

INTERNATIONAL BANKRUPTCY: LIMITED RECOGNITION IN THE NEW U.S. BANKRUPTCY CODE

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I. INTRODUCTION

While it is common to think of bankruptcy as a legal institution in which an insolvent debtor's assets are collected and distributed to creditors,¹ it is equally common to view bankruptcy as only a local phenomenon. This is because of the traditional *in rem* or property-related nature of bankruptcy,² and because truly international insolvencies have always been relatively rare.³ Nevertheless, events of the last quarter century have proved the old notion of bankruptcy to be too narrow. Today the bankrupt's⁴ assets are often found in more than one country.⁵ banks and other organizations engage in far-flung business trans-

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1. This is the usual definition of bankruptcy, but it actually describes the process of "liquidation." Many bankruptcy laws, including that of the United States, allow the bankrupt to work out a plan to repay creditors under the protection of the court. Such rehabilitation or reorganization provisions usually allow the bankrupt to keep his assets and to attempt to regain financial stability. In the U.S. Bankruptcy Code liquidation is governed by Chapter 7, and reorganization by Chapters 11 and 13. See 11 U.S.C. §§ 701-766, 1101-1174 and 1301-1330 (Supp. IV 1980).

2. In common law countries bankruptcy is usually considered to be in the nature of a judgment *in rem*, with the *res* being the estate and the status of the bankrupt debtor. The orders of the bankruptcy court concerning the debtor are in principle considered binding on all the world as to determination of insolvency, powers of management, disposition of assets, and distribution of the dividend to creditors. On the other hand, there is an *in personam* aspect to bankruptcy in that creditors not party to the proceedings are not otherwise considered to be bound by the legal consequences of the bankruptcy. In some common law countries such as the United States, bankruptcy may also be considered *quasi in rem* in that jurisdiction over the debtor may be based solely on the location of assets within the court's territorial limits. J. DALHUISEN, 1 DALHUISEN ON INTERNATIONAL INSOLVENCY AND BANKRUPTCY 3-102, 3-147 (1980) [hereinafter cited as DALHUISEN]; Nadelmann, *National Bankruptcy Act and the Conflict of Laws*, 59 HARV. L. REV. 1025, 1040 (1946) [hereinafter cited as Nadelmann, *National Bankruptcy Act*]. See *infra* notes 9 and 31.

3. For an excellent history of the development of the bankruptcy laws in different countries, see generally DALHUISEN, *supra* note 2, at 1-1 to 1-109.

4. While the party who invokes (voluntarily or otherwise) the bankruptcy laws of his country has traditionally been known as a "bankrupt," the new U.S. Bankruptcy Code uses the term "debtor." Here the terms "bankrupt" and "debtor" will be used interchangeably. See 11 U.S.C. § 101(12) (Supp. IV 1980).

5. Actually, the problem is older than one might think. Records show that the Amanati Bank, an Italian bank with branches all over Europe, became insolvent in 1302. The bank's depositors—many of whom were members of the clergy—were forced to seek the

actions, while many corporations are multinational. Their assets are globally dispersed because our international economy demands it.

Developments in international law rarely keep pace with developments in international commerce. Nowhere is this more apparent than in the body of law devoted to international bankruptcy. Unchanged for many years, it has been governed by treaties when available,⁶ by each country's rules of conflict of laws,⁷ and by national bankruptcy laws.⁸ Since bankruptcy laws derive their authority from the sovereignty of each nation, a country's bankruptcy laws have no inherent effect outside its own borders.⁹ Extraterritorial enforcement of bank-

help of the Pope to collect the bank's widely-dispersed assets. Nadelmann, *Bankruptcy Treaties*, 93 U. PA. L. REV. 58, 58 (1944), reprinted in K. NADELMANN, CONFLICT OF LAWS: INTERNATIONAL AND INTERSTATE 299, 299 (1972) [hereinafter cited as NADELMANN, CONFLICT OF LAWS]. See generally DALHUISEN, *supra* note 2, at 3-120 to 3-122.

6. See DALHUISEN, *supra* note 2, at 3-23 to 3-31, 3-42 to 3-44.2, 3-57, 3-82 to 3-92, 3-160 to 3-163. Volume 2 of the Dalhuisen treatise is an appendix with the full text of most of the treaties applicable to bankruptcy, insolvency and recognition of foreign judgments. See DALHUISEN, *supra* note 2, vol. 2. See also Nadelmann, *Bankruptcy Treaties*, 93 U. PA. L. REV. 58 (1944).

7. See generally DALHUISEN, *supra* note 2, at 3-407 to 3-411; Nadelmann, *Codification of Conflicts Rules for Bankruptcy*, in [1974] ANNUAIRE SUISSE DE DROIT INTERNATIONAL 57 (1975) [hereinafter cited as Nadelmann, *Codification*], reprinted in *Hearings on H.R. 31 and H.R. 32 Before the Subcomm. on Civil and Constitutional Rights of the House Comm. on the Judiciary*, 94th Cong., 2d Sess., 1457 (1976) [hereinafter cited as *Hearings on H.R. 31*]; Nadelmann, *National Bankruptcy Act*, *supra* note 2.

8. See generally DALHUISEN, *supra* note 2, at 3-3 to 3-263.

9. International bankruptcy has always been explained by one of two conflicting theories: universality and territoriality. The universality theory holds that a local bankruptcy adjudication has full effect everywhere in the world. The local court would usually, but not necessarily, be at the debtor's domicile. Proceedings under the universality doctrine have the advantage of speed and efficiency, while promoting an equitable distribution of the debtor's estate and adequately protecting the debtor. A related principle, that of "unity of bankruptcy," holds that the debtor's domicile is the only possible place for bankruptcy proceedings; no other court would have jurisdiction. The property of the debtor's estate, wherever located, is deemed to be situated at the domicile and thus governed by the domiciliary proceedings. Territoriality, on the other hand, dictates that a bankruptcy adjudication has no inherent effect outside the country of bankruptcy. This theory derives, of course, from familiar principles of national sovereignty.

These theories are only conceptual tools, and as a practical matter, no country follows either theory exclusively. What prevails instead is a blend of both doctrines, with one theory or the other being dominant, depending on the degree of that country's protectionist tendencies. Universality in its purest form is rare because to be effective it requires universal cooperation. And in countries subscribing to the territoriality theory, a foreign bankruptcy adjudication, while not given automatic effect locally, may be "domesticated" through local court proceedings. G. CHESHIRE & P. NORTH, CHESHIRE'S PRIVATE INTERNATIONAL LAW 562-63 (9th ed. 1974) [hereinafter cited as CHESHIRE & NORTH]; DALHUISEN, *supra* note 2, 3-182 to 3-191; A. DICEY & J. MORRIS, THE CONFLICT OF LAWS 676 (9th ed. 1973) [hereinafter cited as DICEY & MORRIS]. One of the earliest arguments for holding bankruptcy proceedings at the debtor's domicile can be found at F. SAVIGNY, A TREATISE ON THE CONFLICT OF LAWS 260-63 (W. Guthrie trans. 1869) (2d ed. 1880). For a discussion of countries following the territoriality theory, see Nadelmann, *Discrimination in Foreign Bankruptcy Laws Against Non-Domestic Creditors*, 47 AM. BANKR. L.J. 147, 150-53 (1973); Nadelmann, *Concurrent Bankruptcies and Creditor Equality in the Americas*, 22 REF. J. 51, 53-55 (1948); Nadelmann, *Legal Treatment of Foreign and Domestic Creditors*, 11 L. & CONTEMP. PROB. 696, 701-06 (1946).

ruptcy judgments is thus unpredictable in the absence of treaties. But conflicting national interests have made bankruptcy treaties rare, and preferences for local creditors all too common.¹⁰ Thus, while the traditional goal of bankruptcy has been to ensure equal distribution of the bankrupt's assets to creditors,¹¹ the international legal system seems unsuited to the task when those assets are widely dispersed.¹²

While the need for reform is obvious,¹³ the way to achieve it is not. Reform at the international level, by treaty or other arrangement, is difficult because of the differences in national law. For example, the Benelux countries signed a multilateral recognition convention in 1961, but it was never ratified.¹⁴ The European Economic Community has labored for years to produce its draft convention on harmonization of bankruptcy laws, but the resulting convention has yet to be adopted.¹⁵ Canada and the United States, neighbors with strong cultural and economic ties, have similar bankruptcy laws, but have yet to negotiate a

10. DALHUISEN, *supra* note 2, at 3-8 to 3-10, 3-407; Nadelmann, *Codification, supra* note 7, at 59.

11. "The property of a debtor is a pledge in common for his creditors and the value of it is distributed among them proportionately, unless there are among the creditors legitimate causes of preference." FRENCH CIVIL CODE art. 2093 *as amended* July 1976. But note that if rehabilitation of the debtor is contemplated, the goal would be to preserve the debtor's assets for future use rather than to liquidate them.

12. See DALHUISEN, *supra* note 2, at 3-407.

13. See the comments by the Swiss Federal Tribunal in the Israel-British Bank (London), Ltd. bankruptcy case. Judgment of March 12, 1976, Bundesgericht, 102 BG III 71, reprinted in *Hearings on S. 2266 and H.R. 8200 Before the Subcomm. on Improvements in Judicial Machinery of the Senate Comm. on the Judiciary*, 95th Cong., 1st Sess., 1071-74 (1977) [hereinafter cited as *Hearings on S. 2266*].

14. DALHUISEN, *supra* note 2, at 3-27.

15. As part of its continuing efforts to harmonize the substantive law of the member nations, the European Economic Community in 1963 began work on a draft bankruptcy convention. A preliminary draft was published in 1968, and a revised version in 1970, but the admission to the E.E.C. of several new members slowed the process while these countries studied the convention and proposed changes. The British study done by the "Cork Committee" contains a detailed analysis of the convention and an English translation of the text. THE E.E.C. PRELIMINARY DRAFT CONVENTION ON BANKRUPTCY, WINDING UP, ARRANGEMENTS, COMPOSITIONS, AND SIMILAR PROCEEDINGS, REPORT OF THE ADVISORY COMMITTEE, CMND. No. 6602 (Aug. 1976). Recently, a revised draft convention was issued and is still under consideration by the member states of the E.E.C. Commission of the European Communities Internal Market, Approximation of Laws, III/D/72/80. Document, [U.K.] Department of Trade, E.E.C. Draft Bankruptcy Convention, April 1980. See generally DALHUISEN, *supra* note 2, at 3-163 n.123; Farrar, *The E.E.C. Draft Convention on Bankruptcy and Winding Up: A Progress Report and Evaluation*, 1977 J. BUS. L. 320; Farrar, *The E.E.C. Draft Convention on Bankruptcy*, 1972 J. BUS. L. 256; Hillmon, *An American Lawyer Looks at the Common Market Bankruptcy Convention*, 48 AM. BANKR. L.J. 369 (1974); Hunter, *The Draft E.E.C. Convention—A Further Examination*, 25 INT'L & COMP. L.Q. 310 (1976); Hunter, *The Draft Bankruptcy Convention of the European Economic Community*, 21 INT'L & COMP. L.Q. 682 (1972); Nadelmann, *Rehabilitating International Bankruptcy Law: Lessons Taught by Herstatt and Company*, 52 N.Y.U. L. REV. 1, 27-32 (1977) [hereinafter cited as Nadelmann, *Rehabilitating*]; K. NADELMANN, *The Common Market Bankruptcy Convention Draft: Foreign Assets and Related Problems*, in CONFLICT OF LAWS, *supra* note 5, at 340. For citations to sources in languages other than English, see DALHUISEN, *supra* note 2, at 3-163 n.123.

treaty on recognition of bankruptcy judgments.¹⁶

But a significant improvement in international cooperation is sometimes made possible by only a small change in local law. Thus the enactment of the new Bankruptcy Code by the United States is cause for some optimism.¹⁷ Several little-noticed provisions¹⁸ streamline considerably the procedures by which a foreign court of bankruptcy¹⁹ collects assets in the United States.²⁰ The U.S. Bankruptcy Code is now one of the few national bankruptcy laws in the world to deal directly with the effect of foreign bankruptcies, and specifically with the recognition to be given to the representative of a foreign bankruptcy court.²¹

The most important provisions, sections 304²² and 305,²³ help the foreign court in several ways. For the first time the representative of a foreign court²⁴ liquidating or reorganizing the debtor's estate is expressly authorized to appear on behalf of the estate in a U.S. bankruptcy court. If the foreign court is liquidating the estate, the court's representative can seek relief under the provisions in section 304 that empower the U.S. bankruptcy court to enjoin creditor action against the debtor's U.S. property, and to turn those assets over to the foreign court for administration abroad.²⁵

If the estate is undergoing reorganization abroad, the foreign representative will benefit not only from relief under section 304, but also from the court's abstention power in section 305. This section allows the U.S. bankruptcy court to dismiss or suspend its proceedings when

16. See generally Busler, *Bankruptcy Reciprocity: A Study as to a Treaty with Canada*, 33 A.B.A. J. 1026 (1947), reprinted in 22 REF. J. 57 (1948); Honsberger, *Bankruptcy Administration in the United States and Canada*, 63 CALIF. L. REV. 1515 (1975); Honsberger, *The Need for a Rapprochement of the Bankruptcy Systems of Canada and the United States*, 18 MCGILL L.J. 147 (1972), reprinted in 47 AM. BANKR. L.J. 275 (1973).

17. Bankruptcy Reform Act of 1978, 11 U.S.C. § 101 (Supp. IV 1980). The old bankruptcy law was called the *Bankruptcy Act*; the new law is known as the *Bankruptcy Code*. An excellent bibliography of sources on the Bankruptcy Reform Act is Miller, *Bankruptcy Reform Act Bibliography*, 85 COM. L.J. 373 (1980).

18. 11 U.S.C. §§ 304-306 (Supp. IV 1980).

19. The law is actually not limited to foreign courts applying their bankruptcy law. It is sufficient that the proceedings be for the purpose of liquidation, reorganization, or discharge. 11 U.S.C. § 101(19) (Supp. IV 1980). See *infra* note 76.

20. The issue of jurisdiction by the bankruptcy courts in the United States is discussed at text accompanying notes 61-62 *infra*.

21. DALHUISEN, *supra* note 2, at 3-124.

22. 11 U.S.C. § 304 (Supp. IV 1980).

23. *Id.* § 305.

24. Although the term is somewhat awkward, the administrator appointed by the foreign court to liquidate or reorganize the debtor's estate will be referred to as a "foreign representative" because this is the term used in the Bankruptcy Code. See *id.* § 101(20); see *infra* note 75. Such an administrator is better known as a "trustee" or "receiver."

25. See 11 U.S.C. § 304 (Supp. IV 1980).

there is a pending foreign proceeding involving the debtor.²⁶ This can buy valuable time if the debtor is attempting to work out a plan of arrangement with creditors in the foreign proceedings. The new statute will interest not only practitioners of international law, but also U.S. bankruptcy lawyers, since the law can affect the rights of local creditors to the U.S. property of a debtor in bankruptcy abroad.

II. THE AMERICAN POLICY²⁷

In the past, the United States portion of an international bankruptcy²⁸ was handled by the state courts because of their jurisdiction over the bankrupt's local assets.²⁹ Subject to some qualifications, these courts recognized as a matter of comity the rights of a foreign representative to the bankrupt's local assets.³⁰ The policy was derived from the principle that the foreign bankruptcy judgment constituted an assignment by the bankrupt of his property to the foreign court or its representative, whose rights to the bankrupt's American property derived

26. See *id.* § 305.

27. For convenience, American will refer to residents of the United States, not the continent.

28. Although an "international" bankruptcy can also be a case involving a U.S. domiciliary with assets in other countries, the focus of this article will be on the opposite situation; *i.e.*, a foreign domiciliary in bankruptcy abroad who has assets or a place of business in the United States.

29. The supremacy of this jurisdiction was confirmed when the United States Supreme Court held that no federal question was involved if a state court refused to recognize a foreign transfer (through a foreign bankruptcy judgment) of property located within the state's borders. *Disconto Gesellschaft v. Umbreit*, 208 U.S. 570, 582 (1907). See also *Blake v. McClung*, 172 U.S. 239 (1898).

30. The leading English case was *Solomons v. Ross*, 1 H. Bl. 131, 126 Eng. Rep. 79 (Ch. 1764). See generally *Nadelmann, Solomons v. Ross and International Bankruptcy Law*, 9 MOD. L. REV. 154 (1946), reprinted in NADELMANN, *CONFLICT OF LAWS*, *supra* note 5, at 273. The case held that a foreign representative's right to the foreign bankrupt's local assets would be recognized in England even if a local creditor had previously levied an attachment on the assets.

The English rule was modified in 1910 when the House of Lords ruled that a foreign representative was not entitled to collect the bankrupt's local assets if a local creditor had levied on the assets prior to the foreign bankruptcy judgment. *Galbraith v. Grimshaw*, [1910] A.C. 508.

With one exception, *Holmes v. Remsen*, 4 Johns. Ch. 460 (N.Y. 1820), courts in the United States never accepted the English rule in *Solomons*. See *Harrison v. Sterry*, 9 U.S. (5 Cranch) 289 (1809); *Ogden v. Saunders*, 25 U.S. (12 Wheat.) 213 (1827); *Taylor v. Geary*, Kirby 313 (Conn. 1787); *Blake v. Williams*, 23 Mass. (6 Pick.) 285 (1828); *Saunders v. Williams*, 5 N.H. 213 (1830); *Milne v. Moreton*, 6 Binn. 353 (Pa. 1814).

The American courts recognized the foreign representative's rights to the extent that the rights of local creditors were not impaired. The foreign representative could sue under color of title in state court to collect the assets, *In re Waite*, 99 N.Y. 433, 2 N.E. 440 (1885), but the courts would enforce any attachments by local creditors, regardless of whether the attachments were levied before or after the foreign bankruptcy judgment. The policy formulated by the courts in the United States was stated as early as 1834 by Justice John Story in his *Commentaries on the Conflict of Laws*. J. STORY, *COMMENTARIES ON THE CONFLICT OF LAWS* §§ 403-21 (Boston 1834) [hereinafter cited as STORY]. He referred to this policy as the "American Doctrine." *Id.* at §§ 410, 418.

from this assignment.³¹ When the American courts recognized the foreign assignment, the foreign representative could sue under color of title to collect the bankrupt's local assets.³²

This policy was subject to several exceptions. The notion of comity implied some sort of reciprocity, so that American courts would not recognize the rights of the foreign representative if the foreign court discriminated against American creditors.³³ Also, in keeping with the traditional rules of conflict of laws the assignment was considered to extend only to personal property located in the United States, and

31. Describing bankruptcy as an assignment can be misleading because bankruptcy is conceptually more complicated than that. Bankruptcy also has the characteristics of a judgment: it is a judicial procedure involving judicial decrees. The proceedings determine the rights of parties and establish the relationships between them. A bankruptcy judgment would include a court finding of the debtor's insolvency and an order for the collection and distribution of the debtor's assets to creditors. The judgment theory of bankruptcy seems to be prevalent in France and some other civil law countries.

But the judgment approach fails to consider the traditional purpose of bankruptcy (liquidation), which is to liquidate the debtor's estate and distribute it equitably to creditors. This aspect of the bankruptcy process is more in the nature of an execution or enforcement device, rather than a judgment or decree. Thus bankruptcy is often characterized as a creditors' remedy, such as attachment or garnishment proceedings. The creditors' remedy approach is popular in West Germany.

The assignment theory shows a third aspect of bankruptcy: that the bankruptcy decree acts as a statutory assignment of the debtor's property to the court for the benefit of creditors. This approach is the prevailing one in the common law countries, such as the United States and Great Britain. DALHUISEN, *supra* note 2, at 3-100 to 3-118.

To many, this discussion may seem largely academic because the judgment, creditors' remedy, and assignment theories are merely different aspects of the same complex legal process. But the theory of bankruptcy is important to the issue of international recognition of foreign bankruptcy adjudications. Countries following the judgment theory usually require a foreign bankruptcy adjudication to be "domesticated" through local court proceedings before there can be an execution of the debtor's local property. *Id.* at 3-100. The French *exequatur* proceeding is an example of this.

Few countries recognize the extraterritorial effect of another country's execution or enforcement procedures. For this reason, countries adhering to the creditors' remedy approach, such as West Germany and the Netherlands, make local recognition and execution of foreign bankruptcy adjudications very difficult. *Id.* at 3-106 to 3-115.

The assignment theory offers the most potential for international recognition. Under this theory, the representative of the court acquires rights of title in the debtor's property by virtue of the assignment. It is sometimes easier to have these ownership rights recognized locally, and to execute on them, than to follow the procedures for domestication and execution of foreign judgments. *Id.* at 3-115 to 3-118. The easy recognition of foreign bankruptcies possible in countries following the assignment theory can be seen in the case law of the United States and Great Britain. See *supra* note 30 and accompanying text. It is also apparent in the international provisions of the new U.S. Bankruptcy Code, although relief under these provisions is discretionary with the court.

32. It is important to note that under the American policy the foreign bankruptcy was recognized only as a matter of national comity, not international law. This made possible the restrictions designed to protect local creditors. But what is significant about the American policy is not its restrictions, but rather that the foreign representative's standing to collect local assets has always been recognized in principle. This liberal philosophy was inherited from English law and is traceable to the assignment theory of bankruptcy followed in most common law countries. See *supra* note 31. It is in marked contrast to the nonrecognition policies of many countries. See generally Nadelmann articles *supra* note 9.

33. DALHUISEN, *supra* note 2, at 3-145 to 3-146; STORY, *supra* note 30, at § 414.

never to real property.³⁴ The American court also would not recognize the foreign bankruptcy assignment if the foreign court did not have proper jurisdiction over the bankrupt.³⁵ Even if the foreign court had jurisdiction over the bankrupt, the American court would not recognize the rights of the foreign representative if American creditors had levied attachments on the local assets. Inherent in the principle of comity was the obligation to protect the interests of U.S. citizens. Thus, the courts would always enforce the attachments, making it irrelevant whether they were levied before or after the foreign bankruptcy judgment.

After 1898 it became possible to use the bankruptcy laws to void attachments by local creditors, although the foreign representative had no standing to begin a bankruptcy case.³⁶ This step was usually taken by other creditors in the United States to prevent the attaching creditors from taking a disproportionate share of the bankrupt's local assets.³⁷ In the few reported cases in which a federal court was forced to decide a dispute over the local property of a foreign bankrupt, the courts were influenced by the same principles followed by the state courts.³⁸ This dependence on the common law, some of which pre-

34. *Maconchy v. Delehanty*, 11 Ariz. 366, *rev'd sub. nom. In re Delehanty's Estate*, 95 P. 109 (1908).

35. DALHUISEN, *supra* note 2, at 3-146 to 3-147; STORY, *supra* note 30, at § 586.

36. Although the Constitution gave Congress the right to make bankruptcy laws for the nation, U.S. CONST. art. I, § 8, cl. 4, bankruptcy was not popular, and for most of the Nineteenth Century there was no federal bankruptcy law. But federal bankruptcy laws were in effect 1800-1803, 1841-1843, and 1867-1878. *See* Bankruptcy Act of 1800, 2 Stat. 19 (1800) (repealed 2 Stat. 248 (1803)); Bankruptcy Act of 1841, 5 Stat. 440 (1841) (repealed 5 Stat. 614 (1843)); Bankruptcy Act of 1867, 14 Stat. 517 (1867) (repealed 20 Stat. 99 (1878)). The Bankruptcy Act of 1898 remained in effect for eighty years. Bankruptcy Act of 1898, 30 Stat. 544 (1898) (repealed 92 Stat. 2682 § 401(a) (1978)). *See generally* C. WARREN, BANKRUPTCY IN UNITED STATES HISTORY (1935). Concerning the foreign representative's standing to begin an involuntary case, *see infra* note 196.

37. Under bankruptcy law in the United States, attachments levied by creditors on the debtor's property shortly before bankruptcy is filed can often be avoided by a bankruptcy trustee as a form of preferential transfer to creditors. Bankruptcy Act §§ 60, 67, 70, 11 U.S.C. §§ 96, 107, 110 (1976) (repealed 92 Stat. 2682 § 401(a) (1978)); Bankruptcy Code §§ 544-49, 11 U.S.C. §§ 544-49 (Supp. IV 1980). One commentator noted that while a discharge may be the incentive for debtors to file voluntary bankruptcy, the trustee's avoiding powers provide the incentive for creditors to begin involuntary bankruptcy proceedings against debtors. Teofan & Creel, *The Trustee's Avoiding Powers Under the Bankruptcy Act and the New Code: A Comparative Analysis*, 11 ST. MARY'S L.J. 311, 311 (1979). For specific examples of this practice involving international bankruptcies, *see infra* note 198. For similar avoiding powers in the bankruptcy laws of other countries, *see* DALHUISEN, *supra* note 2, at 3-320 n.28. Both the former Bankruptcy Act and the new Bankruptcy Code give the bankruptcy court jurisdiction over nonresidents with property in the United States, or doing business in the United States. Bankruptcy Act § 2a(1), 11 U.S.C. § 11a(1) (1976) (repealed 92 Stat. 2682 § 401(a) (1978)); Bankruptcy Code § 109(a), 11 U.S.C. § 109(a) (Supp. IV 1980). *See infra* note 61.

38. *See e.g.*, the importance placed by the federal court on the principles of comity and reciprocity in *In re Aktiebolaget Krueger & Toll*:

[A]ny action taken by this court will be taken with a view to the most earnest cooperation with the authorities in Sweden in the interests of all creditors and that

dated the American Revolution,³⁹ was inevitable because the Bankruptcy Act was silent on the subject.⁴⁰

III. THE BANKRUPTCY REFORM ACT OF 1978

The Bankruptcy Reform Act of 1978 was the first major overhaul of the federal bankruptcy law in forty years.⁴¹ It was the culmination of five years of work, in which the drafters attempted, among other things, to make case administration more efficient, provide greater relief for consumer debtors, and streamline the business reorganization sections. Despite the existence of many more important and more controversial aspects to bankruptcy reform, a section dealing with the problem of international bankruptcies appeared in the earliest draft of the new law.⁴² The section generated little controversy⁴³ and later

any administration of the property in America of the Kreuger & Toll Company would be without any thought of preferential treatment of American creditors unless indeed preferential treatment were given in Sweden as against American creditors. . . .

In re Aktiebolaget Kreuger & Toll, 20 F. Supp. 964, 965 (S.D.N.Y. 1937) (emphasis deleted), *aff'd*, 96 F.2d 768 (2d Cir. 1938).

39. See cases cited *supra* note 30.

40. The Bankruptcy Act was amended in 1962 to add § 2a(22): "[Courts of bankruptcy may] exercise, withhold, or suspend the exercise of jurisdiction, having regard to the rights or convenience of local creditors and to all other relevant circumstances, where a bankrupt has been adjudged bankrupt by a court of competent jurisdiction without the United States." Act of Sept. 25, 1962, Pub. L. No. 87-681 § 2, 76 Stat. 570 (codified at 11 U.S.C. § 11a(22) (1976) repealed 92 Stat. 2682 § 401(a) (1978)).

41. The last such reform was the Chandler Act of 1938. Pub. L. No. 696, 52 Stat. 840 (1938) (repealed 92 Stat. 2682 § 401(a) (1978)). Work on the Bankruptcy Reform Act of 1978 was begun in 1970 when Congress created the Commission on the Bankruptcy Laws of the United States (the Commission) to study the bankruptcy system in the United States and to recommend changes. Pub. L. No. 91-354, 84 Stat. 468 (1970). The Commission finished its work in 1973; its report was accompanied by a draft bill for a new bankruptcy law. COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, H.R. DOC. NO. 93-137, Parts I & II, 93rd Cong., 1st Sess. (1973). The Commission Report was found at Part I of the document; the draft bill was in Part II [hereinafter cited as COMMISSION BILL]. Approximately five years later, the final version of the bankruptcy reform bill was passed by both houses of the 95th Congress, and signed into law by President Jimmy Carter on November 6, 1978. The new law became effective on October 1, 1979. Act of November 6, 1978, Pub. L. No. 95-598, 92 Stat. 2549 (codified at 11 U.S.C. § 101 (Supp. IV 1980)). For an excellent legislative history of the Bankruptcy Act of 1978, see *generally* 1979 ANN. SURVEY BANKR. L. 1-75.

42. Section 4-103. *Administration of Debtors' Estates Involving More Than One Country.*

(a) *Complaint by Debtor or Creditor to Obtain Dismissal or Suspension of Case When a Foreign Proceeding is Pending.* When a proceeding for the purpose of the liquidation or rehabilitation of his estate has been commenced in a court of competent jurisdiction in another country or against a debtor who is also a debtor in a case filed under this Act, the debtor or a creditor may file a complaint in the bankruptcy court seeking dismissal or suspension of the case commenced under this Act.

(b) *Petition or Complaint by a Foreign Trustee or Administrator.* A trustee, administrator, or other representative of a debtor's estate appointed in a proceed-

drafts made only minor changes.⁴⁴

A. *International Provisions: An Overview*

In its final form, the Bankruptcy Code contains at least seven pro-

ing in a court of competent jurisdiction in another country for the purpose of its liquidation or rehabilitation may file any of the following pleadings in the bankruptcy court:

(1) *a petition as a creditor* pursuant to section 4-205 of this Act if the debtor is subject to involuntary relief as provided in section 4-204;

(2) *a complaint seeking dismissal* or suspension of a case commenced under this Act or against the debtor;

(3) *a complaint seeking an injunction* to stay the commencement or continuation of any action against the debtor, or the enforcement of any judgment against him, or of any act or the commencement or continuation of any court proceeding to create or enforce any lien against his property; or

(4) *a complaint seeking delivery* of the property of the debtor's estate or its proceeds.

(c) *Power and Discretion of the Court.* After a hearing on notice issued pursuant to the filing of a complaint under subdivision (a) or clause (1) or (2) of subdivision (b), the bankruptcy court may dismiss, suspend, or continue the case commenced under this Act, on such terms as may be appropriate. *In addition*, the court may issue injunctions, turnover orders, and other appropriate relief in a proceeding under this section, *whether or not a petition has been filed by or against the debtor under this Act.* In exercising its discretion under this section, the court shall be guided by a consideration of what will best assure an economical and expeditious administration of the debtor's estate consistent with the objectives of fair and equitable treatment of all creditors, the protection of local creditors against prejudice and inconvenience in the processing of their claims, the avoidance of preferential and fraudulent dispositions of proceeds substantially in accord with the order prescribed by this Act, and, where appropriate, the provision of an opportunity for a fresh start for the debtor.

COMMISSION BILL, *supra* note 41, at § 4-103.

43. The only real opposition to the international provisions in the bill came from Professor Kurt Nadelmann, one of the world's leading authorities on the subject of international insolvency and bankruptcy. *See Hearings on H.R. 31, supra* note 7, at 1446-47 (statement of Prof. Kurt H. Nadelmann). *See infra* note 214.

44. The numbering system used in the COMMISSION BILL was changed, and section 4-103 (*see supra* note 42) became section 304. The provisions of section 4-103 were carried over into the later drafts, but were broken up into several different sections. Section 4-103 covered most aspects of the U.S. part of an international bankruptcy. In the later drafts of the bill, all provisions concerning suspension or dismissal of a case in deference to a foreign proceeding were moved to a separate section dealing with abstention by the court. *See* 11 U.S.C. § 305 (Supp. IV 1980); *infra* text accompanying notes 172-89. The clause in section 4-103 allowing the foreign representative to begin an involuntary bankruptcy case against the debtor was moved to section 303, which governed involuntary petitions. *See* 11 U.S.C. § 303(b)(4) (Supp. IV 1980); *infra* text accompanying notes 190-96. Section 304 was devoted solely to the elements of an ancillary case.

Only two other changes were made later in the revision process. One of the amendments added to compromise differences between the final House and Senate bills made clear that "parties in interest" could oppose the foreign representative's petition for relief. 124 CONG. REC. H11091 (remarks of Rep. Edwards), *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 6442; 124 CONG. REC. S17408 (remarks of Sen. DeConcini), *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 6510. The final House and Senate bills had allowed only the debtor to controvert the petition. *See* H.R. 8200, 95th Cong., 1st Sess. § 304(b) (1977); S. 2266, 95th Cong., 1st Sess. § 304(b) (1977). Another amendment added the requirement that the court consider "comity" when making its decision. 124 CONG. REC. H11091 (remarks of Rep. Edwards); 124 CONG. REC. S17408 (remarks of Sen. DeConcini).

visions dealing with the local effects of a foreign bankruptcy. Sections 101(19)⁴⁵ and 101(20)⁴⁶ define "foreign proceeding" and "foreign representative." The most important sections, however, are sections 304⁴⁷ and 305.⁴⁸ Section 304 allows the representative of a foreign bankruptcy proceeding to begin a "case ancillary to foreign proceedings" in a U.S. bankruptcy court.⁴⁹ Section 305 allows the dismissal or suspension of a U.S. bankruptcy case when there is a pending foreign proceeding.⁵⁰ Thus, sections 304 and 305 are complementary: although both presuppose the existence of foreign bankruptcy proceedings, section 304 assumes that there are no U.S. proceedings, while section 305 assumes that a U.S. bankruptcy case has already begun. Section 304 is longer, and includes detailed guidelines for the court,⁵¹ but Section 305 is cross-referenced to the preceding section,⁵² so the same guidelines apply to decisions made under section 305.

Section 303(b)(4)⁵³ gives the foreign representative standing to begin a regular involuntary bankruptcy case. Section 303(k)⁵⁴ brings foreign banks within U.S. bankruptcy jurisdiction for the first time. Section 306⁵⁵ guarantees the foreign representative immunity from other lawsuits while making an appearance under sections 303, 304, or 305. Section 508(a)⁵⁶ governs multiple recoveries by creditors who have received dividends in the debtor's foreign bankruptcy proceedings. Section 1474⁵⁷ governs venue in an ancillary case.

These sections are not a new approach to the problem. Rather, they derive from the traditional principles followed by state and federal courts for many years.⁵⁸ For example, a "threshold" test is found in the Code's definition of "foreign proceeding:" the duly selected representative of a foreign court⁵⁹ holding bankruptcy or insolvency proceedings for the debtor does not qualify for relief under sections 304 and

45. 11 U.S.C. § 101(19) (Supp. IV 1980).

46. *Id.* § 101(20).

47. *Id.* § 304.

48. *Id.* § 305.

49. Hereinafter referred to as an "ancillary case." See *infra* text accompanying notes 69-171.

50. See *infra* text accompanying notes 172-89.

51. See 11 U.S.C. § 304(c) (Supp. IV 1980).

52. See *id.* § 305(a)(2)(B).

53. *Id.* § 303(b)(4). See text accompanying notes 190-96 *infra*.

54. *Id.* § 303(k).

55. *Id.* § 306.

56. *Id.* § 508(a).

57. 28 U.S.C. § 1474 (Supp. IV 1980). See *infra* text accompanying notes 210-13.

58. See *supra* text accompanying notes 29-35.

59. One commentator has suggested that the foreign representative should prove his authority by "producing the foreign order 'selecting' or appointing . . . [him], attested to by the local vice consul of the United States." Honsberger, *Conflict of Laws and the Bankruptcy Reform Act of 1978*, 30 CASE W.L. REV. 631, 645 (1980) [hereinafter cited as Honsberger,

305 unless the court is located in a country that is the debtor's domicile, residence, principal place of business, or site of the debtor's principal assets.⁶⁰ This establishes the Code's standards for proper jurisdiction by the foreign court, and is a prerequisite for relief under sections 304 and 305.

Jurisdiction by the U.S. bankruptcy court over the U.S. property of the debtor who is the subject of foreign proceedings, and over the debtor himself, is found in section 109.⁶¹ There the Code brings within U.S. bankruptcy jurisdiction any person who resides, has a domicile, has a place of business, or has property in the United States.⁶² Other principles followed by U.S. courts in international bankruptcy cases,⁶³ such as comity⁶⁴ and nondiscrimination by the foreign court,⁶⁵ appear in the guidelines for the court in section 304(c).⁶⁶ While these guidelines are not binding on the court, they show a clear Congressional intent that the courts continue to follow the case law that has developed on the subject,⁶⁷ except when the case law contradicts the language of the statute.⁶⁸

B. Analysis of Section 304

1. *Nature of an Ancillary Case.* Section 304⁶⁹ is an attempt "at a clarification, codification, and federalization, of the principles gov-

Conflict of Laws]. This procedure is a good idea, although there is nothing in the statute requiring attestation by a U.S. diplomat.

60. 11 U.S.C. § 101(19) (Supp. IV 1980).

61. Notwithstanding any other provision of this section, only a person that resides in the United States, or has a domicile, a place of business, or property in the United States, or a municipality, may be a debtor under this title. *Id.* § 109(a).

62. *Id.*

63. See *supra* text accompanying notes 29-35.

64. 11 U.S.C. § 304(c)(5) (Supp. IV 1980).

65. *Id.* § 304(c)(1), (2).

66. See *infra* text accompanying notes 114-45.

67. See, e.g., cases cited *supra* notes 30-35, 38.

68. This conclusion follows from the guidelines in section 304(c). Dalhuisen has also concluded that in applying sections 304 and 305 the bankruptcy courts "will largely follow the established system, with the possible exception of the effect of a foreign adjudication on real property inside the United States and on attachments levied within the United States . . . after the opening of the foreign proceedings." DALHUISEN, *supra* note 2, at 3-144.

69. § 304. 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

erning the status of foreign administrators in insolvency."⁷⁰ The purpose of an ancillary case is to "administer assets located in this country, to prevent dismemberment by local creditors of assets located here, or for other appropriate relief."⁷¹ It is available when a foreign proceeding⁷² is pending against a debtor with assets in the United States.

The debtor is only a bystander under this section; he is relegated to the status of "party in interest."⁷³ He may not commence an ancillary case, but does have standing to oppose it.⁷⁴ Only the "foreign representative"⁷⁵ of a "foreign proceeding"⁷⁶ may commence an ancillary case

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.

11 U.S.C. § 304 (Supp. IV 1980).

70. Riesenfeld, *The Status of Foreign Administrators of Insolvent Estates: A Comparative Survey*, 24 AM. J. COMP. L. 288, 296 (1976). This statement was made in reference to the COMMISSION BILL § 4-103, *supra* note 41, but it applies equally to section 304. *See also Hearings on H.R. 31, supra* note 7, at 1509 (statement of Prof. Stefan A. Riesenfeld).

71. H.R. REP. NO. 95-595, 95th Cong., 1st Sess. 324 (1977) [hereinafter cited as HOUSE REPORT], *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5963, 6281; S. REP. NO. 95-989, 95th Cong., 2d Sess. 35 (1978) [hereinafter cited as SENATE REPORT], *reprinted in* [1978] U.S. CODE CONG. & AD. NEWS 5787, 5821.

72. *See infra* note 76.

73. Section 1109 provides that in a Chapter 11 case a party in interest includes "the debtor, the trustee, a creditors' committee, a creditor, an equity security holder, or any indenture trustee." 11 U.S.C. § 1109(b) (Supp. IV 1980). This section does not apply to other chapters of the Bankruptcy Code, but this is the only indication of what the drafters of the statute intended the term to mean. Compare the Code's definition of "disinterested party" in section 101(13)(E). *Id.* at § 101(13)(E).

74. HOUSE REPORT, *supra* note 71, at 324; SENATE REPORT, *supra* note 71, at 35.

75. "[F]oreign representative' means duly selected trustee, administrator, or other representative of an estate in a foreign proceeding." 11 U.S.C. § 101(20) (Supp. IV 1980). *See infra* note 76.

76. '[F]oreign proceeding' means 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.

Id. § 101(19).

under section 304,⁷⁷ which is done by filing a "petition" with the bankruptcy court.⁷⁸ This does not "commence a case" under the Code, as would filing a petition under sections 301, 302, or 303,⁷⁹ so most of the provisions of Chapters 3, 5, and 7 of the Code may not apply to an ancillary case.⁸⁰ Thus there is no meeting of creditors,⁸¹ no trustee,⁸² and no discharge.⁸³

Although the debtor is not required to appear before the bankruptcy court,⁸⁴ or to file the usual schedules of creditors, assets, and liabilities,⁸⁵ the court has the power to require such action under its general equity powers.⁸⁶ A requirement that the debtor furnish the court with the names of creditors may be necessary if the court assumes the function of giving notice of an ancillary case to parties in interest. Even if the foreign representative is responsible for giving notice of his petition, the court might still want the debtor's schedules and other financial information to help in deciding whether to grant relief in the case.⁸⁷

77. In one of the few reported cases on section 304, a creditor of a foreign debtor with property in the United States petitioned to commence an ancillary case. The bankruptcy judge correctly dismissed the petition because there was no allegation that the debtor was the subject of a pending foreign bankruptcy case. But the court failed to point out that the petition was also defective because a creditor is not eligible to request commencement of an ancillary case under section 304. *See In re Stuppel*, 7 B.R. 341 (Bankr. S.D. Fla. 1980).

78. The procedural requirements of the petition will not be certain unless new Rules of Bankruptcy Procedure cover ancillary petitions. In the absence of such a rule, the petition would presumably be styled "Petition to Commence a Case Ancillary to Foreign Proceedings" and would include a jurisdictional statement describing the nature of the foreign proceedings and the foreign representative's authority to represent the debtor's estate; a description of the nature and location of the debtor's U.S. assets; and a description of the relief sought under section 304. *See supra* note 59.

79. HOUSE REPORT, *supra* note 71, at 324; SENATE REPORT, *supra* note 71, at 35.

80. The broad injunctive powers in section 304 effectively duplicate some of the features found elsewhere in the Bankruptcy Code. *See infra* text accompanying notes 97-99. One court allowed a foreign representative who had initiated an ancillary case to file a complaint seeking to avoid a transfer under section 547. *In re Comstat Consulting Services, Ltd.*, 10 B.R. 134 (Bankr. S.D. Fla. 1981). It appears, however, that section 304 was meant to be self-contained, without the need for reference to other sections of the Code. *See infra* text accompanying note 171.

81. *See* 11 U.S.C. § 341(a) (Supp. IV 1980).

82. *See id.* §§ 701-704. A trustee may be necessary, however, if the court decides to administer all U.S. assets of the debtor in a separate U.S. proceeding, rather than order turnover of the assets to the foreign representative.

83. *See id.* §§ 727(a), 1141(d)(1)(A), 1328(a).

84. Venue for ancillary cases is governed by 28 U.S.C. § 1474 (Supp. IV 1980). *See infra* text accompanying notes 210-13.

85. *See* 11 U.S.C. § 521(1) (Supp. IV 1980). In the *Finabank* case (*see infra* text accompanying notes 103-11) the Second Circuit Court of Appeals said that because of the nature of proceedings ancillary to a foreign bankruptcy, complete schedules may not be necessary. *Banque de Financement, S.A. v. First Nat'l Bank of Boston*, 568 F.2d 911, 919-20 (2d Cir. 1977).

86. *See* 11 U.S.C. § 105 (Supp. IV 1980).

87. The drafters emphasized that the court is to use its discretion in deciding whether to grant relief under sections 304 and 305. HOUSE REPORT, *supra* note 71, at 324-25; SENATE

Commencing an ancillary case does not "create an estate" under section 541.⁸⁸ The statute is ambiguous as to whether the debtor's U.S. assets have any special status apart from the debtor's foreign estate. The answer seems to be "no," because while the presence in the United States of the debtor's property gives the U.S. bankruptcy court jurisdiction,⁸⁹ the language of section 304 implies that the debtor's local assets are to be considered part of the debtor's estate in the foreign proceeding. The statute makes no distinction between the debtor's "property involved in such foreign proceeding" in subsection (b)(1)(A)(i), and "the property of such estate" in subsection (b)(1)(B). Under subsection (2) the court may "order the turnover of the property of such estate." The "property of such estate" to be turned over is, of course, the debtor's U.S. property.⁹⁰ By implication, all terms referring to the debtor's estate mean the same thing. The debtor's U.S. assets are considered "property of such estate" involved in such foreign proceeding. No exceptions are made for any assets that have been attached by local creditors.⁹¹ The absence in the statute of a distinction between the debtor's foreign property and his U.S. property could be considered an implicit recognition by the Bankruptcy Code of the concept of the complete unity⁹² of the debtor's estate.⁹³

REPORT, *supra* note 71, at 35. The guidelines in section 304(c) offer some help, but the court may need more information to make its decision. The court surely has the power to request such information, even though it is not specifically required by statute.

88. "The commencement of a case under sections 301, 302, or 303 of this title creates an estate." (Emphasis added). 11 U.S.C. § 541(a) (Supp. IV 1980).

89. *Id.* § 109.

90. The statute considers the debtor's U.S. assets to be part of the estate administered in the foreign proceeding and allows the turnover of those assets to the foreign representative. The statute does not say, however, whether the foreign representative must have statutory authority to collect the U.S. assets under the law of his own jurisdiction. It has long been a rule of conflict of laws in the United States that a foreign receiver must have specific statutory authority to collect assets located outside his jurisdiction. See *Waxman v. Kealoha*, 296 F. Supp. 1190, 1193-94 (D. Hawaii 1969); Nadelmann, *Codification, supra* note 7, at 64; Nadelmann, *National Bankruptcy Act, supra* note 2, at 1026. This rule is followed in Great Britain as well. DICEY & MORRIS, *supra* note 9, at 691. For a survey of the provisions for extraterritorial effect of their own bankruptcies found in different national bankruptcy laws, see DALHUISEN, *supra* note 2, at 3-153 to 157. As for the foreign representative attempting to collect assets in the United States, Dalhuisen suggests the possibility of obtaining a separate *quasi in rem* judgment in the United States in aid of the foreign judgment, if the foreign law does not specifically provide for collection of assets abroad. DALHUISEN, *supra* note 2, at 3-151.

91. See *infra* note 93; text accompanying notes 161-71.

92. See *supra* note 9.

93. The language of the statute is broad, and it is possible to draw this conclusion from a reading of the statute alone. But if the precedent of case law is to have any effect on the application of this law, the reach of the foreign court is much more restricted than would seem at first glance. Traditionally, courts in the United States have never recognized a foreign bankruptcy judgment to affect real property of the bankrupt located in the United States. *Maconchy v. Delehanty*, 11 Ariz. 366, *rev'd. sub. nom. In re Delehanty's Estate*, 95 P. 109 (1908). See *infra* text accompanying notes 151-60.

Another long-standing U.S. policy has been to reward the diligence of local creditors

Section 304 provides for several forms of relief, including injunction and turnover of assets. Also, the court may order "other appropriate relief."

(a) *Injunction*. One of the stated purposes of the statute is to prevent dismemberment of the estate by local creditors.⁹⁴ To that effect, the court may "enjoin the commencement or continuation of any action against either the debtor with respect to property involved in the [foreign] proceeding; or against the property itself."⁹⁵ The court may also enjoin the enforcement of any judgment against the debtor or the debtor's property, or the commencement or continuation of any judicial proceeding to create or enforce a lien against the property of the estate.⁹⁶

The injunctive relief in section 304 duplicates that provided by the automatic stay in section 362,⁹⁷ and is based on the court's power to use injunction to protect its jurisdiction over assets in its custody.⁹⁸ But the language of the statute is ambiguous as to whether the injunction amounts to only a temporary stay, or if it can be used as a permanent injunction to avoid liens on the debtor's local property.⁹⁹

(b) *Turnover*. The other relief available to the foreign representative, turnover of local assets, has no precedent in the Bankruptcy Act. Its appearance in the Commission bill¹⁰⁰ in 1973 was justified only by some current practices regarding insolvent decedents' estates, and by principles in the *Restatement (Second) of Conflict of Laws*.¹⁰¹ It was criticized for that reason.¹⁰² In August 1977, however, the Court of Appeals for the Second Circuit handed down its opinion in *Banque de*

who levy attachments on the local property of a foreign debtor. This was true even when the attachments were levied *after* a foreign bankruptcy judgment concerning the debtor. See *supra* text accompanying notes 28-35. Thus, if these principles are followed in applying section 304, the estate of the debtor involved in foreign proceedings would not include real property in the United States or personal property in the United States attached by local creditors. But see further discussion in text accompanying notes 151-71 *infra*.

94. HOUSE REPORT, *supra* note 71, at 324; SENATE REPORT, *supra* note 71, at 35.

95. 11 U.S.C. § 304(b) (Supp. IV 1980).

96. *Id.* In one recent case, the court allowed actions pending in the United States against a foreign debtor to proceed up to and through the entry of judgment, but enjoined the litigants from enforcing or executing any judgments obtained without further permission from the court. *In re Lineas Aereas de Nicaragua, S.A.*, 10 B.R. 790 (Bankr. S.D. Fla. 1981).

97. *Id.* § 362.

98. 2 COLLIER ON BANKRUPTCY ¶ 362.01 (15th ed. 1981).

99. See *infra* text accompanying notes 161-71.

100. See *supra* note 41.

101. RESTATEMENT (SECOND) OF CONFLICT OF LAWS §§ 331, 386 (1971). COMMISSION BILL, *supra* note 41, at 4-103 n.2.

102. See *Hearings on H.R. 31, supra* note 7, at 1448-49, 1506 (statement of Prof. Kurt H. Nadelmann).

Financement, S.A. v. First National Bank of Boston.¹⁰³ There the court said that the turnover power was implicit in section 2a(22) of the Bankruptcy Act.¹⁰⁴

The appeals court considered the bankruptcy court's power to administer local assets ancillary to the insolvency proceedings of the Swiss court, and concluded that the Bankruptcy Act permits the United States segment of an international bankruptcy to act essentially as an instrument to set aside preferences.¹⁰⁵ Section 2a(22)¹⁰⁶ and Rule 119¹⁰⁷ authorized the bankruptcy court to "exercise its discretion to dismiss the proceeding, or, after setting aside any preferences, to suspend the proceedings and permit assets located in this country to be administered pursuant to the domiciliary proceeding."¹⁰⁸

The court said that an alternative to turnover of the assets was a full administration of the assets in the United States coordinated with the foreign proceeding. Creditors would have the option of filing claims in either proceeding, and marshalling provisions would ensure equal distribution.¹⁰⁹ The court said in dicta that "undoubted power" to turn over the local assets came from section 2a(22) and Rule 119.¹¹⁰ But the court was less certain about the coordinated administration of

103. 568 F.2d 911 (2d Cir. 1977), reprinted in 16 I.L.M. 1367 (1977); noted in 13 TEX. INT'L L.J. 340 (1978).

104. 568 F.2d at 919-21. See *supra* note 40.

Banque de Financement (Finabank) was a Swiss bank that neither did business in the United States nor maintained an office here. The bank became insolvent when another bank defaulted on its foreign exchange contracts. Finabank began reorganization proceedings in a Swiss court. Negotiations with creditors proved unsuccessful, and almost two years later the Swiss court ordered the bank's liquidation.

Finabank's insolvency had caused it to default on foreign exchange contracts with a number of American banks. The U.S. creditors immediately attached a \$12 million New York bank account that Finabank used to cover its foreign exchange obligations. Within four months of the attachments, Finabank filed for reorganization under Chapter XI of the Bankruptcy Act. It asked the court to await the results of the negotiations pending in the Swiss court proceedings. Eight months later, with no plan of arrangement imminent in the Swiss court, the bank had yet to submit a plan or even a complete schedule of creditors in the U.S. proceedings. The bank was unable to file a complete schedule of creditors because Swiss banking laws provide criminal penalties for disclosure of a bank's depositors. The bankruptcy court then dismissed the bank's petition, leaving intact the attachments by the American banks. *In re Banque de Financement, S.A.*, 2 BANKR. CT. DEC. (CCR) 83 (S.D.N.Y. 1976). On appeal by Finabank, the district court affirmed, *In re Banque de Financement, S.A.*, No. 75-B-764, [1976] 6 BANKR. L. REP. (CCH) ¶ 66,326, (S.D.N.Y. July 30, 1976) but the appeals court reversed. 568 F.2d 911. The court held that the bankruptcy court was wrong to dismiss the bank's petition without considering the possibility of a U.S. administration ancillary to the Swiss proceedings. *Id.* at 921-22.

105. *Id.* at 918-19.

106. See *supra* note 39.

107. Fed. R. Bankr. P. 119. Presumably Rule 119 has been superseded by the enactment of section 305 of the Bankruptcy Code. See 11 U.S.C. § 305 (Supp. IV 1980).

108. 568 F.2d at 919.

109. *Id.* at 920. Marshalling is discussed *infra* in text accompanying notes 205-09.

110. *Id.* at 920 n.18.

the assets. The court admitted that there was no express statutory support, but said that such action might be within the bankruptcy court's powers as a court of equity.¹¹¹

Section 304 explicitly codifies the turnover power that the court found implicit in section 2a(22) of the Bankruptcy Act. There is still no statutory support in the Code expressly authorizing a concurrent local administration of the debtor's assets, but this is certainly within the court's power to grant "other appropriate relief."¹¹² Because of this power, the court is not limited to the injunctive and turnover relief in section 304(b). The statute is intended to give the bankruptcy court great flexibility to shape its relief to the circumstances of the case.¹¹³

In the only bankruptcy court opinion to consider the procedure to be followed in a case initiated under section 304, the court found that an ancillary case can be divided into two parts or issues: (1) objections to the petition and (2) the relief sought by the foreign representative. Any objections to the ancillary petition should be considered first. If the objections are overruled, the court would then consider the relief requested by the foreign representative.¹¹⁴

2. *Discretion of the Bankruptcy Court.* The decision on what relief to grant, if any, under section 304 is discretionary with the court. This discretion is an essential safeguard because of the great differences in legal systems in the world. For example, a fundamental principle of the U.S. bankruptcy system is equal treatment of creditors. Cooperation with the representative of a foreign court under section 304 presupposes the existence of a similar policy in the foreign jurisdiction. The Congress did not intend to put American creditors at the mercy of a foreign legal system that discriminates against nondomestic creditors.¹¹⁵

The bankruptcy court is advised to be "guided by what will best

111. *Id.*

112. See 11 U.S.C. § 304(b) (Supp. IV 1980). A concurrent administration of the local assets would be desirable if the court decides that a turnover of the assets to the foreign representative is not warranted. A concurrent local administration would ensure equal distribution of the local assets without forcing U.S. creditors to make claims in the foreign proceeding. In *In re Lineas Aereas de Nicaragua, S.A.* the court granted the request of the foreign representative for turnover of the foreign debtor's U.S. assets, subject to the condition that none of the assets would be removed from the United States, and that they would be applied primarily to satisfy debts owing to the debtor's U.S. creditors. *In re Lineas Aereas de Nicaragua, S.A.*, 10 B.R. 790 (Bankr. S.D. Fla. 1981).

113. HOUSE REPORT, *supra* note 71, at 324-25; SENATE REPORT, *supra* note 71, at 35.

114. *In re Egeria Societa Per Azioni Di Navigazione*, 20 B.R. 625 (Bankr. E.D. Va. 1982). Although the court refers in the opinion to the "debtor" seeking relief under section 304, the petition was filed by the foreign representative of the debtor. *Id.* at 626.

115. *See Banque de Financement, S.A. v. First Nat'l Bank of Boston*, 568 F.2d 911, 921 (2d Cir. 1977).

assure an economical and expeditious administration of . . . such estate. . . ."¹¹⁶ To further aid the court, the drafters have included as guidelines six principles of policy. When making its decision, the court must consider the following principles:

- (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.¹¹⁷

The statute says that these principles must be considered by the court when making its decision. While the court's ultimate decision should be consistent with them, they are intended only to guide the court, not to bind it. The legislative history stresses that the guidelines are intended to give the court "maximum flexibility" in dealing with the ancillary case.¹¹⁸ This appears to be an attempt by the drafters to summarize within the statute the principles of policy that have developed in the case law over the years.

Consideration of the first two principles¹¹⁹ will require the bankruptcy court to determine the law of the foreign jurisdiction regarding claims by nondomestic creditors. If the representative of the foreign court can prove that domestic and nondomestic creditors are treated equally in the distribution of the debtor's estate, this will substantially satisfy the first two criteria. If the law of the foreign jurisdiction discriminates against nondomestic creditors, the bankruptcy court should not grant any relief under section 304 that would force American creditors into the foreign proceedings. The appellate court in *Finabank* took the position that "[i]n exercising its discretion the district court is to guard against forcing American creditors to participate in foreign proceedings in which their claims will be treated in some manner inimical to this country's policy of equality."¹²⁰

116. 11 U.S.C. § 304(c) (Supp. IV 1980).

117. *Id.*

118. HOUSE REPORT, *supra* note 71, at 325; SENATE REPORT, *supra* note 71, at 35.

119. 11 U.S.C. § 304(c)(1)-(2) (Supp. IV 1980).

120. 568 F.2d at 921.

Convenience¹²¹ presents a different consideration. Undoubtedly, whenever a creditor from the United States is forced to file a claim in a foreign proceeding, the creditor will find it inconvenient. This is a problem that cannot be completely eliminated. But if this consideration were paramount, it would effectively prohibit a turnover of assets to a foreign representative *whenever* there are American creditors. This could not have been the intent of Congress, since such an interpretation would effectively emasculate the relief provisions of the statute. A reasonable approach to the issue of convenience would be to examine the status of the American creditors in question. Creditors of a debtor with assets in more than one country are likely to be large commercial concerns capable of employing local counsel to represent them in the foreign proceeding. Where the creditor is an individual or a small business, having to file a claim abroad may work a serious hardship. Convenience would then become an important issue for the court to consider.

The principle of equality of distribution has always been the basis for the bankruptcy court's power to avoid preferences gained by creditors immediately preceding bankruptcy.¹²² A policy that favors American creditors with attachments or assignments from the nonresident debtor is inimical to this principle of equality. The court in *Finabank* noted that "[s]ection 2a(22) was not intended to be the instrument by which jurisdiction over a foreign domiciliary grounded in section 2a(1) could be undercut for the purpose of validating preferential transfers to United States nationals."¹²³ Thus factor (3) seems intended to remind the bankruptcy court that a decision to deny relief under section 304 could have the effect of *preserving* "preferential or fraudulent dispositions of property" of the estate.¹²⁴

The court must also remember that the substantive law of bankruptcy varies considerably from country to country. Factor (4)¹²⁵ shows that the drafters of the statute were concerned not only with equal treatment of creditors abroad, but also with the distribution scheme used by the foreign court. Sections 507 and 726 of the Bankruptcy Code determine the priority given to each type of claim. The drafters believe that the foreign method of distribution should be "substantially in accordance with" the American scheme¹²⁶ in order to

121. 11 U.S.C. § 304(c)(2) (Supp. IV 1980).

122. See 4 COLLIER ON BANKRUPTCY ¶ 547.03 (15th ed. 1981).

123. 568 F.2d at 921.

124. See 11 U.S.C. § 304(c)(3) (Supp. IV 1980).

125. *Id.* § 304(c)(4).

126. *Id.* There is, of course, no way to determine here what kind of system would be "substantially in accordance with" the distribution system used in the Bankruptcy Code.

avoid prejudice to local creditors. If the difference in the priority given a creditor's claim by the foreign court would substantially diminish the amount of a creditor's recovery, the bankruptcy court would have to weigh this heavily in its decision.¹²⁷

The fifth consideration for the court is "comity."¹²⁸ This principle determines how the courts of one country recognize and enforce locally the judicial and legislative acts of another country. There is a presumption in favor of recognition, but it is ultimately a matter of discretion. Comity requires recognition except when to do so would prejudice the interests of the country's own citizens,¹²⁹ or when it would be repugnant to its public policy.¹³⁰ The essence of comity is voluntary, rather than compulsory, recognition.

The leading U.S. case on comity, *Hilton v. Guyot*,¹³¹ is perhaps better known for the dictum that reciprocity is an essential element of comity; that is, a U.S. court should recognize a foreign judgment only to the extent that the foreign court would recognize the same judgment rendered by an American court. But reciprocity has never had much influence on the comity doctrine internationally.¹³² In the United States the reciprocity requirement has been criticized,¹³³ and a number

The drafters did not indicate how much variation would be permissible. But this ambiguity can also be considered "flexibility," and allows more room for a subjective decision by the court.

This section does solve a potential choice of law problem if the bankruptcy court were to decide to administer the debtor's local assets in a separate U.S. proceeding rather than allowing their administration by the foreign court. The intent is clear that in that situation the local assets would be administered according to U.S. law rather than the law of the foreign country, even though the U.S. proceedings are only ancillary to the main proceedings abroad.

127. Because of the great differences in national bankruptcy laws, this may prove to be a major obstacle to cooperation between the U.S. court and the foreign court in the context of sections 304 and 305. See *supra* note 8. This is unfortunate because as Dalhuisen notes, the essence of bankruptcy in the traditional sense is "equitable distribution," not "equality of creditors." This is a more flexible interpretation and allows for greater differences in the substantive and procedural details of national bankruptcy systems—differences which are often caused by differing needs and goals of each society. The definition of what is equitable distribution can, and should be, left to local statute. DALHUISEN, *supra* note 2, at 3-182 n.34.

128. 11 U.S.C. § 304(c)(5) (Supp. IV 1980).

129. See *infra* note 137.

130. See *infra* note 138.

131. *Hilton v. Guyot*, 159 U.S. 113 (1895). There the U.S. Supreme Court defined comity to be:

neither a matter of absolute obligation . . . nor of mere courtesy and good will 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.

Id. at 163-64. See also *Somportex, Ltd. v. Philadelphia Chewing Gum Corp.*, 453 F.2d 435 (3d Cir. 1971), *cert. denied*, 405 U.S. 1017 (1972).

132. See DALHUISEN, *supra* note 2, at 3-34.

133. See H. GOODRICH & E. SCOLES, *CONFLICT OF LAWS* 392 (4th ed. 1964) [hereinafter

of state courts have not followed it.¹³⁴

Traditional defenses to recognition of foreign judgments include lack of jurisdiction by the foreign court,¹³⁵ and fraud in the procurement of the judgment.¹³⁶ Comity is also withheld when granting recognition would prejudice the rights of local citizens,¹³⁷ or would be contrary to the public policy of the forum.¹³⁸

Subdivision (c)(6)¹³⁹ is an anomaly in that it is concerned with the welfare of the debtor, while most of the other guidelines are designed to protect the interests of creditors. Here the bankruptcy court is required to consider whether the debtor can receive a discharge in the foreign proceedings. The right of an honest debtor to receive a "fresh start" by having his debts discharged in bankruptcy is largely taken for granted in the United States.¹⁴⁰ But the bankruptcy and insolvency laws of many countries do not show the same benevolence toward insolvent debtors.¹⁴¹ In those countries not providing for a discharge, the debtor will still be liable for unpaid debts, even after the estate has been liquidated.

This subsection is another attempt to ensure that the bankruptcy court's traditional principles are not compromised in the administration of an ancillary case. But there are other aspects to the discharge issue that limit the practical effect of this guideline. It assumes, of

cited as GOODRICH & SCOLES]; Reese, *The Status in this Country of Judgments Rendered Abroad*, 50 COLUM. L. REV. 783, 792-93 (1950).

134. *Cowans v. Ticonderoga Pulp & Paper Co.*, 219 A.D. 120, 219 N.Y.S. 284, *aff'd*, 246 N.Y. 603, 159 N.E. 669 (1927); *Johnston v. Compagnie Generale Transatlantique*, 242 N.Y. 381, 152 N.E. 121 (1926). See A. EHRENZWEIG, A TREATISE ON THE CONFLICT OF LAWS 165 (1962). States not following the reciprocity requirement include New York, Connecticut, Georgia, Illinois and Louisiana. DALHUISEN, *supra* note 2, at 3-48 n.13.

The issue of comity has been considered recently in several international bankruptcy cases. All spoke approvingly of the role of reciprocity, but none found it determinative. *Clarkson Co. v. Shaheen*, 544 F.2d 624 (2d Cir. 1976); *In re Colorado Corp.*, 531 F.2d 463 (10th Cir. 1976); *Waxman v. Kealoha*, 296 F. Supp. 1190 (D. Hawaii 1969). See *Letter*, 52 N.Y.U. L. REV. 726, 728-29 (1977).

135. GOODRICH & SCOLES, *supra* note 133, at 398. See *Deltac Banking Corp. v. Compania Italo-Argentina de Electricidad*, 46 A.D. 2d 847, 362 N.Y.S.2d 391 (App. Div. 1974), where recognition of an Argentine bankruptcy judgment was refused because the court's jurisdiction over the non-Argentine debtor was based solely on the debtor's ownership of stock in an insolvent international corporation doing business in Argentina.

136. *Id.* at 397.

137. "[N]ational comity requires us to give effect to such assignments only so far, as may be done without impairing the remedies, or lessening the securities, which our laws have provided for our own citizens." STORY, *supra* note 30, § 414.

138. GOODRICH & SCOLES, *supra* note 133, at 398.

139. 11 U.S.C. § 304(c)(6) (Supp. IV 1980).

140. See *Local Loan Co. v. Hunt*, 292 U.S. 234, 244 (1934), *citing Williams v. U.S. Fidelity & Guar. Co.*, 236 U.S. 549, 554-55 (1915); 9 AM. JUR. 2d *Bankruptcy* § 74 (1980).

141. Although a discharge in bankruptcy has long been a feature of bankruptcy law in England and the United States, the institution has never been popular on the European continent. DALHUISEN, *supra* note 2, at 2-5.

course, that the debtor would be eligible for a discharge under U.S. law. But a foreign debtor with substantial assets in the United States will often be a corporation, and thus ineligible for a discharge in liquidation in the United States.¹⁴²

Even if the debtor can be discharged under U.S. law, the discharge may not be effective abroad. The Bankruptcy Code discharges a debtor from all debts and liabilities incurred before the order for relief was entered.¹⁴³ The discharge is binding on all creditors who either participated in the bankruptcy proceedings or had knowledge of the proceedings, and is automatically enforceable in any court in the United States.¹⁴⁴ The discharge purports to have effect outside the United States, but enforcement of the discharge order by a foreign court would be subject to the rules of conflicts of law in that jurisdiction. As a practical matter, many foreign courts do not enforce discharge orders entered by a U.S. court.¹⁴⁵

3. *Opposition to the Petition.* A "party in interest"¹⁴⁶ may timely controvert the petition. Although the debtor and creditors are obviously parties in interest, any party with a pecuniary interest in the estate would probably be included. The debtor may wish to oppose the petition for an ancillary case in order to obtain a discharge in the U.S. proceedings. Creditors may want to oppose the petition to prevent removal of the assets from the country.

The party planning to oppose the foreign representative's petition would have perfect grounds if the foreign judgment violated traditional conflicts rules, such as fraud or lack of jurisdiction.¹⁴⁷ Usually such disabilities will be absent, so the objecting party must look elsewhere for support. Here the guidelines in section 304(c) provide such support. If the objecting party can prove that granting relief under section 304 would violate one or more of the guidelines, he would have a strong argument for denying or modifying the relief requested. While the guidelines are not binding on the court, they are a clear indication of Congressional intent.

Until new Rules of Bankruptcy Procedure are promulgated by the Supreme Court, the proper procedure for controverting a petition

142. See 11 U.S.C. § 727(a)(1) (Supp. IV 1980).

143. *Id.* § 727(b).

144. A discharge of a nonresident debtor by a U.S. bankruptcy court would be binding on actions brought in state or federal court in the United States. Recognition of a U.S. discharge by a foreign court would depend on the rules of conflict of laws followed by that court. See 1A COLLIER ON BANKRUPTCY ¶ 17.07 (14th ed. 1978).

145. Honsberger, *Conflict of Laws*, *supra* note 59, at 664-66.

146. See *supra* note 73.

147. See GOODRICH & SCOLES, *supra* note 133, at 397, 395.

under section 304 will be open to question. Possible methods include an answer, a complaint, or a motion. Although the statute requires opposition to the petition to be "timely,"¹⁴⁸ no time limits are set. Bankruptcy Rule 112, which sets the time for responsive pleadings at twenty days, would probably govern.¹⁴⁹ This time may be extended under Rule 906 at the court's discretion.¹⁵⁰

4. *Problem Areas.* The statute leaves several important questions unanswered. Under section 304, can the bankruptcy court affect the debtor's real property in the United States? The statute refers to the "property of the debtor's estate," and makes no distinction between real and personal property.¹⁵¹ It becomes important then to determine the extent of the foreign bankruptcy estate.¹⁵²

In theory at least, the foreign bankruptcy estate should include real property in the United States. Bankruptcy is a proceeding *in rem*, but it differs from the typical *in rem* action in that the *res* in a bankruptcy is the estate and the status of the debtor, while the *res* in a typical *in rem* action is a particular piece of property.¹⁵³ The bankruptcy estate is usually viewed as one entity consisting of all of the debtor's property wherever located, and proper *in rem* jurisdiction is based on the debtor's residence or domicile.¹⁵⁴ Proper *in rem* jurisdiction in a non-bankruptcy case can only be had if the *res* or particular piece of property is located within the court's territorial jurisdiction.¹⁵⁵

Thus, in a normal action *in rem* maintained in a foreign court,¹⁵⁶ the court would have no jurisdiction over real or personal property in the United States. But in a foreign bankruptcy the *res* would be considered the estate, which should include all of the debtor's property, even real and personal property in the United States. U.S. bankruptcy law is in accord with this theory, and provides that the estate consists of

148. 11 U.S.C. § 304(b) (Supp. IV 1980).

149. FED. R. BANKR. P. 112.

150. *Id.* 906.

151. This is evidently the basis of one commentator's conclusion that the drafters' intended to include real property within the reach of this section. See DALHUISEN, *supra* note 2, at 3-115 n.18.

152. See *supra* text accompanying notes 88-93.

153. DALHUISEN, *supra* note 2, at 3-148 n.91.

154. *Id.* See, e.g., the jurisdictional requirements for recognition of foreign proceedings in section 101(19). 11 U.S.C. § 101(19) (Supp. IV 1980). See *supra* note 76.

155. DALHUISEN, *supra* note 2, at 3-148.

156. Actually, the concept of the judgment *in rem* is peculiar to legal systems in common law countries, and is unknown in civil law countries. But declaratory and "constitutive" judgments under civil law are roughly comparable to the common law judgment *in rem*. DALHUISEN, *supra* note 2, at 3-5, 3-101 to 3-102.

all of the debtor's property, wherever located.¹⁵⁷

In practice, however, courts in the United States have never recognized a foreign bankruptcy judgment as giving the foreign court rights in the debtor's real property in the United States.¹⁵⁸ If this case law is to be followed in applying section 304, then the foreign bankruptcy estate would not include the debtor's real property, and the court would be unable to grant the foreign representative any relief regarding that real property.¹⁵⁹

Nevertheless, in light of the legislative history of this section, it should be interpreted to place as few constraints as possible on the powers of the court. This follows from the broad drafting of the statute, which omits any special status for real property, and from the drafters' insistence that the court be given "maximum flexibility in handling ancillary cases. . . . [and] be permitted to make the appropriate orders under all of the circumstances of each case, rather than being provided with inflexible rules."¹⁶⁰

Another question is whether the bankruptcy court can, as part of the relief to be granted under section 304, affect the rights of local creditors who have levied judicial attachments on the debtor's U.S. property. The statute says only that the court may enjoin the commencement or continuation of any act or judicial proceeding to create or enforce a lien against property of the estate.¹⁶¹ It seems clear from this language that the court can affect the rights of attaching creditors, at least temporarily. One of the stated purposes of the statute is to prevent dismemberment of the estate by local creditors.¹⁶² At the very least this allows the court temporarily to stay any ongoing creditor action against the debtor's U.S. assets, and to prevent any further action during the pendency of the proceedings. Beyond this, the extent of the statute's injunctive power is unclear.

An argument can be made that the court should also be able to enjoin permanently any ongoing lien enforcement attempts; a power that would amount to lien avoidance. This interpretation is plausible

157. 11 U.S.C. § 541(a) (Supp. IV 1980). *See also* Bankruptcy Act § 70 (11 U.S.C. § 110 (1976) (repealed 92 Stat. 2682 § 401(a) (1978))).

158. *Maconchy v. Delehanty*, 11 Ariz. 366, *rev'd. sub. nom. In re Delehanty's Estate*, 95 P. 109 (1908).

159. The foreign representative could, however, commence an involuntary case under section 303(k), thereby giving the bankruptcy court jurisdiction, and have the real property liquidated in a U.S. bankruptcy proceeding. The proceeds would probably be distributed in a separate U.S. administration concurrent with the foreign proceedings. *See* 11 U.S.C. § 303(k) (Supp. IV 1980).

160. HOUSE REPORT, *supra* note 71, at 325; SENATE REPORT, *supra* note 71, at 35.

161. 11 U.S.C. § 304(b)(1) (Supp. IV 1980).

162. HOUSE REPORT, *supra* note 71, at 324; SENATE REPORT, *supra* note 71, at 35.

because it would be a more effective way to preserve the estate. A temporary stay of lien enforcement would hardly prevent dismemberment of the estate, since local creditors would be free to continue their efforts when the stay is lifted.

But once again, if past case law is to have any effect on the application of the statute, there may be limits on the powers of the court under section 304. Courts in the United States have traditionally refused to allow a representative of foreign bankruptcy proceedings to take local property of the debtor that has been attached by American creditors.¹⁶³ This tradition could cause the bankruptcy court to decide that for the purposes of section 304 the foreign bankruptcy estate does not include U.S. property attached by local creditors.

Perhaps the strongest support for this view is the early legislative history of the Bankruptcy Reform Act. The notes accompanying section 4-103 of the Commission bill said that the proposed ancillary proceedings did not "override the general American rule of conflict of laws that foreign trustees may not defeat rights acquired by local creditors through levy on local assets."¹⁶⁴ The drafters suggested instead that if it is necessary to avoid a transfer that occurred before relief is sought under this section, the foreign representative should commence an involuntary case.¹⁶⁵ This advice seems to contradict the statement in the same paragraph that the injunctive powers available in an ancillary case "*will enable the foreign trustee to protect the estate against dismemberment by local actions in this country without the necessity of commencing a bankruptcy or rehabilitation case under this Act.*"¹⁶⁶

These statements in the Commission bill should, however, be balanced, against the fact that neither the statute as enacted, nor the most recent legislative history placed specific restrictions on the bankruptcy court's powers to grant relief under section 304. Instead, the most recent legislative history suggested that "the court be permitted to make the appropriate orders under all of the circumstances of each case, rather than being provided with inflexible rules."¹⁶⁷

Additionally, section 304(c)(3) advises the court to guard against "preferential or fraudulent dispositions of the property of the estate."¹⁶⁸ The U.S. Court of Appeals warned that the abstention provisions in the Bankruptcy Act were not intended to be used "for the purpose of vali-

163. See *supra* text accompanying notes 29-35.

164. COMMISSION BILL, *supra* note 41, at § 4-103 n.3.

165. *Id.*

166. *Id.*

167. HOUSE REPORT, *supra* note 71, at 324-25; SENATE REPORT, *supra* note 71, at 35.

168. 11 U.S.C. § 304(c)(3) (Supp. IV 1980).

dating preferential transfers to United States nationals."¹⁶⁹ The court also said that the Bankruptcy Act permits the United States segment of an international bankruptcy to act essentially as an instrument to set aside preferences.¹⁷⁰

This analysis is based on the premise that section 304 is meant to be self-contained. There appears to be no need for reference to other sections of the Code because the legislative history shows that initiating an ancillary case under section 304 does not commence a full bankruptcy case under the Code, and because section 304 provides powers that effectively duplicate the automatic stay and avoidance powers found elsewhere in the Code.

Nevertheless, one bankruptcy court has evidently interpreted the commencement of an ancillary case under section 304 to be analogous to the commencement of a case under sections 301, 302, and 303 because the court allowed the foreign representative who had initiated an ancillary case to file a complaint to avoid a transfer under section 547.¹⁷¹ If other courts adopt this more expansive view of the relationship between section 304 and the rest of the Code, then the question whether the foreign representative may avoid liens by local creditors will no longer be as significant as it once was.

C. Analysis of Section 305: "Abstention"

Throughout this article, section 305,¹⁷² entitled "Abstention,"¹⁷³ is discussed as an international bankruptcy provision. It is apparent, however, that its usefulness goes far beyond the context of an interna-

169. 568 F.2d at 921.

170. *Id.* at 918-19. While the *Finabank* opinion is a major precedent in the U.S. case law on the subject of international bankruptcy, it has not been without its critics. "If one is to applaud judicial treaty-making there is much to admire in the result, but it is not without heavy pounding at refractory bankruptcy rules that the court shapes its reversal." *Letter*, *supra* note 134, at 728.

171. *In re Comstat Consulting Services, Ltd.*, 10 B.R. 134 (Bankr. S.D. Fla. 1981).

172. 11 U.S.C. § 305 (Supp. IV 1980).

173. § 305. Abstention

(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.

11 U.S.C. § 305 (Supp. IV 1980).

tional bankruptcy case.¹⁷⁴ The grounds for abstention contained in subsection (a)(1) are so broad that they apply in any bankruptcy case. In fact, because international bankruptcies are much less common than their domestic counterparts, section 305 will always be used more often in domestic bankruptcies.¹⁷⁵

As an international provision, section 305 is the counterpart of section 304. While section 304 presupposes that there are no pending U.S. bankruptcy proceedings for the debtor, section 305 assumes that such a case has already been commenced in the United States. So while section 304 provides for initiation of special proceedings in the United States, section 305 is concerned with stopping proceedings already underway. It permits the court to dismiss or suspend proceedings in a case if "(1), the interests of creditors and the debtor would be better served by such dismissal or suspension; or (2)(A), there is a pending foreign proceeding; and (B), the factors specified in section 304(c) . . . warrant such dismissal or suspension."¹⁷⁶ The decision to dismiss or suspend may be requested by the foreign representative¹⁷⁷ or made by the court *sua sponte*.¹⁷⁸

The court may dismiss or suspend only after notice and a hearing,¹⁷⁹ which would give parties in interest the chance to contest the petition. It must be remembered, however, that under the Code's peculiar rules of construction, a requirement of "notice and a hearing" does not mean that a hearing must actually be held after notice.¹⁸⁰ The party in interest who wishes to contest the petition may have to request the hearing. The Code requires such opportunity for a hearing as is appropriate under the circumstances, but authorizes action without a hearing.¹⁸¹ If the foreign representative gives proper notice of the peti-

174. This section has generated a large volume of case law since the Code became effective in 1979, but none of the cases involved debtors who were the subject of foreign proceedings. *See, e.g., In re St. Matthew Lutheran Church*, 1 Collier's Bankruptcy Cases (C.B.C.) 2d 682 (Bankr. C.D. Cal. 1980); *In re Sun World Broadcasters*, 5 B.R. 719 (Bankr. M.D. Fla. 1980); *In re Co Petro Marketing Group*, 6 B.R. 119 (Bankr. C.D. Cal. 1980); *In re Fast Food Properties*, 5 B.R. 539 (Bankr. C.D. Cal. 1980).

175. This is ironic in that the broader provisions in subsection (a)(1) seem almost an afterthought. The only abstention provision in the Bankruptcy Act, section 2a(22), applied strictly to international bankruptcy cases. Section 305 of the Bankruptcy Code evolved in the drafting process from section 4-103 of the COMMISSION BILL, which also dealt only with international bankruptcies. Only in later drafts of the Bankruptcy Reform Act was the abstention power broadened to make it applicable in domestic bankruptcies. *See supra* note 43.

176. 11 U.S.C. § 305(a) (Supp. IV 1980).

177. *Id.* § 305(b).

178. *See Id.* § 305(a). *In re Coram Graphic Arts*, 11 B.R. 641 (Bankr. E.D. N.Y. 1981); *In re Fast Food Properties, Ltd.*, 5 B.R. 539 (Bankr. C.D. Cal. 1980).

179. 11 U.S.C. § 305(a) (Supp. IV 1980).

180. *Id.* § 102(1).

181. *Id.*

tion for relief, and if an opposing party does not "timely" request a hearing, or if there is "insufficient time" for a hearing, relief under section 305 may be entered *ex parte*.¹⁸² Also, a decision by the court to dismiss or to suspend, or to refrain from doing so, is final and may not be reviewed on appeal.¹⁸³

The legislative history explained that at common law a court with jurisdiction over a particular matter was required to take jurisdiction. Section 305 recognizes that there will be situations in which the court should decline jurisdiction.¹⁸⁴ It seems a better argument that as a court of equity the bankruptcy court has an inherent right to dismiss or to suspend an entire case or any proceedings therein.¹⁸⁵ Section 305 is merely a codification of this inherent power. This section has additional precedent in section 2a(22)¹⁸⁶ of the Bankruptcy Act.

Sections 304 and 305 are complementary and can be used separately or together, depending on the circumstances. If past experience is any indication,¹⁸⁷ creditors will probably commence a U.S. bankruptcy case soon after the debtor is forced into bankruptcy abroad.¹⁸⁸ Thus a foreign representative will often have to seek relief under section 305. If the debtor is in reorganization abroad, the foreign representative may have to do no more than have U.S. proceedings suspended or dismissed in deference to the plan of arrangement being negotiated abroad. If the debtor's estate is being liquidated in the foreign proceedings, and the foreign court does not want a concurrent liquidation by the U.S. court of the debtor's U.S. assets, the foreign representative may have to use section 304 in conjunction with section 305: first petition the court to have U.S. bankruptcy proceedings suspended or dismissed under section 305, then begin an ancillary case to

182. *Id.*

183. *Id.* § 305(c).

184. HOUSE REPORT, *supra* note 71, at 325; SENATE REPORT, *supra* note 71, at 35. An abstention by the court under section 305 is of jurisdiction over the entire case. Abstention from a particular proceeding in a case is governed by 28 U.S.C. § 1471(d) (Supp. IV 1980).

185. Securities and Exch. Comm. v. United States Realty and Improvement Corp., 310 U.S. 434, 455 (1940).

A court of equity may in its discretion in the exercise of the jurisdiction committed to it grant or deny relief upon the performance of a condition which will safeguard the public interest. It may . . . even withhold relief altogether, and it would seem that it is bound to stay its hand in the public interest when it reasonably appears that the private right will not suffer.

Id. See also *In re Coram Graphic Arts*, 11 B.R. 641 (Bankr. E.D. N.Y. 1981); *In re Fast Food Properties, Ltd.*, 2 C.B.C. 2d 1159, 5 B.R. 539 (Bankr. C.D. Cal. 1980).

186. See *supra* note 40.

187. See generally Nadelmann, *Rehabilitating*, *supra* note 15, for a discussion of the recent foreign bank cases. See also note 198 *infra*.

188. Creditors will still have to begin an involuntary bankruptcy case when dealing with a foreign debtor. The streamlined procedures of section 304 are available only to a foreign representative. See *supra* note 77.

request a turnover of the local assets.¹⁸⁹

D. Related Sections

1. *Section 303(b)(4)*. Commencing an ancillary case is not the only choice open to the foreign representative. Under section 303(b)(4)¹⁹⁰ the foreign representative is given standing to commence an involuntary case against the debtor. This would begin a full bankruptcy case in the United States concurrent with the foreign proceedings. The debtor's local assets would be administered by the U.S. bankruptcy court in the same manner as any other case.

The foreign representative may bring an involuntary petition without the usual three or more petitioning creditors.¹⁹¹ The foreign representative would have to show, however, that the debtor qualifies for relief in an involuntary bankruptcy. The grounds for such relief are (1) the debtor is generally not paying debts as they become due; or (2) within 120 days before filing of the petition, a custodian was appointed to take possession of the debtor's property to enforce a lien against that property.¹⁹² The most commonly used grounds for involuntary relief is the first one, failure to pay debts as they become due.

This requirement is significant because the foreign representative must show that the debtor is eligible for bankruptcy relief under U.S. law, not under the law of the foreign jurisdiction. It is not sufficient that the debtor is already the subject of bankruptcy proceedings in the foreign court and meets the requirements for bankruptcy relief in that jurisdiction. So, conceivably, a foreign representative could qualify for relief under sections 304 and 305 because the debtor is the subject of foreign proceedings and has property or place of business in the United States, but be unable to begin an involuntary bankruptcy proceeding under section 303 because the debtor does not meet the requirements in section 303(h).

The status of property of the estate might create a problem because

189. Although in *Finabank* the Court of Appeals found the turnover power to be implicit in the old "abstention" statute, section 2a(22), such a construction is not applicable to section 305. Since there was no express provision in the Bankruptcy Act for a turnover power, the court construed it to be part of the only related section in the Act, section 2a(22). In the Bankruptcy Code, Congress has expressly provided for turnover of assets and has allowed its use only with the procedures in section 304. See 11 U.S.C. § 304 (Supp. IV 1980).

190. "§ 303. Involuntary cases

(b) An involuntary case is commenced by the filing with the bankruptcy court of a petition under Chapters 7 or 11 of this title—

(4) by a foreign representative of the estate in a foreign proceeding concerning such person." 11 U.S.C. § 303(b) (Supp. IV 1980).

191. See *Id.* § 303(b)(1).

192. *Id.* § 303(h).

the statute purports to give control of all of the debtor's assets to the bankruptcy court or its trustee, even if the property is located outside the United States.¹⁹³ If the bankruptcy court's jurisdiction over the debtor is based strictly on the presence of the debtor's property in the United States, or on the presence of the debtor's place of business in the United States, few foreign courts would recognize bankruptcy court jurisdiction over property outside the United States.¹⁹⁴ Also, if the debtor is already the subject of foreign bankruptcy proceedings, a U.S. bankruptcy court could not claim jurisdiction over assets already controlled by a foreign court. But creditors who receive payment in the foreign proceedings would be limited in their ability to partake in the U.S. distribution by the provisions of section 508.¹⁹⁵

Under the Bankruptcy Act, the foreign representative did not have standing to begin an involuntary case.¹⁹⁶ The only apparent reason for changing this in the Bankruptcy Code is to give the representative the greatest possible flexibility in administering the debtor's U.S. assets. He can now do directly what before he could do only indirectly through friendly creditors. In most situations, the representative would want to use the simpler procedures in section 304 rather than begin a regular involuntary case.

2. *Section 303(k)*. This subsection¹⁹⁷ brings foreign banks with assets in the United States, but not doing business here, within the coverage of the Bankruptcy Code.¹⁹⁸ It allows a creditor to file an involun-

193. Commencement of a case under section 303 creates an estate comprised of all legal and equitable interests of the debtor in property *wherever located*. *Id.* § 541(a)(1).

194. DALHUISEN, *supra* note 2, at 3-248; Nadelmann, *Bankruptcy Jurisdiction: News from the Common Market and a Reflection for Home Consumption*, 56 AM. BANKR. L.J. 65, 68-70 (1982).

195. *See infra* text accompanying notes 205-09.

196. An involuntary case could only be initiated by three or more creditors of the bankrupt. Bankruptcy Act § 59, 11 U.S.C. § 95 (1976) (repealed 92 Stat. 2682 § 401(a) (1978)).

197. "§ 303. Involuntary Cases

(k) Notwithstanding subsection (a) of this section, an involuntary case may be commenced against a foreign bank that is not engaged in such business in the United States only under Chapter 7 of this title and only if a foreign proceeding concerning such bank is pending." 11 U.S.C. § 303(k) (Supp. IV 1980).

198. A number of foreign and U.S. banks engaged in currency speculation suffered huge losses when the 1973 Arab oil embargo caused wild currency fluctuations. When some of the foreign banks (Bankhaus I.D. Herstatt KGaA i.L., Israel-British Bank (London), Ltd. and Banque de Financement, S.A.) were forced into bankruptcy at home, creditors in the United States immediately attached millions of dollars that the banks kept on deposit at correspondent banks in New York. The bankrupts and creditors without attachments attempted to void the attachments by filing bankruptcy petitions in the United States. Although the Bankruptcy Act gave jurisdiction over nonresidents with property in the United States, it excepted banks from its coverage. Bankruptcy Act § 4(b), 11 U.S.C. § 22 (1976) (repealed 92 Stat. 2682 § 401(a) (1978)).

The *Herstatt* case was settled out of court, but in *In re Israel-British Bank (London), Ltd.*, 1 BANKR. CT. DEC. 528 (S.D.N.Y. 1974), *rev'd.*, 401 F. Supp. 1159 (S.D.N.Y. 1975),

tary petition against such a bank only if the bank is already the subject of foreign proceedings. The representative of the foreign proceedings may also petition for involuntary relief for the bank. The drafters felt that commencement of a bankruptcy case in the United States would only be proper if similar proceedings had already begun in a foreign jurisdiction.¹⁹⁹ Otherwise, creditors could effectively close the bank down by tying up its U.S. assets in a bankruptcy case.

A foreign bank with assets in the United States but not doing business here can petition for voluntary relief in the U.S. bankruptcy courts, however. It is only involuntary bankruptcy that is restricted. Also, this section does not affect a foreign bank doing business in the United States. Such a bank can be a "debtor"²⁰⁰ and qualifies for both voluntary and involuntary relief under the Bankruptcy Code.

3. *Section 306.* Section 306²⁰¹ allows the foreign representative to make an appearance in the bankruptcy court to seek relief under sections 303, 304, or 305, without subjecting himself to the jurisdiction of other courts. The section is designed to prevent "jurisdiction by ambush" in which local creditors would commence an involuntary bankruptcy case, requiring the foreign representative to appear, then obtaining jurisdiction over him in connection with other suits in this

rev'd. sub. nom. Israel-British Bank (London), Ltd. v. Federal Deposit Ins. Corp., 536 F.2d 509 (2d Cir.), *cert. denied*, 429 U.S. 978 (1976), the issue of the Act's applicability to foreign banks was decided. The bankruptcy court held that the bank exclusion clause did not apply, finding no Congressional intent to exclude foreign banks, which were subject to neither state nor federal regulation. The district court reversed, but the Second Circuit Court of Appeals affirmed the decision of the bankruptcy court. Section 303(k) codifies the result in the *Israel-British Bank (London), Ltd.* case and makes it clear that foreign banks are subject to the bankruptcy laws of the United States in some situations. See generally Becker, *Transnational Insolvency Transformed*, 29 AM. J. COMP. L. 706 (1981); BECKER, *International Insolvency: The Case of Herstatt*, 62 A.B.A.J. 1290 (1976); Nadelmann, *Rehabilitating, supra* note 15; Comment, *United States Bankruptcy Jurisdiction Over Unregulated Foreign Banks*, 17 HARV. INT'L L.J. 359 (1976); *Israel-British Bank (London), Ltd.*, 52 AM. BANKR. L.J. 369 (1978); 10 VAND. J. TRANS. L. 163 (1977). The other bank case, *In re Banque de Financement, S.A.*, is discussed *supra* text accompanying notes 103-11.

199. HOUSE REPORT, *supra* note 71, at 324; SENATE REPORT, *supra* note 71, at 35. The drafters were evidently concerned that because a foreign bank not doing business in the United States is not subject to regulation by the state or federal governments, it should not be subject to involuntary bankruptcy under U.S. bankruptcy laws. Honsberger, *Conflict of Laws, supra* note 59, at 640.

200. 11 U.S.C. § 109 (Supp. IV 1980).

201. § 306. Limited Appearance

An appearance in a bankruptcy court by a foreign representative in connection with a petition or request under sections 303, 304 or 305 of this title does not submit such foreign representative to the jurisdiction of any court in the United States for any other purpose, but the bankruptcy court may condition any order under sections 303, 304 or 305 of this title on compliance by such foreign representative with the orders of such bankruptcy court.

Id. § 306.

country.²⁰² The protection of section 306 enables the foreign representative to seek relief from the bankruptcy court without fear of meeting a process-server at the courthouse door.²⁰³

Section 306 also allows the bankruptcy court to condition any relief under sections 303, 304, or 305 on compliance by the foreign representative with orders of the court. This merely restates an inherent power of the court; it is also implicit in the powers granted by section 105.²⁰⁴

4. *Section 508(a)*.²⁰⁵ This is the so-called "marshalling"²⁰⁶ provision, which was codified as section 65(d)²⁰⁷ in the Bankruptcy Act. It is designed to ensure equal distribution to creditors when the debtor's estate is administered in more than one jurisdiction. Subsection (a) provides that if a creditor receives partial satisfaction of his claim in a foreign proceeding, the creditor may not receive any payment in the U.S. distribution until all other creditors of the same class or priority level²⁰⁸ have received as much as the creditor received abroad. This is an application of what had traditionally been called the "hotchpot rule."²⁰⁹

202. HOUSE REPORT, *supra* note 71, at 325-26; SENATE REPORT, *supra* note 71, at 37. In the only reported case involving section 306, the bankruptcy court mistakenly cited section 306 as authority for ruling that a creditor had entered a "limited appearance" to contest jurisdiction in a case. *In re Ohnstead*, 1 C.B.C. 2d 494 (Bankr. D. S.D. 1980). Section 306 clearly applies only to a foreign representative appearing to request relief under sections 303, 304 or 305. See 11 U.S.C. § 306 (Supp. IV 1980); HOUSE REPORT, *supra* note 71, at 325-26; SENATE REPORT, *supra* note 71, at 37.

203. The absence in the COMMISSION BILL of such protection for the foreign representative was criticized during the committee hearings on the bill. See *Hearings on H.R. 31, supra* note 7, at 1517-18 (statement of Bernard Shapiro).

204. See 11 U.S.C. § 105 (Supp. IV 1980).

205. § 508. Effect of distribution other than under this title

(a) If a creditor receives, in a foreign proceeding, payment of, or a transfer of property on account of, a claim that is allowed under this title, such creditor may not receive any payment under this title on account of such claim until each of the other holders of claims on account of which such holders are entitled to share equally with such creditor under this title has received payment under this title equal in value to the consideration received by such creditor in such foreign proceeding.

Id. § 508(a) (Supp. IV 1980).

206. See Nadelmann, *National Bankruptcy Act, supra* note 2, at 1049-51. Marshalling of assets in this sense means that when a creditor is able to satisfy his claim from assets distributed by a foreign court and by a U.S. court, and does receive a dividend in the foreign proceedings, other creditors who were unable to claim in the foreign proceedings will be paid in the U.S. proceedings before the creditor who had the chance to satisfy his claim from other sources. See BLACK'S LAW DICTIONARY 878 (5th ed. 1979).

207. Bankruptcy Act § 65(d), 11 U.S.C. § 105(d) (1976) (repealed 92 Stat. 2682 § 401(a) (1978)).

208. For priority levels and classes, see 11 U.S.C. §§ 507, 726 (Supp. IV 1980).

209. CHESHIRE & NORTH, *supra* note 9, at 565-66. This policy is also followed by the British courts. DICEY & MORRIS, *supra* note 9, at 682-83. Under West German law, however, creditors are allowed to keep whatever assets of the debtor they manage to collect

5. *Section 1474.*²¹⁰ This section governs venue in ancillary cases brought under section 304. It provides that where relief is sought to enjoin an action in state or federal court, the ancillary case must be commenced in the bankruptcy court for the district in which the state or federal court sits.²¹¹ An ancillary case seeking to enjoin the enforcement of a lien against property or to require turnover of the property must be brought in the bankruptcy court for the district in which the property is located.²¹² Otherwise, an ancillary case must be brought in the bankruptcy court for the district in which the debtor's principal assets are located.²¹³

IV. CONCLUSION

The legislative history shows that Congress wanted to make it easier for U.S. bankruptcy courts to cooperate with foreign insolvency proceedings, and to defer to them if necessary. Thus, Congress established the special procedure in section 304 by which a foreign representative could easily obtain relief in a U.S. bankruptcy court.²¹⁴

abroad and do not have to account for it before claiming in the local bankruptcy proceedings. DALHUISEN, *supra* note 2, at 3-156.

210. § 1474. Venue of cases ancillary to foreign proceedings

(a) A case under section 304 of title 11 to enjoin the commencement or continuation of an action or proceeding in a State or Federal court, or the enforcement of a judgment, may be commenced only in the bankruptcy court for the district where the State or Federal court sits in which is pending the action or proceeding against which the injunction is sought.

(b) A case under section 304 of title 11 to enjoin the enforcement of a lien against property, or to require turnover of property of an estate, may be commenced only in the bankruptcy court for the district in which such property is found.

(c) A case under section 304 of title 11, other than a case specified in subsection (a) or (b) of this section, may be commenced only in the bankruptcy court for the district in which is located the principal assets in the United States, of the estate that is the subject of such case.

28 U.S.C. § 1474 (Supp. IV 1980).

211. *Id.* § 1474(a) (Supp. IV 1980). One effect of this venue provision seems to be that if actions are pending against the debtor or his property in more than one location, such as suits in courts in New York and Chicago, the foreign representative would have to begin separate ancillary cases in the bankruptcy courts for the Southern District of New York and the Northern District of Illinois. 1 COLLIER ON BANKRUPTCY ¶ 3.02, at 3-194 (15th ed. 1981).

212. 28 U.S.C. § 1474(b) (Supp. IV 1980).

213. *Id.* § 1474(c). The final House and Senate bills had included the debtor's principal place of business in the United States as an alternative place of venue of subsection (c). The removal of this provision from the law as enacted reduced the number of places an ancillary case can be commenced. See H.R. 8200, 95th Cong., 1st Sess. (1977); S. 2266, 95th Cong., 1st Sess. (1977).

214. Some commentators have made the argument that Congress does not have the power to enact this kind of statute, and that the provisions of section 304 may be unconstitutional. They suggest that the recognition of claims arising under foreign law exceeds the power granted Congress by the bankruptcy clause of the U.S. Constitution; that the bankruptcy clause presumes a domestic bankruptcy interest; and that the power to recognize

Consistent with this Congressional intent, there should be an initial presumption in favor of granting the relief requested by the foreign representative.²¹⁵ The statute, in effect, makes the representative's *prima facie* case for relief. Such a presumption should be easily defeated, however, by a showing that granting the relief would violate the letter or the spirit of one or more of the guidelines in section 304(c).²¹⁶

The changes in the law are significant for several reasons. They will simplify the complex administration of a multinational bankruptcy. Even though the changes are unilateral, the Commission hoped that foreign countries would reciprocate.²¹⁷ That belief may be unrealistic,²¹⁸ but as an act that promotes international cooperation, the new law is admirable. And while a spirit of cooperation is implicit in the new law, it incorporates adequate safeguards to protect the interests of United States citizens.

The new law gives the foreign representative a federal alternative to the traditional state court remedies. These remedies are now stated explicitly by federal statute, and are no longer left to interpretation of common law precedent. In situations in which a U.S. bankruptcy case has already commenced concerning the debtor who is also the subject of foreign proceedings, the bankruptcy court has exclusive jurisdiction over the case, and original but not exclusive jurisdiction over all matters related to it.²¹⁹

The traditional American rule that a foreign bankruptcy judgment did not affect either local real property of the debtor, or property attached by local creditors,²²⁰ may greatly limit the effect of sections 304 and 305. But it was suggested here²²¹ that the bankruptcy court should

foreign judgments is reserved to the states under the Tenth Amendment. See *Hearings on H.R. 31*, *supra* note 7, at 1446-47 (statement of Prof. Kurt H. Nadelmann); Comment, *United States Bankruptcy Jurisdiction Over Unregulated Foreign Banks*, 17 HARV. INT'L L.J. 359, 390 (1976).

This argument has been unpersuasive because it depends on an extremely narrow interpretation of the scope of the bankruptcy power. The Constitution does not define the "subject of bankruptcies," but case law suggests that the bankruptcy power is broad; perhaps even broader than the commerce power. *Id.* Additional authority for section 304 can be found in the federal power over foreign commerce and foreign relations. See *Hearings on H.R. 31*, *supra* note 7, at 1515-16 (statement of Prof. Stefan A. Riesenfeld).

215. This follows also from the presumption of recognition inherent in the principle of comity. See text accompanying notes 130-40 *supra*.

216. This is consistent with the judicial discretion that is also an element of comity. Also, the bankruptcy court in *In re Egeria Societa Per Azioni di Navigazione* found that if the court should sustain any of the objections to the ancillary petition, the ancillary case must be dismissed. 20 B.R. 625, 627 (Bankr. E.D. Va. 1982). See *supra* text accompanying note 114.

217. COMMISSION BILL, *supra* note 41, § 4-103 n.2.

218. See *Hearings on H.R. 31*, *supra* note 7, at 1448 (statement of Prof. Kurt H. Nadelmann).

219. 28 U.S.C. § 1471(a)-(b) (Supp. IV 1980).

220. See *supra* text accompanying notes 29-35.

221. See *supra* text accompanying notes 151-71.

not be bound absolutely by such rules. The legislative history of the law instead emphasizes that the court should have the flexibility to make a decision based on the circumstances of each case,²²² unhindered by inflexible rules developed to meet the needs of a different era.

Ultimately, the international provisions of the Bankruptcy Code are the embodiment of a theme stated by the Court of Appeals for the Second Circuit in the *Finabank* opinion:

[T]he goal of equality of distribution of assets in the international context. . . . requires . . . first, a recognition of the fact that international bankruptcies can raise problems not contemplated by the [Bankruptcy] Act, and then, some flexibility in responding to those problems consistent with the strong public policy that is at the core of the Act.²²³

While this goal may be a difficult one to achieve, the international provisions of the new U.S. Bankruptcy Code are definitely a step in the right direction.

222. HOUSE REPORT, *supra* note 71, at 324-25; SENATE REPORT, *supra* note 71, at 35.

223. 568 F.2d at 919.

Editor's Note:

The following article was accepted for publication prior to the United States Supreme Court's decision in the In re Alien Children Education Litigation cases. (Plyler v. Doe, 102 S. Ct. 2382 (1982) (5-4 decision)). That decision did not, as was urged by the authors of this article, favor the position taken by the State of Texas. Justice Brennan's majority opinion struck down the Texas statute that barred the admission of illegal alien children to public schools. The Plyler decision focused on the failure of the State to establish that it had "substantial state interests" which could support the statute. Absent such a showing, the Court held that the Texas statute violated the Equal Protection Clause of the Fourteenth Amendment.