



# Chapter 15 of the U.S. Bankruptcy Code: Ancillary and Cross-Border Cases

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## **Summary**

The Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 added chapter 15 to the U.S. Bankruptcy Code. Chapter 15 implements the United Nations Commission on International Trade and Investment's Model Law on Cross-Border Insolvency. In so doing, chapter 15 (1) retains the Code's focus on the role of the foreign representative, initially introduced in 1978; (2) clarifies procedural cooperation between U.S. and foreign courts; and (3) promotes comity and reciprocity, wherever possible, with respect to the interpretation and application of substantive law. Chapter 15 applies to international bankruptcy cases involving individuals or businesses; however, multinational banks and corporations have had a higher profile. This report summarizes the evolution and the content of chapter 15.

This report was prepared by Georgine Kryda, Law Clerk, under the general supervision of (name redacted), Legislative Attorney.

## Contents

Introduction .....	1
Evolution of Chapter 15 .....	1
Three Critical Cases in the Mid-1970s.....	2
The Bankruptcy Reform Act of 1978.....	5
The U.S. Bankruptcy Code from 1978 to the BAPCPA.....	6
Development of the Model Law .....	7
Content of Chapter 15 .....	9
Definitions .....	9
Application for Recognition .....	10
Recognition of Main and Ancillary Proceedings .....	10
Treatment of Creditors .....	11
Cooperation and Coordination.....	12
Conclusion.....	13

## Contacts

Author Contact Information .....	13
Acknowledgments .....	13

## Introduction

Chapter 15 of the U.S. Bankruptcy Code, 11 U.S.C. §§ 1501-1532, was enacted pursuant to the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 (BAPCPA).<sup>1</sup> It was designed to facilitate cooperation between U.S. and foreign courts and to clarify administration of three types of international insolvency proceedings: (1) full or “main” bankruptcy proceedings, commenced either in the U.S. with cooperation sought from foreign courts or vice versa; (2) ancillary proceedings, such as limited requests to administer specific assets under U.S. jurisdiction; and (3) requests to suspend or dismiss U.S. proceedings so as to avoid conflicts with foreign proceedings already in progress. Provisions addressing these situations in current law first appeared in the Bankruptcy Reform Act of 1978<sup>2</sup> and were codified primarily at 11 U.S.C. §§ 303-306. In response to practitioner requests for greater multilateral cooperation, from 1994 to 1997 the United Nations Commission on International Trade Law (UNCITRAL) developed a Model Law on Cross-Border Insolvency (Model Law).<sup>3</sup> The BAPCPA implemented the Model Law by adding chapter 15 to the Code.<sup>4</sup> Chapter 15 replaced 11 U.S.C. § 304, which was repealed; modified 11 U.S.C. §§ 303, 305, and 306; and addressed other concerns. This report summarizes the evolution and content of chapter 15.

## Evolution of Chapter 15

All international insolvency cases possess a tension between the: (1) principal objective of the insolvency proceeding, which is to preserve the maximum value of the debtor’s assets wherever those assets are located, and (2) jurisdictional reach of a state or nation’s enforcement powers, which is limited to territorial borders. Cooperation between courts of different jurisdictions is essential to efficiently identify, preserve, manage, and allocate the debtor’s dispersed assets. Such cooperation between courts is called “comity” or “reciprocity” and may be procedural or substantive in form.

Comity is the voluntary consideration of laws or judicial decisions made in another jurisdiction. Reciprocity is the recognition and enforcement of laws, privileges, or judicial decisions made in another jurisdiction. In cross-border insolvency proceedings, procedural cooperation can give the foreign creditor or trustee: (1) the right to appear and request that the host court declare a debtor insolvent, (2) the ability to enforce a foreign court order for turnover of assets in the host jurisdiction, and (3) assurance that the assets within the host jurisdiction will be preserved until a final ruling is issued. Procedural cooperation also involves communication (e.g., notifying creditors of proceedings and deadlines, exchanging transcripts and documentation, updating other courts with new information, overseeing administration of reorganization or liquidation plans).

Substantive cooperation has been the principal obstacle for foreign creditors and trustees who may find their claims unrecognized by the host court or subordinated to those of domestic parties in interest. U.S. creditors and trustees encountered such problems abroad. Likewise, foreign creditors and trustees found their claims against a debtor’s assets impacted by U.S. state

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<sup>1</sup> P.L. 109-8, 119 Stat. 23 (April 20, 2005).

<sup>2</sup> P.L. 95-598, 92 Stat. 2549 (November 6, 1978).

<sup>3</sup> UNCITRAL, *1997-UNCITRAL Model Law on Cross-Border Insolvency with Guide to Enactment* [http://www.uncitral.org/uncitral/en/uncitral\\_texts/insolvency/1997Model.html](http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency/1997Model.html).

<sup>4</sup> Title VIII of P.L. 109-8, 119 Stat. 134.

statutes—depending on the nature of the claim (e.g., wages, mortgages) or by its timing (e.g., local parties in interest usually were the first to file their claims)—rather than participating in a single pro rata distribution among all parties who filed claims by a set deadline.

In the late 19<sup>th</sup> and early 20<sup>th</sup> centuries, several nations entered into bankruptcy treaties or held international conferences in order to facilitate the handling of concurrent bankruptcies in multiple jurisdictions.<sup>5</sup> The U.S. did not enter into these treaties, opting instead to maximize judicial discretion for the relatively few international insolvency cases that U.S. courts encountered.<sup>6</sup> This ad hoc system existed until three high-profile cases in the mid-1970s gave impetus to the 1978 reforms regarding international insolvency.<sup>7</sup> The discussion below summarizes the developments from the mid-1970s through 2005 that led to the enactment of chapter 15.

### Three Critical Cases in the Mid-1970s

Three high-profile cases gave impetus to the enactment of 11 U.S.C. §§ 303-306 in 1978. These cases involved foreign banks that were declared insolvent abroad but held assets in the U.S.<sup>8</sup> Prior to 1978, “[f]oreign banks desiring to establish a direct U.S. presence obtained state licenses”<sup>9</sup> and fell under separate rules for insolvent banks. However, none of the three banks (Herstatt,<sup>10</sup> IBB,<sup>11</sup> or Finabank<sup>12</sup>) had a direct presence in the U.S. None had an office or had done business in the U.S.; they only had accounts with major U.S. banks in order to settle foreign exchange contracts. Were the three entities banks or corporations under U.S. law? Confusion arose because the foreign banks’ structure did not clearly correspond to U.S. forms of business organization (e.g., corporation, partnership).

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<sup>5</sup> See Kurt H. Nadelmann, *Bankruptcy Treaties*, 93 U. PA. L. REV. 58 (1944). See also, Jan Hendrik Dalhuisen, DALHUISEN ON INTERNATIONAL INSOLVENCY AND BANKRUPTCY (New York: M. Bender, 1980—).

<sup>6</sup> *Hilton v. Guyot*, 159 U.S. 113 (1895), is the U.S. Supreme Court decision which is generally interpreted to extend formal recognition of comity and reciprocity by U.S. courts to foreign courts. Yet, states such as California and New York were not bound by the doctrine if their statutes did not recognize reciprocity. See Willis L. M. Reese, *The Status in This Country of Judgments Rendered Abroad*, 50 COLUM. L. REV. 783, 790 n.39 (1950).

<sup>7</sup> The Congress appointed a bankruptcy review commission in 1970. P.L. 91-354, 84 Stat. 468 (July 24, 1970). The Commission on Bankruptcy Laws filed its report in 1973. REPORT OF THE COMMISSION ON BANKRUPTCY LAWS, H.R. DOC. NO. 137, parts I and II, 93d Cong., 1<sup>st</sup> Sess. (1973). However, legal scholars usually cite these three cases as the genesis for the 1978 reforms regarding international insolvency. See Kurt H. Nadelmann, *Rehabilitating International Bankruptcy Law: Lessons Taught by Herstatt and Company*, 52 N.Y.U. L. REV. 1 (1977).

<sup>8</sup> Domestic banks are not eligible to file under the U.S. Bankruptcy Code. 11 U.S.C. § 109(b)(2).

<sup>9</sup> Joseph J. Norton & Christopher D. Olive, *A By-product of the Globalization Process: The Rise of Cross-Border Bank Mergers and Acquisitions—The U.S. Regulatory Framework*, 56 BUS. LAW. 591, 596 n.23 (2001) (citing U.S. GENERAL ACCOUNTING OFFICE, FOREIGN BANKS: ASSESSING THEIR ROLE IN THE U.S. BANKING SYSTEM 47 (GAO/GGD-96-26, 1996)).

<sup>10</sup> *In re Bankhaus I.D. Herstatt KGaA i.L. (Herstatt)*, Bankruptcy No. 74-1134 (S.D.N.Y. involuntary bankruptcy petition filed on Aug. 6, 1974, dismissal order issued May 7, 1975). See Joseph D. Becker, *Transnational Insolvency Transformed*, 29 AM. J. COMP. L. 706, 707 (1981).

<sup>11</sup> *In re Israel-British Bank (London) Ltd., (IBB)*, 1 BANKR. CT. DEC. 428 (S.D.N.Y. 1974), *rev'd* 401 F. Supp. 1159 (S.D.N.Y. 1975), *rev'd sub. nom. Israel-British Bank (London) Ltd. v. Federal Deposit Ins. Corp.*, 536 F.2d 509 (2d Cir. 1976), *cert. denied*, 429 U.S. 978 (1976).

<sup>12</sup> *In re Banque de Financement, S.A. (Finabank)*, 2 BANKR. CT. DEC. 83 (S.D.N.Y. 1976), *aff'd* No. 75 B764 (S.D.N.Y. 1976), *rev'd sub. nom. Banque de Financement v. First National Bank of Boston*, 568 F.2d 911 (2d Cir. 1977).

The central issue in all three cases was whether the foreign bank was covered by or exempt from the predecessor to the 1978 Bankruptcy Code, the Bankruptcy Act of 1898.<sup>13</sup> If the banks were subject to the 1898 Act, then they would be entitled to file a petition for voluntary bankruptcy, just like any other corporation, and benefit from the fact that certain claims made against their assets within four months prior to filing would be voidable preferences under U.S. law.<sup>14</sup> Voiding transactions made within four months prior to the debtor's filing was intended to promote equity among all creditors, rather than favoring those creditors who first sensed that the debtor was going to declare bankruptcy.

The 1898 Act, as amended, was silent regarding Congress' intended coverage of foreign banks. If the foreign banks were "banking corporations" under U.S. law, then they would be exempt from coverage under the 1898 Act and would be subject to the separate regime for insolvent banks.<sup>15</sup> If the banks were simply foreign corporations, akin to a partnership, then they would be eligible to file a petition under the bankruptcy law.<sup>16</sup>

Major U.S. banks attached claims to the foreign banks' U.S. accounts, arguing that the foreign banks were banking corporations, ineligible to file for bankruptcy. The three foreign banks tried to have the U.S. attachments voided and the funds turned over to their respective liquidators, each of whom had been appointed by a non-U.S. court. If the U.S. banks prevailed, their claims would have been satisfied in full, outside of bankruptcy, in the order in which their attachments had been made—until the foreign banks' assets were exhausted.<sup>17</sup> If the foreign banks prevailed, then all of the U.S. banks would be required to participate in the foreign liquidation plan in which creditors would receive pro rata distribution, most likely partial recoupment or "pennies on the dollar." Decisions by the Southern District Court for New York and the U.S. Court of Appeals for the Second Circuit regarding this central issue, and others, would inform §§ 303-306.

The American and German parties in *Herstatt* settled, but the Second Circuit issued decisions in *IBB* and *Finabank* to (1) assert the 1898 Act's coverage over foreign banks holding assets, but not doing business, in the U.S., and (2) set a tone of comity, if not reciprocity, in concurrent international insolvency proceedings. In *IBB*, the Second Circuit viewed its role "to be in aid of the order of the High Court [of England]."<sup>18</sup> In *Finabank*, the Second Circuit acknowledged the pending Swiss proceeding and noted the Swiss proceeding's stated objective to ensure an equitable outcome for all of Finabank's creditors.<sup>19</sup> Congress incorporated these criteria—the Second Circuit's sense of comity and assurance of protection of U.S. creditors—in § 304 of the Bankruptcy Reform Act of 1978.

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<sup>13</sup> 30 Stat. 544 (July 1, 1898).

<sup>14</sup> 30 Stat. 562, § 60(b) (1898).

<sup>15</sup> 30 Stat. 547 § 4(a) (1898).

<sup>16</sup> 30 Stat. 547 § 5 (1898).

<sup>17</sup> Nadelmann (1977), *supra* note 8, at 7.

<sup>18</sup> 536 F.2d at 511.

<sup>19</sup> 568 F.2d at 917.

In *IBB*, the English Receiver and Provisional Liquidator filed the voluntary bankruptcy petition in New York with the express intention of preserving IBB's U.S. assets for distribution among all of the bank's creditors. The Second Circuit not only relied on the High Court's order appointing New York counsel to file the petition, but also on the reciprocity that would exist if the situations were reversed. Under English law, an English court could void attachments made within six months prior to a petition for "winding up."<sup>20</sup>

The Second Circuit reversed the lower courts' dismissal of Finabank's chapter 11 petition and remanded the case to the bankruptcy court.<sup>21</sup> Finabank had filed the U.S. petition while a Swiss proceeding determined Finabank's prospects for rehabilitation.<sup>22</sup> (A Swiss court ultimately ordered Finabank to be liquidated.<sup>23</sup>) The petition was incomplete because Swiss banking law prohibited Finabank from revealing the names and addresses of depositors and creditors.<sup>24</sup> The Second Circuit held that Finabank's filing of the chapter 11 petition in order to frustrate the U.S. creditors' attachments was insufficient to prove that Finabank did not truly intend to seek rehabilitation,<sup>25</sup> but failure to file a complete list of creditors was fatal because that requirement had never been waived for any debtor.<sup>26</sup> "Flexibility in the international context of course should not come at the expense of the orderly administration of the [Bankruptcy] Act."<sup>27</sup> Nevertheless, the Second Circuit acknowledged that *Finabank* was atypical and opened the door to two options upon remand: (1) permitting assets in the U.S. to be administered by a Swiss proceeding, or (2) coordinating a full proceeding in the U.S. with a Swiss court.<sup>28</sup>

By the conclusion of these three cases in 1977, additional cross-border insolvency cases involving non-banks and complicated fact patterns were emerging.<sup>29</sup> The circumstances were ripe for Congress to clarify procedures for administering cross-border insolvency cases. Congress responded with §§ 303-306 of the Bankruptcy Reform Act of 1978.<sup>30</sup>

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<sup>20</sup> 536 F.2d at 511 (citing Companies Act, 11 & 12 Geo. 6, c. 38 § 320(1) (1948)).

<sup>21</sup> 568 F.2d at 922.

<sup>22</sup> *Id.* at 913.

<sup>23</sup> *Id.*

<sup>24</sup> *Id.* at 914-15.

<sup>25</sup> *Id.* at 917.

<sup>26</sup> *Id.* at 917-18.

<sup>27</sup> *Id.* at 919.

<sup>28</sup> *Id.* at 919-20.

<sup>29</sup> See e.g., *Cornfeld v. Investors Overseas Services, Ltd.*, 471 F. Supp. 1255 (S.D.N.Y. 1979), *aff'd without opinion* 614 F.2d 1286 (2d Cir. 1979); *Fluger v. Clarkson Company Ltd.*, 86 F.R.D. 388 (N.D. Tex. 1980); *Clarkson Co. Ltd. v. Shaheen*, 544 F.2d 624 (2d Cir. 1976).

<sup>30</sup> Congress also passed the International Banking Act (IBA) of 1978. P.L. 95-369, 92 Stat. 607 (September 17, 1978) (codified at 12 U.S.C. § 3101). The IBA was the first act to subject foreign banks to federal supervision. See Patricia S. Skigen & John D. Fitzsimmons, *The Impact of the International Banking Act of 1978 on Foreign Banks and Their Domestic and Foreign Affiliates*, 35 BUS. LAW. 55 (1979).

## The Bankruptcy Reform Act of 1978

Sections 303-306 of the Bankruptcy Reform Act of 1978 focused on the role of the foreign representative.<sup>31</sup> Specifically, a duly-appointed foreign representative now had standing in a U.S. court to (1) file a petition for involuntary bankruptcy against a party already involved in foreign proceedings (§ 303),<sup>32</sup> (2) file a petition for ancillary proceedings to administer U.S. assets (§ 304), or (3) request that the U.S. court suspend or dismiss its proceedings in deference to the foreign lead court (§ 305). Section 306 granted the foreign representative the right to make a limited appearance (i.e., not be subject to a court's jurisdiction for any proceeding unrelated to the bankruptcy).

Section 303 responded directly to the three banking cases. In order to thwart the use of U.S. law to force a foreign bank into bankruptcy, § 303(k) prohibited a foreign bank from being placed in bankruptcy in the U.S. unless a foreign proceeding was already pending against the bank.<sup>33</sup>

Before the enactment of § 304, a foreign representative seeking relief involving assets located in the United States had two choices: “resort to litigation in state or federal nonbankruptcy courts or subject the debtor’s estate to a full bankruptcy case.”<sup>34</sup> Section 304(c) enumerated six factors that the court could consider to determine whether to grant relief in addition to formally recognizing “principles of international comity and respect for the judgments and laws of other nations”.<sup>35</sup>

In determining whether to grant relief ... 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.<sup>36</sup>

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<sup>31</sup> P.L. 95-598, 92 Stat. 2549 (November 6, 1978). See Charles F. Miller, Jr., *Bankruptcy Reform Act Bibliography*, 85 COM. L.J. 373 (1980).

<sup>32</sup> 11 U.S.C. § 301 permitted any party that qualified as a debtor under any chapter of Title 11 to file for voluntary bankruptcy.

<sup>33</sup> 92 Stat. 2560, § 303(k). However, “only a foreign bank receives this protection. The protection does not extend to a foreign savings bank, or cooperative bank or any ‘near bank’.” John D. Honsberger, *Conflict of Laws and the Bankruptcy Reform Act of 1978*, 30 CASE W. RES. L. REV. 631, 640 (1980).

<sup>34</sup> Richard A. Gitlin & Evan D. Flaschen, *The International Void in the Law of Multinational Bankruptcies*, 42 BUS. LAW. 307, 316 (1987).

<sup>35</sup> 92 Stat. 2561, § 304(c).

<sup>36</sup> *Id.*



“The U.S. Bankruptcy Code [became] 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 in court.”<sup>37</sup> The role of the foreign representative would prove to be quite valuable, as illustrated by the Singer reorganization of 1999-2001.<sup>38</sup> The Singer Company, N.V., successor in interest to the Singer Sewing Machine Company, and 46 affiliates filed chapter 11 petitions in 1999.<sup>39</sup> The bankruptcy judge appointed two of Singer’s lawyers to act as foreign representatives, pursuing “the essential objective of ensuring that all creditors, wherever located, were treated equally.”<sup>40</sup>

The lawyers were already familiar with Singer’s situation. In their capacity as foreign representatives, they took steps to prevent local creditors from attaching Singer’s assets and to negotiate a global agreement among Singer’s creditors that leveraged the creditors’ other business relationships in the U.S.<sup>41</sup> “[N]ot once did Singer actually need to seek bankruptcy court relief with respect to potential violations of the automatic stay.”<sup>42</sup> Upon filing in bankruptcy, the automatic stay<sup>43</sup> immediately enjoins all entities from collection activities against a debtor or the debtor’s property. To be effective in international insolvency, an automatic stay imposed by a court in one country must be recognized and enforced by courts in other countries.<sup>44</sup>

Despite these provisions in the 1978 Act, the original tensions remained between the principal objective of preserving assets wherever located and the territorial limitations on courts’ jurisdiction. Lawyers, regulators, judges, and academics working in the field of bankruptcy called for improved multilateral cooperation. Their efforts led to UNCITRAL’s Model Law on Cross-Border Insolvency, which ultimately was enacted as chapter 15 of the Bankruptcy Code.

## The U.S. Bankruptcy Code from 1978 to the BAPCPA

Cross-border insolvency cases increased in their complexity. Protocols were used successfully to coordinate multiple main proceedings for multinational bankruptcies, such as Maxwell Communication Corporation PLC.<sup>45</sup> Yet, uncertainty remained regarding substantive cooperation in areas such as foreign recognition of U.S. judgments regarding chapter 11 reorganization plans and U.S. authority to pursue violations of the automatic stay.<sup>46</sup> Other countries, such as England

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<sup>37</sup> Stephen B. James, *International Bankruptcy: Limited Recognition in the New U.S. Bankruptcy Code*, 3 Hous. J. INT’L L. 241, 244 (1981).

<sup>38</sup> Evan D. Flaschen, Anthony J. Smits, & Leo Plank, *Foreign Representatives in U.S. Chapter 11 Cases: Filling the Void in the Law of Multinational Insolvencies*, 17 CONN. J. INT’L L. 3 (2001).

<sup>39</sup> *Id.* at 3; *In re Singer Company N.V.*, 262 B.R. 257 (Bankr. S.D.N.Y. 2001).

<sup>40</sup> *Id.* at 21. The authors note that, at the time of their writing, nine Chapter 11 cases had “Singer-style Foreign Representative[s]” appointed, all with similarly defined roles. *Id.* at 17.

<sup>41</sup> *Id.* at 21.

<sup>42</sup> *Id.*

<sup>43</sup> 11 U.S.C. § 362.

<sup>44</sup> *See e.g., In re Nakash*, 190 B.R. 763, 767 & 770 (Bankr. S.D.N.Y. 1996).

<sup>45</sup> Flaschen *et al.*, *supra* note 39, at 9. “Protocols, entered into during bankruptcy proceedings, may cover any range of issues. The substance of the Maxwell Protocol concerned the coordination of the two insolvency proceedings in the United Kingdom and the United States.” *Id.* *See In re Maxwell Communication Corp.*, 93 F.3d 1036, 1041-42 (2d Cir. 1996).

<sup>46</sup> *See e.g., Robert B. Chapman, Recent Developments in U.S. Bankruptcy Cases Affecting Foreign Creditors, Debtors and Assets*, 8 INT’L INSOLVENCY REV. 61 (1999).

and Canada (two of the United States' largest trade and investment partners), did not recognize discharges of indebtedness as orders of U.S. courts.<sup>47</sup> Thus, a final judgment rendered in one country might not settle the case in all jurisdictions. The following excerpt from a statement before a congressional subcommittee illustrates these problems.

In a case known as *Paolo Gucci*, we, for example, discovered real estate, very valuable real estate in England held in a Liberian corporation.... We retained solicitors only to learn that the U.S. bankruptcy and the U.S. bankruptcy trustee was not entitled to recognition [in England], the law was not clear, and that we would have to commence litigation.... Also in this *Paolo Gucci* case, during the case, post-bankruptcy, in violation of our automatic stay, a party in Korea attached valuable Korean trademarks which belonged to the estate. We are now litigating that issue in the Korean courts. Our Korean counsel advised us that our automatic stay would not be recognized and that attachment is holding up a very large sum of money which we are due to receive under a sale of assets, but we need to clear up the attachment first.<sup>48</sup>

Harmonizing substantive bankruptcy law on a global, or even regional scale, would be very difficult. Although the Europeans did not implement the European Union Regulation on Insolvency until May 2002,<sup>49</sup> their dual-approach of harmonizing international procedures while acknowledging differences in individual nation's substantive laws inspired three other multilateral initiatives to harmonize bankruptcy laws: (1) the American Law Institute (ALI)'s Transnational Insolvency Project, in conjunction with NAFTA;<sup>50</sup> (2) the International Bar Association's *Committee J Cross-Border Insolvency Concordat*;<sup>51</sup> and (3) the United Nations Conference on International Trade and Investment's (UNCITRAL's) Model Law of Cross-Border Insolvency.

## Development of the Model Law

The need for comity in international insolvency had long been acknowledged by the parties most directly involved in such proceedings, but practical considerations lay between conceptualization and implementation. UNCITRAL's decision to undertake work on cross-border insolvency was in response to suggestions made by practitioners directly concerned with the problem, particularly those expressed at the UNCITRAL Congress, "Uniform Commercial Law in the 21<sup>st</sup> Century," held in May 1992.<sup>52</sup> In April 1994, UNCITRAL and the International Association of Insolvency

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<sup>47</sup> Honsberger, *supra* note 34, at 650.

<sup>48</sup> U.S. Congress, Senate Subcomm. on Admin. Oversight and the Courts of the Comm. on the Judiciary, *Examining the Need to Make Changes to Our Bankruptcy Laws to Facilitate International Trade*, S. Hrg. 105-473, 105<sup>th</sup> Cong., 1<sup>st</sup> sess., December 4, 1977 (Washington: GPO, 1998), pp. 13-14 (statement of Jonathan L. Flaxer, Esq.).

<sup>49</sup> Council Regulation (EC No. 1346/2000) on insolvency proceedings at [http://ec.europa.eu/justice\\_home/fsj/civil/insolvency/printer/fsj\\_civil\\_1346\\_en.htm](http://ec.europa.eu/justice_home/fsj/civil/insolvency/printer/fsj_civil_1346_en.htm).

<sup>50</sup> The American Law Institute's Transnational Insolvency project promulgated "principles and procedures for managing the general default of an economic enterprise having its center of interest in a NAFTA country and having assets, creditors, and operations in more than one NAFTA country." Page 2 at <http://www.ali.org/ali/InsolvencyPrinciples.pdf>. See also Jay L. Westbrook, *The Transnational Insolvency Project of the American Law Institute*, 17 CONN. J. INT'L L. 99 (2001).

<sup>51</sup> The International Bar Association's COMMITTEE J CROSS-BORDER INSOLVENCY CONCORDAT was "prepared to provide a framework of general principles for addressing cross-border insolvencies." Page 3 at <http://www.iiiglobal.org/international/projects/concordat.pdf>.

<sup>52</sup> UNCITRAL Working Group on Insolvency Law, 18<sup>th</sup> Sess., *Cross-Border Insolvency, Possible issues relating to judicial cooperation and access and recognition in cases of cross-border insolvency*, at 3, ¶ 2, U.N. Doc. A/CN.9/WG.V/WP.42 (September 26, 1995) at [http://www.uncitral.org/pdf/english/travaux/insolvency/acn9-wg5-\(continued...\)](http://www.uncitral.org/pdf/english/travaux/insolvency/acn9-wg5-(continued...))

Practitioners (INSOL) held a Colloquium on Cross-Border Insolvency for judges, lawyers, regulators, bankers, and academics.<sup>53</sup> The Working Group on Insolvency met from 1994 to 1997 in order to achieve cooperation between courts, recognition of foreign proceedings, and access to foreign proceedings by estate representatives.<sup>54</sup>

From its inception, the Working Group recognized that “it would be desirable to harmonize ground rules in some areas of insolvency law,” ... but “that it may be unrealistic to suppose that any principle of universality of insolvency proceedings could be attained at the global, or even at the regional, level in the foreseeable future.”<sup>55</sup> Hence, the Working Group focused on harmonizing procedural rather than substantive law. The Working Group opted for a model law rather than a convention because the former offers greater flexibility.<sup>56</sup> A nation can incorporate sections of a model law and tailor it to complement its existing law, whereas ratifying and executing treaties tends to be a more formal and rigid process.

The issue of automatic stays illustrates the difficulties encountered and compromises reached in harmonizing the ground rules.

It was noted that the main purpose of the stay of individual action was to prevent the debtor’s assets from being dispersed through enforcement measures ordered in individual actions. While there was general support for the need to stay all individual actions that could lead to such a situation, different views were expressed as to how the scope of the stay ... should be defined.<sup>57</sup>

The Working Group compromised by agreeing that an automatic stay should be imposed when a court recognizes a foreign main proceeding, but should be subject “to any limitations or exceptions to a stay which occur under local law.”<sup>58</sup>

UNCITRAL approved and adopted the Model Law on May 30, 1997.<sup>59</sup> On December 15, 1997, without a vote, the U.N. General Assembly adopted Resolution 52/158 recommending that all members review their insolvency laws in light of the Model Law.<sup>60</sup> To further its objective of providing a prototype for procedural cooperation between national governments, UNCITRAL subsequently released a legislative guide. On June 25, 2004, UNCITRAL adopted its 400-page

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<sup>53</sup> *Id.* at ¶ 3. The Colloquium Report is contained in U.N. Doc. A/CN.9/398 (1994).

<sup>54</sup> S. Hrg. 105-473, *supra* note 49, at 12 (statement of Judge Tina L. Brozman).

<sup>55</sup> UNCITRAL WORKING GROUP ON INSOLVENCY LAW, 26<sup>TH</sup> SESS., *Possible Future Work, Note by the Secretariat, Addendum, Cross-border Insolvency*, at 11, ¶¶ 50-51, U.N. Doc. A/CN.9/378/Add.4 (June 23, 1993), at <http://www.uncitral.org/pdf/english/travaux/insolvency/acn9-378-add4-e.pdf>.

<sup>56</sup> UNCITRAL WORKING GROUP ON INSOLVENCY LAW, 20<sup>TH</sup> SESS., at 6, ¶¶ 16-20, U.N. Doc. A/CN.9/433 (October 24, 1996). *See also* S. Hrg. 105-473, *supra* note 49, at 39 (remarks by Harold S. Burman, Executive Dir., Advisory Comm. on Private Int’l Law, Dep’t of State).

<sup>57</sup> UNCITRAL Working Group on Insolvency Law, 20<sup>th</sup> Sess., at 28, ¶ 116, U.N. Doc. A/CN.9/433 (October 24, 1996).

<sup>58</sup> UNCITRAL Working Group Will Meet in N.Y. on Model Insolvency Law, 9 BNA BANKR. L. REPTR. No. 3 (January 16, 1997) at <http://pubs.bna.com/NWSSTND/IP/BNA/bky.nsf/SearchAllView/71A217439E99E9118525642000811480?>

<sup>59</sup> UNCITRAL, 1997 - UNCITRAL Model Law on Cross-Border Insolvency with Guide to Enactment, at [http://www.uncitral.org/uncitral/en/uncitral\\_texts/insolvency/1997Model.html](http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency/1997Model.html).

<sup>60</sup> G.A. Res. 158, U.N. GAOR, 52<sup>nd</sup> Sess., Agenda Item 148, U.N. Doc. A/RES/52/158 (1998), at <http://www.un.org/ga/documents/gares52/res52158.htm>.

Legislative Guide on Insolvency Law with the intention that it “be used as a reference by national authorities and legislative bodies when preparing new laws and regulations or reviewing the adequacy of existing laws and regulations.”<sup>61</sup> On December 2, 2004, the United Nations General Assembly passed Resolution 59/40 requesting the Secretary-General publish the legislative guidelines and endorsing further adoption of the Model Law.<sup>62</sup>

On December 4, 1997, the U.S. Senate Subcommittee on Administrative Oversight and the Courts held a hearing regarding UNCITRAL’s Model Law and other requests for reform of § 304 of the U.S. Bankruptcy Code.<sup>63</sup> Unanimous endorsements by the National Bankruptcy Review Commission and by the State Department Advisory Committee on Private International Law facilitated the introduction of UNCITRAL’s Model Law into the U.S. legislation, which culminated in its adoption through the BAPCPA. As of July 2006, the U.S. was one of 11 countries and territories with legislation based on the Model Law.<sup>64</sup>

## **Content of Chapter 15**

Chapter 15 may be divided into five categories: definitions, application for recognition, recognition of main and ancillary proceedings, treatment of creditors, and cooperation and coordination.

### **Definitions**

The BAPCPA amended several definitions. Changes to 11 U.S.C. § 101(23): (1) recognize a foreign court’s interim proceedings (not only final decisions), (2) dispense with the difficulty of defining the location of a debtor’s “principal” assets, and (3) use the terms “liquidation” and “reorganization,” which correspond directly with Chapters 7 and 11, respectively, of the U.S. Bankruptcy Code. Likewise, § 101(24) expands the definition of “foreign representative” to include any “person or entity” appointed on an interim basis to administer the liquidation or reorganization or to act as a representative.<sup>65</sup> Section 109, “who may be a debtor,” is explicitly linked with the International Banking Act of 1978 in order to maintain consistency in the definitions of banks and of bank-like enterprises covered by federal regulation.<sup>66</sup>

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<sup>61</sup> UNCITRAL, 2004 - UNCITRAL Legislative Guide on Insolvency Law, at [http://www.uncitral.org/uncitral/en/uncitral\\_texts/insolvency/2004Guide.html](http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency/2004Guide.html).

<sup>62</sup> G.A. Res. 40, U.N. GAOR, 59<sup>th</sup> Sess., Agenda Item 143, U.N. Doc. A/Res/59/40 (2004), at <http://daccessdds.un.org/doc/UNDOC/GEN/N04/478/66/PDF/N0447866.pdf>.

<sup>63</sup> The National Conference of State Legislatures asked Congress to modify § 304 of the federal Bankruptcy Code. Section 304 had allowed foreign insurance companies to remove trust fund assets (serving as collateral in the U.S.) to the foreign country and had exempted foreign insurance companies from state solvency regulations. 11 U.S.C. § 1501(d) now prohibits a court from granting relief involving any deposit/fund/security under state “insurance law or regulation for the benefit of claim holders in the United States.”

<sup>64</sup> UNCITRAL, Status, 1997—Model Law on Cross-border Insolvency, at [http://www.uncitral.org/uncitral/en/uncitral\\_texts/insolvency/1997Model\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency/1997Model_status.html).

<sup>65</sup> 11 U.S.C. § 101(24). The new § 1505 explicitly authorizes a trustee of an estate appointed by a U.S. court to act in a foreign country “in any way permitted by the applicable foreign law.” 11 U.S.C. § 1505.

<sup>66</sup> 11 U.S.C. § 109(b).

## Application for Recognition

The application for recognition of a foreign proceeding under § 1515 is the starting point for a foreign representative for any type of proceeding. Failure to file an application does not terminate the foreign representative's rights to sue or collect a claim from the debtor, but it will forestall future action.<sup>67</sup> The act of filing an application does not subject the applicant to any other U.S. jurisdiction for any other purpose.<sup>68</sup>

In filing the application for recognition, the foreign representative provides the U.S. district court<sup>69</sup> with certification, translated into English, of the foreign court's: (1) commencement of the foreign proceeding, and (2) appointment of the foreign representative.<sup>70</sup> The foreign representative must identify for the U.S. court all known foreign proceedings involving the debtor.<sup>71</sup> Section 1516 presumes: (1) the authenticity of the documents provided, and (2) that a debtor's registered office or habitual residence is the center of the debtor's main interests.<sup>72</sup>

The court may grant limited relief as soon as the petition for recognition of the foreign proceeding is filed.<sup>73</sup> Public policy concerns may override any relief;<sup>74</sup> however, few courts have relied on public policy concerns to justify denying relief. Courts that have denied relief have defined the public policy exception narrowly.<sup>75</sup>

## Recognition of Main and Ancillary Proceedings

Section 1517 covers orders granting recognition of the foreign proceeding. Such orders may be granted subject to the public policy exception described above and after notice and a hearing.<sup>76</sup> If the foreign proceeding is in the same country as the center of the debtor's interests, then the U.S. recognizes it as the foreign main proceeding; otherwise, as a foreign nonmain proceeding.<sup>77</sup> Upon recognition of a foreign main proceeding, adequate protection of the property (§ 361) and an automatic stay (§ 362) apply to the debtor's assets under U.S. territorial jurisdiction.<sup>78</sup> The foreign representative may also operate the debtor's business, including leasing or selling

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<sup>67</sup> 11 U.S.C. § 1509(f). See *United States v. J.A. Jones Construction Group, LLC*, 333 B.R. 637, 639 (E.D.N.Y. 2005) (holding that the Eastern District Court of New York had no authority to consider a foreign representative's request for a stay "[i]n the absence of recognition under chapter 15" by the bankruptcy court).

<sup>68</sup> 11 U.S.C. § 1510.

<sup>69</sup> 119 Stat. 145-46, §802(c) modified 28 U.S.C. 1334(c) to make the district court the sole starting point for an application to recognize a foreign proceeding. The district court may refer the case to a bankruptcy court under 28 U.S.C. § 157(a). The appropriate district court or venue for chapter 15 cases is determined by: (1) the debtor's principal place of business or assets in the U.S.; (2) other proceedings against a debtor without a business or assets in the U.S.; and (3) the interests of justice and convenience of the parties. 28 U.S.C. § 1410(a).

<sup>70</sup> 11 U.S.C. § 1515(b).

<sup>71</sup> 11 U.S.C. § 1515(c).

<sup>72</sup> 11 U.S.C. § 1516(b)&(c).

<sup>73</sup> 11 U.S.C. § 1519.

<sup>74</sup> 11 U.S.C. § 1506.

<sup>75</sup> *Stonington Partners, Inc. v. Lernout & Hauspie Speech Products, N.V.*, 310 F.3d 118, 127 (3d Cir. 2002).

<sup>76</sup> 11 U.S.C. § 1517(a).

<sup>77</sup> 11 U.S.C. § 1517(b). The debtor must be conducting "nontransitory economic activity" in the foreign country where the proceeding is pending. 11 U.S.C. §§ 1502 & 1517(b)(2).

<sup>78</sup> 11 U.S.C. § 1520(a)(1).

property within the territorial jurisdiction of the U.S. or making other transfers of interest under §§ 363, 549, and 552 of Title 11.<sup>79</sup> These provisions do not automatically accompany recognition of a nonmain proceeding.

Upon recognition of any foreign proceeding, the court may grant other forms of relief as it deems appropriate, either to respond to a petitioner's request or to coordinate with other proceedings.<sup>80</sup> All forms of relief are subject to the public policy exception, described above. Upon recognition of the foreign proceeding, the foreign representative in that proceeding may participate as a party in interest in any case under Title 11 regarding the debtor.<sup>81</sup>

## Treatment of Creditors

Upon recognition of any foreign proceeding, the U.S. court may entrust the debtor's assets located in the U.S. to the foreign trustee or to a third party, "provided that the court is satisfied that the interests of creditors in the United States are sufficiently protected."<sup>82</sup> Foreign and domestic creditors have the same rights to commence or to participate in a case against a debtor.<sup>83</sup> Their claims follow the same priority of claims as under §§ 507 or 726, "except that the claim of a foreign creditor under those sections shall not be given a lower priority than that of general unsecured claims without priority solely because the holder of such claim is a foreign creditor."<sup>84</sup>

When deciding whether to provide assistance to a foreign body, the U.S. court shall consider whether U.S. claim holders will be prejudiced and inconvenienced in the processing of claims abroad.<sup>85</sup> This language drew the attention of the courts in the matters of *Artimm, S.r.L.*<sup>86</sup> and *Board of Directors of Multicanal, S.A.*<sup>87</sup> The court in *Artimm* applied § 304 because the case had been filed prior to the BAPCPA taking effect on October 17, 2005; however, the court was informed by the new chapter 15's principles. "The 'provided that' language in § 1521(b) seems to make the protection of the interests of creditors in the United States a mandatory condition on the turnover of U.S. assets to a foreign representative. The language of § 304(c) is less demanding."<sup>88</sup>

The court in *Multicanal*, though, found that its authority to assist foreign representatives and to protect all claim holders "is even clearer under Chapter 15" than it had been under § 304.<sup>89</sup> *Multicanal's* board of directors initiated the ancillary proceeding in the U.S. to enjoin prosecution

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<sup>79</sup> 11 U.S.C. §§ 1520(a)(2)-(4).

<sup>80</sup> 11 U.S.C. § 1521.

<sup>81</sup> 11 U.S.C. § 1512.

<sup>82</sup> 11 U.S.C. § 1521(b).

<sup>83</sup> 11 U.S.C. § 1513(a).

<sup>84</sup> 11 U.S.C. § 1513(b)(1). The House Judiciary Committee Report on the BAPCPA noted that, "The law as to priority for foreign claims" under § 507 "is unsettled. This section permits the continued development of case law on that subject and its general principle of national treatment should be an important factor to be considered." H.R. REPT. 109-31, Part 1, 111 (2005). National treatment is the principle whereby the host nation does not discriminate against the foreign interest solely because the party is foreign.

<sup>85</sup> 11 U.S.C. § 1507(b)(2).

<sup>86</sup> 335 B.R. 149 (Bankr. C.D. Cal. 2005).

<sup>87</sup> 340 B.R. 154 (Bankr. S.D.N.Y. 2006).

<sup>88</sup> 335 B.R. at 160.

<sup>89</sup> 340 B.R. at 167.

of U.S. lawsuits and to dismiss an involuntary chapter 11 petition against the firm.<sup>90</sup> One issue in the case concerned the bankrupt Multicanal's subsequent offer to exchange securities initially purchased by U.S. investors. Section 3(a)(10) of the Securities Act of 1933 requires a fairness hearing to protect investors affected by such exchanges.<sup>91</sup> The court in *Multicanal* found that, "There is no sound reason why a foreign representative should not be entitled to seek a § 3(a)(10) fairness hearing in connection with an ancillary petition, and every reason why this relief should be available."<sup>92</sup> The court then reiterated its acknowledgment that U.S. securities law might impede a foreign restructuring; hence, a fairness hearing could simultaneously satisfy U.S. securities law (give voice to affected investors) and bankruptcy law (give assistance to foreign representatives, just treatment of all claim holders, and protection of U.S. investors during the foreign restructuring).<sup>93</sup>

## Cooperation and Coordination

Chapter 15 directs courts to cooperate with foreign courts and representatives to the maximum extent possible<sup>94</sup>—subject to the public policy exception and other specific considerations—in order “to provide effective mechanisms for dealing with cases of cross-border insolvency.”<sup>95</sup> Such cooperation may include, but is not limited to, direct communications, personnel appointments, approval or implementation of agreements, and coordination of administration, supervision, or concurrent proceedings.<sup>96</sup>

Coordination of concurrent cases considers scenarios in which: (1) cases are filed or relief is granted in the U.S. before or after recognition of a foreign proceeding, and (2) multiple foreign proceedings occur. Essentially, all relief must be consistent with the relief granted in any U.S. case.<sup>97</sup> Once the U.S. recognizes a foreign main proceeding pursuant to chapter 15, a case under another chapter of Title 11 (e.g., chapter 7, 11) may be commenced against the same debtor only if that debtor has assets in the United States.<sup>98</sup>

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<sup>90</sup> *Id.* at 154.

<sup>91</sup> Codified at 15 U.S.C. § 77(c)(a)(10).

<sup>92</sup> 340 B.R. at 166.

<sup>93</sup> *Id.* at 166-67.

<sup>94</sup> 11 U.S.C. §§ 1525-1526.

<sup>95</sup> 11 U.S.C. § 1501.

<sup>96</sup> 11 U.S.C. § 1527.

<sup>97</sup> 11 U.S.C. § 1529(1)&(2). Even if the foreign proceeding is a foreign main proceeding, the adequate protection, automatic stay, right to operate a business, and right to use or transfer property do not automatically apply. 11 U.S.C. § 1529(1)(B).

<sup>98</sup> 11 U.S.C. § 1528.

If no U.S. case is pending and a foreign main proceeding is recognized (either before or after a foreign nonmain proceeding), then relief granted upon filing for or granting recognition of a foreign nonmain proceeding must be consistent with the foreign main proceeding.<sup>99</sup> If no U.S. case is pending and no foreign main proceeding has been recognized, then relief granted to multiple foreign nonmain proceedings must be done so as to best facilitate coordination between the proceedings.<sup>100</sup> A creditor who receives payment out of one foreign insolvency proceeding may not collect on the same claim so long as creditors of the same class receive “proportionately less than the payment the creditor has already received.”<sup>101</sup>

## **Conclusion**

The BAPCPA added chapter 15 to the U.S. Bankruptcy Code in order to implement UNCITRAL’s Model Law on Cross-Border Insolvency. By modifying and expanding §§ 303-306 of the 1978 Act, chapter 15 continues to focus on the role of the foreign representative and clarifies procedural cooperation in full/main, ancillary, and suspension/dismissal proceedings. Chapter 15 also aspires to promote comity and reciprocity with regard to the substantive law in order to enhance the efficiency and equity of international insolvency proceedings.

## **Author Contact Information**

(name redacted)

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This report was prepared by Georgine Kryda, Law Clerk, under the general supervision of (name redacted), Legislative Attorney.

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<sup>99</sup> 11 U.S.C. § 1530(1)&(2).

<sup>100</sup> 11 U.S.C. § 1530(3).

<sup>101</sup> 11 U.S.C. § 1532.



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