creditors.”<sup>205</sup> A foreign creditor may never be given priority lower than general unsecured creditors.<sup>206</sup> The Chapter also provides for equal notice to foreign creditors as to U.S. creditors.<sup>207</sup>

Section 1507 might not have been necessary, as section 1519 already grants courts the power to grant provisional relief, and section 1521 provides other appropriate relief upon recognition of a foreign proceeding. “In light of this

(5) if appropriate, the provision of an opportunity for a fresh start for the individual that such foreign proceeding concerns.

200. *Id.*

201. 11 U.S.C. §1507(b) (“In determining whether to provide additional assistance under this title or under other laws of the United States, the court shall consider whether such additional assistance, consistent with the principles of comity, will reasonably assure . . .”) (emphasis added).

202. Huber, *supra* note 34, at 761.

[C]omity is not necessary to the resolution of whether the foreign court has proper jurisdiction over the debtor, as may be the case with questions of recognition and enforcement of other acts of foreign judiciaries. This resolution must be founded on section 304(a), ignoring the principles of subsection (c) but guided by the definition of the term “foreign proceeding” in section 101(20) of the Code. Accordingly, the scope of the applicability of section 304(c)(5) is reduced to the question whether the foreign adjudication in bankruptcy violated United States public policy. If comity is limited to such a narrow field of application, it would be far better to replace the term in section 304(c)(5) and to define explicitly the requirement’s range.

203. 11 U.S.C. §1521(b).

Upon recognition of a foreign proceeding, whether main or non-main, the court may, at the request of the foreign representative, entrust the distribution of all or part of the debtor’s assets located in the United States to the foreign representative or another person, including an examiner, authorized by the court, provided that the court is satisfied that the interests of creditors in the United States are sufficiently protected.

204. 11 U.S.C. §1522(a).

205. 11 U.S.C. §1513(a).

206. 11 U.S.C. §1513(b).

207. 11 U.S.C. §1514.

display of weaponry, it is not clear what section 1507 adds to the arsenal.”<sup>208</sup> However, it does allow courts to incorporate the prior section 304 case history into their current analysis of Chapter 15.<sup>209</sup> It also necessitates the continued comparison of the substantive bankruptcy laws of the United State and the foreign jurisdiction when applying the five criteria to the case at hand.

## 2. Clear statutory definition of “Foreign Proceedings”

The new Bankruptcy Code now contains a much clearer definition of foreign proceeding. As it stands, a “foreign proceeding” under the new Code,

means a collective judicial or administrative proceeding in a foreign country, including an interim proceeding, under a law relating to insolvency or adjustment of debt in which proceeding the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganization or liquidation.<sup>210</sup>

Thus, under this new definition in Chapter 15, the specification of proceedings “under the law relating to insolvency or the adjustment of debt” underlines that “[C]hapter 15 is available not only to debtors that are technically insolvent or facing liquidation but also to debtors who are in financial distress and may need to reorganize.”<sup>211</sup> However, section 1531 gives a “presumption of insolvency based on recognition of a foreign main proceeding.”<sup>212</sup> The statute states, “In the absence of evidence to the contrary, recognition of a foreign main proceeding is . . . proof that the debtor is generally not paying its debts as such debts become due.”<sup>213</sup> Since under U.S. Bankruptcy law a voluntary case may be filed under Chapter 11 without a determination of insolvency, this presumption only applies to involuntary cases under the Bankruptcy Code.<sup>214</sup>

Under these new statutes, it is left unclear whether the Scheme of Arrangement in *In re Hopewell*, which altered the contract of the debtor with its creditors for the purpose of eventually winding down its business, would be considered a foreign proceeding. Although Collier highlights that foreign proceedings include reorganization for debtors who are in financial distress,<sup>215</sup> Hopewell predicted it would still be solvent at the conclusion of its run off.<sup>216</sup> *In re Rose*, on the other hand, would have come out with the same conclusion if it had been adjudicated under Chapter 15 because, in the court’s opinion, the corporate restructuring did

---

208. COLLIER, *supra* note 43, ¶ 1507.01.

209. *Id.*

210. 11 U.S.C. §101(23) (2005).

211. COLLIER, *supra* note 43, ¶ 101.23.

212. 11 U.S.C. §1531.

213. *Id.*

214. COLLIER, *supra* note 43, ¶ 1531.01.

215. *Id.* ¶ 101.23.

216. *In re Bd. of Dirs. of Hopewell Int’l Ins. Ltd.*, 238 B.R. 25, 35 n.7 (Bankr. S.D.N.Y. 1999).

not come under laws relating to insolvency or adjustment of debt.<sup>217</sup> Yet all corporate restructuring will have financial considerations at the heart of the reorganization. Future case law will have to form the distinction between simple financial restructuring and adjustment of debt.

#### IV. CROSS-BORDER INSOLVENCY OF SUBSIDIARY AND PARENT CORPORATIONS

The Model Law and Chapter 15 outline the procedures for dealing with cross-border insolvencies. They do not deal with substantive choice-of-law issues concerning which relevant jurisdiction would oversee the insolvency proceedings.<sup>218</sup> They also do not address proceedings involving corporate groups.<sup>219</sup> Large corporations are unlikely to do business directly with foreign nations. Rather, they will do business through subsidiaries incorporated under the local laws of the foreign nation. Therefore, the attitude of the foreign jurisdiction towards the cross-border insolvency of the corporate group will determine the treatment of the bankruptcy.

##### A. *Entity versus Enterprise?*

Within the past century, the concept of the corporation has evolved into a concept of the corporate group, with “dominant” parent corporations owning stock in “subservient” subsidiary corporations.<sup>220</sup> This structure, which has become known as corporate “enterprise” law as opposed to corporate entity law, serves as protection of the parent corporation from the liabilities of its subsidiary.<sup>221</sup> The limited liability available to the parent/subsidiary corporate structure was only infringed, at first, under traditional “piercing the corporate veil” jurisprudence.<sup>222</sup> Recently, as the theory of “enterprise” corporate structures has gained acceptance, courts exercising their equitable powers have looked beyond traditional veil-piercing criteria and into the business of the entire corporate enterprise.<sup>223</sup> Courts applying enterprise principles look to the existence of control of the subsidiary by the parent, operational and economic unity, and whether the objectives of the law in the area are better served by enterprise rather than entity principles.<sup>224</sup>

---

217. *In re Rose*, 318 B.R.771, 776 (Bankr. S.D.N.Y. 2004).

218. Canuel, *supra* note 151, at 24.

219. *Id.*

220. PHILLIP I. BLUMBERG, THE MULTINATIONAL CHALLENGE TO CORPORATION LAW, THE SEARCH FOR A NEW CORPORATE PERSONALITY 58-59 (1993)

221. *Id.* at 59. For a comprehensive summary of Phillip I. Blumberg’s work on the evolution of enterprise theory. See also Hector Jose Miguens, *Liability of a Parent Corporation for the Obligations of an Insolvent Subsidiary Under American Case Law and Argentine Law*, 10 AM. BANKR. INST. L. REV. 217, 218-19 (2002).

222. BLUMBERG, *supra* note 220, at 89.

223. *Id.*

224. *Id.* at 92.

Where the foregoing factors can be shown, the increasing number of common law courts applying enterprise law will do so, notwithstanding the absence of other factors essential for application of traditional “piercing the veil jurisprudence.” Such elements, unnecessary for enterprise law, are the lack of indicia of the separate existence of the subsidiary, including

One area of law that courts have alluded to being better served by enterprise law, as opposed to entity law, is the area of corporate bankruptcy, especially as applied to equitable subordination, voidable preferences, and substantive consolidation.<sup>225</sup> “Although entity continues to prevail elsewhere in [American] bankruptcy law, there are signs of change, particularly in such areas as fraudulent transfers and jurisdiction [of corporate groups].”<sup>226</sup> In general, however, entity law still prevails over enterprise law when considering the bankruptcy of corporate groups, the exception being substantive consolidation.<sup>227</sup> The majority of bankruptcy cases that have imposed liability on a parent corporation for the debts of the subsidiary rely on corporate veil-piercing jurisprudence.<sup>228</sup>

The rise of enterprise law as applied to corporate groups is not limited to the United States. Enterprise theories have been seen within Europe as well. “Throughout the Western world, legal systems are recognizing, in varying degrees, the importance of implementing regulatory programs over corporate groups by proceedings in selected areas on an enterprise basis, rather than by continued reliance on entity law.”<sup>229</sup> Countries may attempt to use “home country extraterritoriality” to extend control over the international subsidiaries of a domestic parent corporation under its jurisdiction.<sup>230</sup> “Such extraterritorial application necessarily means extension of the scope of the home country’s laws to foreign subsidiaries that are subject as well to the laws of the host country under which they are incorporated or have their *siege*.”<sup>231</sup> Nations could also attempt to exercise “host country extraterritoriality” by imposing jurisdiction over the foreign parent of a domestic subsidiary.<sup>232</sup> Chapter 15 uses “foreign main proceedings” in a manner that could be described as “home country,” encouraging host countries to defer to a home country court.<sup>233</sup>

Although not based on U.S. bankruptcy law, there is a U.S. “common law *fiduciary obligation* of the controlling shareholder to creditors arising from the subsidiary’s insolvency,” the obligation being the liability of a parent for the depletion of the insolvent’s estate.<sup>234</sup> This obligation is not unique to U.S. law and is readily seen in foreign jurisdictions. In Argentine law, for example, “the dominant party can be made liable in case of bankruptcy.”<sup>235</sup> Corporate veil-

---

lack of respect for corporate formalities or lack of offices, equipment, employees, and so on; and the presence of inequitable or wrongful conduct detrimental to creditors.

225. *Id.* at 117.

226. *Id.*

227. Miguens, *supra* note 221, at 219. Miguens also highlights the courts’ use of enterprise law in equitable subordination, although that option is beyond the scope of this paper because either: (1) the parent is not bankrupt, or (2) the parent is considered a corporate insider. *Id.* at 224.

228. *Id.* at 220-21, n.7.

229. BLUMBERG, *supra* note 220, at 167.

230. *Id.* at 169.

231. *Id.*

232. *Id.*

233. Reuven S. Avi-Yonah, *National Regulation of Multinational Enterprises: An Essay on Comity, Extraterritoriality, and Harmonization*, 42 COLUM. J. TRANSNAT’L L. 5, 22 (2003).

234. Miguens, *supra* note 221, at 223.

235. *Id.* at 229.

piercing is not necessary. However, this rule considers only the solvent parents of insolvent subsidiaries and not insolvent corporate groups as a whole.

A clear definition of foreign proceedings is also important for the concept of corporate groups. The reorganization of corporate groups, or interior restructuring of the corporate enterprise like that found in *In re Rose*, may or may not be found to constitute a “foreign proceeding” under Chapter 15.<sup>236</sup> Section 304 litigation stressed the amount of judicial supervision, while the new Chapter 15 definition requires readjustment of debt.<sup>237</sup> This question is largely left open when considering the reorganization of the corporate group.

There is also the question of how much control over a subsidiary is needed for a country desiring to apply enterprise theory to actually find “control.” Many multinational corporations are composed of partly-owned subsidiaries, in which the parent corporation may share ownership with a local body or local government. Foreign courts may apply their own form of corporate veil-piercing or a control test to determine whether the parent and subsidiary should be considered a “corporate group” and attempt to exert extraterritorial application to their law regarding enterprise theory.

#### B. *Substantive Consolidation*

Substantive consolidation is the consolidation of assets and liabilities of different legal entities into a single estate to be administered jointly and treated as a single legal entity.<sup>238</sup> Substantive consolidation is not a codified statute in the Bankruptcy Code, and authority to consolidate legal entities comes only from the bankruptcy court’s discretionary equitable powers of section 105(a).<sup>239</sup> Substantive consolidation is not to be confused with procedural consolidation, which involves the administration of “two or more affiliated debtors as part of a single proceeding, without affecting in any way the substantive rights and liabilities of the creditors, the debtors, or the allocation of assets and pro rata satisfaction of claims.”<sup>240</sup> This is done only for administrative convenience and judicial economy.<sup>241</sup> Substantive consolidation, on the other hand, involves a pooling of assets and liabilities.<sup>242</sup> In effect, it also equalizes the position of all unsecured creditors of the consolidated entities.<sup>243</sup>

There is no clearly developed legal standard to guide the courts in deciding when substantive consolidation should be applied.<sup>244</sup> However, “[c]ourts have developed two principal tests for determining whether the estates of two or more

---

236. Phelan & Everett, *supra* note 71, at 44.

237. 11 U.S.C. §101(23).

238. COLLIER, *supra* note 43, ¶ 105.09[1][a].

239. *Id.* ¶ 105.09[1][b], citing 11 U.S.C. §105(a) (2005).

240. BLUMBERG, *supra* note 72, §88.02.

241. *Id.* §83.01.

242. *Id.* §88.02.

243. BLUMBERG, *supra* note 220, at 118.

244. COLLIER, *supra* note 43, ¶ 105.09[2].

related debtors should be substantively consolidated.”<sup>245</sup> First, the traditional elements test is similar to the criteria of corporate veil-piercing.<sup>246</sup> Second, a more recent balancing test looks to whether more creditors would be benefited than prejudiced as a result of substantive consolidation as well as the substantial identity of the entities to be consolidated.<sup>247</sup> Because “[i]t would be unusual for the debtors or other legal entities that are to be consolidated to have the same ratio of assets to liabilities,”<sup>248</sup> unsecured creditors less likely to recover from one entity may benefit from substantive consolidation, while creditors likely to receive a high percentage of recovery on their claims are prejudiced by substantive consolidation.<sup>249</sup>

Substantive consolidation, when not decided under a corporate veil-piercing jurisprudence, gives effect to enterprise theory. It treats the parent and subsidiary corporations as one unit for the purpose of bankruptcy proceedings. “Substantive consolidation vividly illustrates the inherent nature of enterprise principles; they prevail and supersede traditional entity law only when they more effectively achieve the underlying legal objectives in the area.”<sup>250</sup> Like enterprise theory in general, it is used when “the equitable objectives of bankruptcy may supersede the traditional principles of corporate law.”<sup>251</sup>

In the context of multinational corporate groups, questions will arise concerning the substantive consolidation of affiliates located in and falling under the jurisdiction of different nations. The first question under this consideration is whether both or all corporations considered for consolidation must be insolvent. A number of decisions in U.S. bankruptcy courts have permitted consolidation of a debtor corporation with a non-debtor affiliated corporation, but traditionally on the grounds that the corporations lacked separateness or met the criteria of corporate veil-piercing.<sup>252</sup> This result is correct in theory, even without a veil-piercing analysis, in the case of insolvency of the parent because the subsidiary is essentially an asset of the insolvent parent. “Solvency of the subsidiary does not present any hurdle to the institution of voluntary proceedings with respect to the subsidiary and therefore does not present any hurdle to subsequent procedural or substantive consolidation with the proceedings of its insolvent parent.”<sup>253</sup> However, some countries that host a solvent subsidiary, even where the country’s bankruptcy code allows for voluntary proceedings, may not wish to release jurisdiction of the

---

245. *Id.*

246. *Id.* ¶ 105.09[2][a].

247. *Id.* ¶ 105.09[2][b].

248. *Id.* ¶ 105.09[1][a].

249. *Id.*

250. BLUMBERG, *supra* note 72, §91.01[G].

251. *Id.* §83.01.

252. COLLIER, *supra* note 43, ¶ 105.09[1][c]; *see, e.g., In re Augie/Restivo Baking Co., Ltd.*, 860 F.2d 515, 518-21 (2d Cir. 1988); *In re Auto-Train Corp., Inc.*, 810 F.2d 270, 275-78 (D.C. Cir. 1987); *In re New Center Hosp.*, 187 B.R. 560, 566-71 (E.D. Mich. 1995); *In re Meridian Place, N.W., Inc.*, 15 B.R. 89, 96-99 (Bankr. D.C. 1981).

253. BLUMBERG, *supra* note 72, §89.03.

proceedings in a substantive consolidation with a foreign parent corporation under a foreign bankruptcy code.

A second question concerning substantive consolidation is, again, a choice of law question for competing jurisdictions with different substantive law. In *In re Ionica*, joint administrators of an English subsidiary involved in an English insolvency proceeding filed a Chapter 11 plenary proceeding in the United States for the purpose of obtaining either an equitable subordination or substantive consolidation against the solvent parent company.<sup>254</sup> The two courts entered a cross-border protocol to “coordinate and harmonize the plenary proceedings pending in London and New York” that governed which law would be applied to the distribution of relevant assets.<sup>255</sup> The U.S. court chose to defer to the English proceeding by dismissing the entire Chapter 11 proceeding, at the behest of the creditors, under section 304.<sup>256</sup> It was relevant to the court that the debtor had no intention to actually reorganize under Chapter 11, and the debtor’s only connections with the United States were pledged securities held by two American indenture trustees.<sup>257</sup>

Aside from the question of extraterritorial application of an order of substantive consolidation, the general criteria that guide the U.S. courts’ determination of ancillary proceedings to a foreign court are not harmed by substantive consolidation. As stated above, substantive consolidation only affects the standing of unsecured creditors, usually to their benefit. Most litigation over section 304 criteria involved the rights of secured creditors under foreign law, and the protected status of secured creditors is, if anything, enhanced with the protections offered in Chapter 15.<sup>258</sup> Thus, a prevalence in substantive consolidation of cross-border corporations would not injure secured creditors and might actually serve an advantage to unsecured creditors.

### C. *The American Law Institute’s Transnational Insolvency Project*

The American Law Institute (ALI) began the Transnational Insolvency Project in 1997. The Project’s goal was to “develop cooperative procedures for use in business insolvency cases involving companies with assets or creditors in more than one of the three NAFTA countries.”<sup>259</sup> The effort culminated in 2000 with “a set of agreed principles governing multinational bankruptcy cases and . . . useful approaches to managing such cases based on those principles.”<sup>260</sup>

The ALI’s summary of bankruptcy law of the three member NAFTA nations highlights problems of achieving universalism. For example, contrary to U.S.

---

254. *In re Ionica*, 241 B.R. 829, 831 (Bankr. S.D.N.Y. 1999).

255. *Id.* at 835.

256. *Id.* at 838.

257. *Id.* at 834.

258. *See supra* Part III (D)(1).

259. AMERICAN LAW INSTITUTE US, *supra* note 39, at 1.

260. TRANSNATIONAL INSOLVENCY PROJECT: PRINCIPLES OF COOPERATION IN TRANSNATIONAL INSOLVENCY CASES AMONG THE MEMBERS OF THE NORTH AMERICAN FREE TRADE AGREEMENT, 3 (Am. L. Inst. Tentative Draft 2000) (hereinafter AMERICAN LAW INSTITUTE PRINCIPLES).

policy favoring universalism, Mexican bankruptcy law has been comparatively slow in adopting a policy implementing universalism. A foreign bankruptcy judgment will only be enforced in Mexico if the court procedure corresponds with Mexican procedural requirements, although Mexico often attempts extraterritorial enforcement of its own judgments.<sup>261</sup> If a foreign judgment is recognized, the effects will still be governed under Mexican law.<sup>262</sup> Canadian courts, on the other hand, have recognized Chapter 11 proceedings brought in the United States against an entire corporate group that included a solvent Canadian affiliate.<sup>263</sup> However, this is not always the rule, and Canadian courts have alternately denied recognition of U.S. proceedings against Canadian subsidiaries.<sup>264</sup>

The ALI project is unique in that, unlike the Model Law, it highlights the complexities of cross-border insolvencies that involve multi-tiered corporations.<sup>265</sup> “There is relatively little authority dealing with the concept of corporate groups in transnational insolvency, but in the United States, as elsewhere, the corporate form is generally respected.”<sup>266</sup> ALI reports that substantive consolidation is permitted in the United States and Canada only in rare circumstances, and it is never recognized in Mexico.<sup>267</sup> It predicts that substantive consolidation of a United States parent in bankruptcy proceedings and its foreign subsidiary would be rare.<sup>268</sup> However, the Project encourages consolidation of a subsidiary corporation into the bankruptcy proceedings of its parent, at least “absent a proceeding involving the subsidiary in the country of its main interests.”<sup>269</sup> Furthermore, the Project lists as a viable option a subsidiary filing for bankruptcy in the parent’s jurisdiction and seeking recognition of that bankruptcy proceeding in its home country through ancillary jurisdiction.<sup>270</sup> The Project emphasized that consolidation of a parent and subsidiary proceeding is the best way to prevent manipulation of the subsidiary by the parent, as one court could monitor all of the parent’s actions.<sup>271</sup> The Project predicts that U.S. courts would not grant ancillary jurisdiction to a U.S. subsidiary of a foreign parent with its center of operation in the U.S and rather would force the U.S. subsidiary into full U.S. bankruptcy proceedings.<sup>272</sup> It also predicts that U.S. courts would accept jurisdiction of subsidiary bankruptcy in connection with the bankruptcy proceeding of the domestic parent. “Nonetheless, the corporate form

---

261. TRANSNATIONAL INSOLVENCY PROJECT: INTERNATIONAL STATEMENT OF MEXICAN BANKRUPTCY LAW, 112-13 (Am. L. Inst. Tentative Draft 1998).

262. *Id.* at 112.

263. Canuel, *supra* note 151, at 16.

264. *Id.* at 17. Recognition by Canadian courts of U.S. bankruptcy proceedings against Canadian corporations has also been highly criticized. *Id.*

265. BLUMBERG, *supra* note 72, §90.07[B]; Canuel, *supra* note 151, at 25.

266. AMERICAN LAW INSTITUTE US, *supra* note 39, at 131.

267. BLUMBERG, *supra* note 72, §90.07[B].

268. AMERICAN LAW INSTITUTE US, *supra* note 39, at 131.

269. AMERICAN LAW INSTITUTE PRINCIPLES, *supra* note 260, at 109.

270. *Id.* at 111.

271. *Id.* at 114.

272. *Id.* at 112.

will be respected and it may be expected that substantive consolidation between a United States parent and a foreign subsidiary will be extremely rare.”<sup>273</sup>

*D. Treatment of Corporate Group Insolvency by U.S. Courts Before Chapter 15*

Under section 304, the question of treatment of bankruptcy parent and subsidiary corporations fell under the discretion of the bankruptcy judge. Then, it became a question of whether the judge viewed a multi-tiered corporation under the entity theory or the enterprise theory.

In *In re Brierley*, one bankruptcy judge upheld the corporate form of separate parent and subsidiary bankrupt corporations and refused to grant the foreign representative of the parent corporation automatic control of the subsidiary assets. “What Brierly is not entitled to,” the court notes,

is injunctive relief with respect to suits against subsidiaries and their property. He attempts to blur the distinction between a claim against a subsidiary (as well as entitlement to the surplus in an estate after its liquidation) and a claim to specific property. It is well settled in this circuit that ownership of all the outstanding stock of a corporation is not the equivalent of ownership of the subsidiary's property or assets.<sup>274</sup>

In the next breath, however, the judge acknowledged that the foreign representative would have power over the subsidiary, as a corporate asset, should the creditors attempt to take action against the subsidiary.

Were a creditor trying to seize the stock of a subsidiary, injunctive relief might be appropriate, since the stock is plainly [the parent]'s property. Similarly, were a creditor of a subsidiary embarking on some action which substantially threatened the ability of [the parent] to sell stock of the subsidiary, an injunction might be appropriate. But a blanket injunction preventing suit against all of [the parent]'s subsidiaries, direct and indirect, is not proper.<sup>275</sup>

Thus, the court refused to give direct control of a subsidiary to a foreign representative during bankruptcy proceedings unless a creditor attempted to take control of the subsidiary. At that point, however, respect for the corporate form would diminish to the need to grant the foreign representative control over the bankrupt estate's assets.

When a creditor of a parent corporation did attempt to take the assets of a subsidiary corporation, one court granted section 304 relief. With *In re Schimmelpenninck*, a Dutch parent corporation filed for liquidation in the

---

273. BLUMBERG, *supra* note 72, §90.07[B].

274. *In re Brierley*, 145 B.R. 151, 169 (Bankr. S.D.N.Y. 1992).

275. *Id.*

Netherlands.<sup>276</sup> A creditor attempted to reverse-pierce the corporate veil to reach the assets of a wholly-owned and solvent U.S. subsidiary for repayment of the debt.<sup>277</sup> The debtor in turn filed a section 304 petition requesting the court to enjoin the lawsuit for the preservation of the estate's assets. The court granted the petition under Section 304 analysis, asserting that the subsidiary constituted property "involved in" the foreign proceedings.<sup>278</sup>

The Second Circuit ultimately denied section 304 protection to a foreign debtor's subsidiary assets in *In re Treco*.<sup>279</sup> Although the court denied the section 304 petition because of the secured creditor's subordinate status to the bankruptcy administration costs in the Bahamian bankruptcy proceedings, the assets sought after by the U.S. creditor included the funds of the bankrupt corporation's subsidiary.<sup>280</sup> Unlike *Schimmelpenninck*, however, the debtor had pledged the assets of the subsidiary to the secured creditor.<sup>281</sup>

Despite the lack of guidance concerning plenary cases in multiple jurisdictions in the prior bankruptcy law, a clear precedent had been set for coordination and cooperation between the U.S and foreign court proceedings that grants deference to the substantive law of nation with the most interest in the debtor corporation.<sup>282</sup> A clear example of cooperating plenary bankruptcy proceedings is found with *In re Maxwell Communication Corp*, which involved an English holding company that filed for Chapter 11 in the United States and reorganization proceedings in England.<sup>283</sup> When it became evident that one creditor could be subject to a preference action under U.S. law but not under laws of the United Kingdom, the English court gave jurisdiction of the preference issue to the U.S. bankruptcy court.<sup>284</sup> All parties agreed that the use of U.S. preference law in this case would be extraterritorial.<sup>285</sup> After a long discussion, the court ruled that U.S. preference law should not apply to a foreign debtor when "the center of gravity of that transfer is overseas."<sup>286</sup> Rather, the court held that "the law of the jurisdiction having the greatest interest in the controversy" should apply.<sup>287</sup> While acknowledging that, "in an age of multinational corporations, it may be that two (or more) countries have equal claim to be the 'home country' of the debtor,"<sup>288</sup> the court decided that

---

276. *In re Schimmelpenninck*, 183 F.3d 347, 347 (5th Cir. 1999).

277. *Id.* at 350.

278. *Id.* at 361-62.

279. *In re Treco*, 240 F.3d 148, 152 (2d Cir. 2001).

280. *Id.* at 152.

281. *Id.* at 156. The case was ultimately remanded for a determination of whether the creditor's claim was secured. *Id.* at 163.

282. *In re Maxwell Comm. Corp.*, 170 B.R. 800, 818 (Bankr. S.D.N.Y. 1994).

283. *Id.* at 802.

284. *Id.* at 804-05. The repayment money the banks obtained from MCC were from the proceeds of U.S. assets. *Id.* at 804.

285. *Id.* at 809.

286. *Id.* at 814.

287. *Id.* at 816.

288. *Id.* at 817.

England had the greatest interest in the outcome of the proceedings, and in this case English preference law should apply.<sup>289</sup>

The *Maxwell* rule, looking to the country with the greatest interest in the bankruptcy proceedings, was adopted by the Third Circuit in *Stonington Partners, Inc. v. Lernout & Hauspie Speech Product N.V.* for both the propositions that the court should determine which substantive law of the two jurisdictions would apply based on interests as well as the encouragement of an open dialogue between the two plenary jurisdictions.<sup>290</sup> Prior to the implementation of Chapter 15 in the United States, U.S. courts involved in plenary bankruptcy cases with Canada also compromised on differing substantive law and cooperated with decisions involving corporate groups of affiliates in both countries.<sup>291</sup>

#### *E. Treatment of Multi-tiered Corporate Bankruptcy Under Chapter 15*

Chapter 15 takes steps to amend the complex issues surrounding multi-tiered corporations in bankruptcy proceedings. In section 1515, “[a] petition for recognition shall also be accompanied by a statement identifying all foreign proceedings with respect to the debtor that are known to the foreign representative.”<sup>292</sup> This statement may be interpreted to include all bankruptcy proceedings of subsidiary corporations, spread throughout the world, for a bankrupt parent applying for relief under Chapter 15. Perhaps a more controversial question is whether a subsidiary corporation applying for recognition or relief under Chapter 15 must report the bankruptcy proceedings of the corporation’s sister subsidiaries. Whether a sister or even parent corporation would be considered to be “with respect to the debtor” depends on whether the examiner views corporate organization under the entity or enterprise theory.<sup>293</sup> Creditors would likely find reporting of parent and sister subsidiary proceedings usefully for possible veil-piercing or equitable subordination claims.

Procedural consolidation may be attempted under Chapter 15, at least to the efforts of cooperation and coordination between parallel proceedings and ancillary proceedings in multiple foreign jurisdictions. Section 1527 extends the form of cooperation to include concurrent proceedings of the debtor,<sup>294</sup> while section 1530 requests coordination with related foreign proceedings, whether they be main or non-main proceedings.<sup>295</sup> Under these statutes, and in the policy of “coordination” reiterated throughout all of Chapter 15, a strong argument may be made towards the procedural consolidation of parent and subsidiary corporations into one main

---

289. *Id.* at 818.

290. *Stonington Partners, Inc. v. Lernout & Hauspie Speech Prod. N.V.*, 310 F.3d 118, 131-33 (3d Cir. 2002). The case was remanded to bankruptcy court for a more thorough consideration of the substantive law and policies at play in the two competing jurisdictions. *Id.* at 133.

291. Canuel, *supra* note 151, at 21-22 (discussing the Olympia and York cross-border insolvency of the 1900’s).

292. 11 U.S.C. §1515(c).

293. *Id.*

294. 11 U.S.C. §1527(5).

295. 11 U.S.C. §1530.

bankruptcy proceeding. This argument is ever stronger if the facts at hand indicate an overall disregard of corporate form towards the security held by secured creditors.<sup>296</sup>

#### F. Possible Solutions

Some commentators have argued that inconvenience to a U.S. creditor should not be the basis to deny ancillary jurisdiction because, “creditors presumably know of the potential for bankruptcy and its attendant complications when they decide to do business with foreign companies.”<sup>297</sup> This simplistic view overlooks the complexities of corporate groups. If substantive consolidation across national borders is attempted, creditors may find themselves in a much larger proceeding than originally foreseen. As long as substantive law differs across jurisdictional lines, there will continually be an incongruence between the treatment of insolvent corporate groups.

The adjudication of certain “criteria” before granting ancillary relief or substantive consolidation, as was present in section 304 and continues with section 1507 of Chapter 15, will necessitate a comparison of substantive law that all too often is simply irreconcilable. Universal consolidation of parent and subsidiary corporate groups would be a sensible option to the question of corporation group bankruptcy. In theory, the subsidiary would be an asset of the parent corporation during the parent corporation’s proceedings and, by necessity, would be dealt with as part of the parent’s bankruptcy estate. Secured creditors would not be harmed, and unsecured creditors might be better off. On the other hand, Robert K. Rasmussen argues that a territoriality approach might be a better way to handle multiple multinational subsidiaries of a bankrupt corporate structure.<sup>298</sup> “This global segmentation,” writes Rasmussen,

provides each country with a discrete firm to focus on. On the one hand, there may be firms that experience financial, but not economic, distress, and whose constituent parts are so well integrated that any successful reorganization will need the active cooperation of all countries in which the firm has an affiliate. On the other hand, some firms may yield a higher return when administered on a territorial basis.<sup>299</sup>

The basic criticism of territorialism rests on the presumption that a country will favor its domestic creditors over foreign creditors.<sup>300</sup> Because most modern countries already have bankruptcy laws that prevent the parceling out of a debtor’s assets to the first petitioning unsecured creditor, which is the universalists’ fear

---

296. See, e.g. 11 U.S.C. §1522.

297. Kraft & Aranson, *supra* note 5, at 350.

298. Rasmussen, *supra* note 18, at 2259.

299. *Id.*

300. Robert K. Rasmussen, *A New Approach to Transnational Insolvencies*, 19 MICH. J. INT’L L. 1, 29 (1997).

concerning the territoriality approach, the efficiency of universalism is greatly trivialized.<sup>301</sup> “By disrupting the harmony that would otherwise exist between bankruptcy and corporate law, universalism threatens the system of laws that nations have developed to police firm performance.”<sup>302</sup> The crux of Rasmussen’s argument is that corporate groups should be allowed to decide for themselves whether they would prefer the universal or territorial approach to any possible bankruptcy proceedings of their subsidiary corporations.<sup>303</sup>

Treaties would be an easy way to adopt substantive law that would control when corporate groups would be consolidated across national borders and which substantive law would apply to cross-border insolvencies. Such a treaty, between two or more nations whose bankruptcy laws are essentially in harmony, could grant jurisdiction of subsidiary corporations to the domicile nation of the parent. This option would give firm guidance to creditors, who would have fair warning as to when a subsidiary could be consolidated with the bankruptcy proceedings of a parent in a foreign jurisdiction. However, the United States is not a party to any international insolvency treaty.<sup>304</sup>

#### CONCLUSION

Despite a United States Supreme Court case that granted comity only in the presence of reciprocity, the United States has a long tradition of granting comity to foreign bankruptcy proceedings involving assets located in the United States. This tradition of comity was codified in Title 11 of the United States Code, section 304, which granted ancillary jurisdiction to foreign proceedings. However, the relief depended upon the foreign proceedings meeting six statutory criteria that required a comparison of substantive law between the United States and the competing jurisdiction. Case law routinely confirmed that when secured creditors would be placed at a disadvantage in the foreign proceedings, ancillary jurisdiction would not be granted. The definition of “foreign proceedings” was also debated, usually necessitating both a high level of court supervision and creditor voice in the proceedings before ancillary jurisdiction would be granted the foreign proceedings. The recent case of *In re Rose*, however, held that a corporate restructuring would not be considered reorganization for Section 304 purposes.

This past year, Congress adopted the Model Law on Cross-Border Insolvency into the new Chapter 15 of the U.S. Bankruptcy Code. Chapter 15 calls for cooperation and coordination of proceedings in multiple jurisdictions involving the same debtor, as well as near-automatic recognition of petitions for ancillary proceedings. The statutory criteria from section 304 are still present but are only

---

301. *Id.* at 31-32.

302. Rasmussen, *supra* note 18, at 2260.

303. *Id.*

304. COLLIER, *supra* note 43, ¶ 304.08[5][a]. *See also* Canuel, *supra* note 149, at 29:

The lone attempt at codifying a definitive approach to contending with U.S.-Canadian cross-border insolvencies, the unratified United States of America-Canada Bankruptcy Treaty of 1979, failed as it was viewed as a threat to sovereignty by mandating a single proceeding in one venue and the application of one jurisdiction’s law in a foreign court.

considered if “additional assistance” is requested. Creditor’s rights are still highly-protected. A new definition of “foreign proceedings” states that the proceedings in the foreign jurisdiction must related to insolvency or adjustment of debt, although it still leaves in question which types of corporate restructuring would be considered financial reorganization.

Chapter 15, however, does not address the substantive issues of cross-border insolvencies of multinational corporation groups. The American Law Institute’s Transnational Insolvency Project recommends that the proceedings of subsidiaries should be substantively consolidated into the proceedings of the insolvent parent corporations. This solution, while in theory protecting secured creditors and bettering the position of all unsecured creditors of the corporate group, does not address the desire for sovereignty from the multiple jurisdictions that might be affected by the insolvency of a corporate group. The limited case law in the United States has respected the corporate form of separate parent and subsidiary insolvency proceedings unless and until debtors of the parent corporation attempt to reach the assets of the subsidiary. The case law also indicates a precedent of coordinated plenary proceedings with foreign jurisdictions and a determination of applicable substantive law by the country with the most interest in the proceedings. Although this common law is essentially codified into the new Chapter 15, it demonstrates a willingness to release jurisdiction of corporate bankruptcy to a foreign jurisdiction when appropriate.