THE WRETCHED REFUSE

LEADING THE FOREIGN CORPORATION
TO A FRESH START
IN THE UNITED STATES

by

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I.
INTRODUCTION

Since the late 1800s, a shining, steadfast monument has stood over the United States as a savior of the poor and downtrodden. **The sculptor intended the work to be an immense and impressive symbol of human liberty.** As this guardian of the lowly and oppressed approached its historic 100th birthday, it was in need of restoration. Congress therefore authorized and funded a major renovation of the national shrine that improved access, repaired existing structural problems, and refurbished this hallmark of our heritage. Millions of Americans now visit it each year, and this protector also stands as a beacon to foreigners–those wretched refuse looking for a fresh start.

Yes, the Bankruptcy Act and Code–Mecca to the financially tempest-tossed all around the world for over a century. Countless individuals from overseas have sought the benefits and protections of the American bankruptcy system, including its award of a discharge of indebtedness to the honest but unfortunate debtor. But is this financial freedom available only to individuals, or may foreign companies also seek shelter here from their creditors? That is, may a foreign corporation, headquartered in a foreign country, initiate a full-fledged bankruptcy case in the United States? Yes. The company need only establish that it has a residence, place of business, or property within the United States. Sounds simple, right? Actually, that determination can be a tricky one, and even if the company establishes its credentials, there is no guaranty that a bankruptcy court will retain jurisdiction over the case. Sometimes the foreign corporation must seek bankruptcy protection in its own country and file a more limited, ancillary proceeding in the U.S.

II.
HISTORY

Section 109 of the Bankruptcy Code, the current source of eligibility requirements for relief under the Bankruptcy Code, was derived in large part from section 2a(1) of the Bankruptcy Act of 1898. Section 2a(1) provided in relevant part that a bankruptcy court may "[a]djudge persons bankrupt who have had their principal place of business, resided, or had their domicile within their respective territorial jurisdictions for the preceding six months, or for a longer portion of the preceding six months than in any other jurisdiction, or who do not have their principal place of business, reside, or have their domicile within the United States, but have property within their jurisdiction . . . ."

With a few exceptions noted in the next paragraph, the eligibility requirements for relief under section 2a(1) of the Bankruptcy Act were similar to those under § 109 of the Bankruptcy Code. Therefore, cases construing section 2a(1) are generally authoritative in the interpretation of § 109. *Bank of Am., N.T. & S.A. v. World of English, N.V.*, 23 B.R. 1015, 1019 (N.D. Ga. 1982) ("These requirements [under § 109] were also found in § 2(a) of the Bankruptcy Act. Therefore, cases construing the meaning of the requirements under the Act will be useful in any analysis of 11 U.S.C. § 109.").

Two differences to note: First, whereas a person's "*principal* place of business" in the United States was a ground for relief under section 2a(1), § 109 requires only that a person have a "place of business" in the United States. Second, whereas having property in the United States was a ground for relief under section 2a(1) only if the debtor did not have a domicile, residence, or principal place of business here, § 109 affords a debtor relief if the person has property in the U.S. irrespective of the other eligibility requirements.

III.
SECTION 109 REQUIREMENTS

Section 109 of the Bankruptcy Code defines who may be a debtor under the various chapters of the Bankruptcy Code. Section 109(a) provides that a person may be a debtor under the Bankruptcy Code if the person "resides or has a domicile, a place of business, or property in the United States . . . ." 11 U.S.C. § 109(a). A "person" is defined generally as an individual, partnership, or corporation. 11 U.S.C. § 101(41). Foreign corporations are therefore generally eligible for relief under the Bankruptcy Code.

Section 109(b)-(g) then limits who may be a debtor under the Bankruptcy Code. Any person is eligible for relief under Chapter 7 (liquidation) except for railroads, insurance companies, and certain banking institutions. 11 U.S.C. § 109(b). Any person eligible for relief under Chapter 7, except for stockbrokers or commodity brokers, may file for relief under Chapter 11, the business reorganization bankruptcy. 11 U.S.C. § 109(d). Chapters 9, 13, and 12 of the Bankruptcy Code are limited to certain domestic municipalities, individuals with regular income, and family farmers, respectively. 11 U.S.C. § 109(c), (e), (f).

To summarize, a foreign corporation that is not a railroad, insurance company, or a banking institution and that has a residence, domicile, place of business, or property in the United States may file a Chapter 7 bankruptcy. A foreign corporation that is not a railroad, insurance company, banking institution, stockbroker, or commodity broker and that has a residence, domicile, place of business, or property in the United States may file a Chapter 11 bankruptcy.

A. DOMICILE

A person that has a domicile in the United States may be a debtor under the Bankruptcy Code. A corporation's domicile is the state of incorporation. *Underwood v. Hilliard* (*In re Rimsat, Ltd.*), 98 F.3d 956, 960 (7th Cir. 1996) (citing *Bank of Augusta v. Earle*, 38 U.S. (13 Pet.) 519, 588, 10 L.Ed. 274 (1839); Restatement (Third) of the Foreign Relations Law of the United States § 213 (1987)). Therefore, a foreign corporation, incorporated in a foreign country, must have a residence, place of business, or property in the United States to qualify for relief under § 109.

B. RESIDENCE

A person that resides in the United States may be a debtor under the Bankruptcy Code. Questions regarding corporate residence arise in a variety of diverse contexts such as jurisdiction, attachment, taxation, and bankruptcy, and must be treated individually in connection with the statutes in which the term is used. *Pennsylvania Ins. Guar. Ass'n v. Charter Abstract Corp.*, 790 F.Supp. 82, 85 (E.D. Pa.1992). *See*, *e.g.*, 28 U.S.C. § 1391(c) (providing that "[f]or purposes of venue under this chapter, a defendant that is a corporation shall be deemed to reside in any judicial district in which it is subject to personal jurisdiction at the time the action is commenced.").

The concept of a corporation's "residence" is a slippery one, however, and bankruptcy courts that have considered petitions for relief by foreign debtors have grabbed on to the (somewhat) more concrete determination of whether the foreign corporation has a place of business or property in the United States.

C. PLACE OF BUSINESS

A person that has a place of business in the United States may be a debtor under the Bankruptcy Code. Bankruptcy courts construing the place-of-business requirement for foreign debtors were given guidance by the early opinion of *In re Carnera*, 6 F.Supp. 267 (S.D. N.Y. 1933). In *Carnera*, an Italian boxer who frequently fought in the United States filed a voluntary petition in New York. For several months prior to the petition date, the debtor lived in a hotel where he received his mail, negotiated fights and exhibitions, paid trainers and sparring partners, and kept correspondence files and a typewriter used by his manager for business use. The court concluded that the hotel was the debtor's principal place of business for the greater part of the six months preceding the petition date: "It does not matter that there was no sign on the door or that there were no office boys moving around. [The debtor] and his staff had business, and the place where most of that business was carried on was his quarters at the Hotel Victoria." *Id.* at 269.

A relatively recent case that followed *Carnera* in eschewing the notion that a debtor need have a formal place of business in the U.S. to qualify for bankruptcy relief was *In re Brierley*, 145 B.R. 151 (Bankr. S.D. N.Y. 1992).[1] The debtor in *Brierley* was one of the many entities related to Maxwell Communication Corporation, which was the subject of dual insolvency proceedings in the United States and England. The debtor had an accountant working in the New York office of Arthur Anderson on behalf of the joint administrators of the Maxwell companies. The accountant worked in Arthur Anderson's offices and reported to a partner at Arthur Anderson. The accountant's employment agreement with the debtor deemed her an independent contractor, although that was done on the advice of tax attorneys. The debtor's name did not appear in the building directory or on any signs. However, the accountant worked full-time for the debtor, was paid by the debtor, communicated regularly with the debtor's personnel in England, and kept in her office certain books and records of the debtor. Moreover, the debtor's location in New York was widely broadcast to third parties having business with the debtor. Therefore, "by virtue of [the accountant's] continuous presence and employment and the substantial activities conducted here by [the debtor, the debtor] has a place of business in this district, notwithstanding that its premises are contained within the larger premises of Arthur Anderson." *Id.* at 162.

The debtors in *Carnera* and *Brierley* did their business on land. But the wretched refuse also come by sea. In *In re Spanish Cay Co., Ltd.*, 161 B.R. 715 (Bankr. S.D. Fla. 1993), a Bahamian corporation whose principal asset was an island in the Bahamas filed for Chapter 11 relief in Florida. The debtor's president sold island lots and island club memberships and conducted the advertising, marketing, and other business affairs of the debtor, all from a houseboat in Florida. The court held that the debtor qualified for relief under § 109 because, among other things, it had a place of business in the U.S. The court rejected a creditor's argument that the debtor's place of business should not be recognized under § 109 because the business was unlawful in that the debtor had failed to comply with applicable state laws regulating business entities: "This Court refuses to deny the debtor eligibility under Section 109 on these grounds."[2] *Id.* at 721. The creditor also urged the court to deny § 109 relief on the ground that any advertising and marketing activities were actually conducted by affiliates of the debtor and not by the debtor itself. However, because the debtor "or" its related entities undoubtedly conducted business activities in Florida and because there was a "continuity of interest" between the debtor and the related entities, the debtor had a place of business in Florida. *Id.* at 721-22.

The wretched refuse also came by sea in *In re Global Ocean Carriers Ltd.*, No. 00-955(MFW) to 00-969(MFW), 2000 WL 1036044 (Bankr. D. Del. July 5, 2000). The fifteen affiliated debtors in *Global Ocean* were involved in the shipping industry and were headquartered in Athens, Greece. All but one of the debtors were incorporated in Cyprus, Singapore, or Liberia. To establish their eligibility for Chapter 11 relief, the Debtors presented evidence that, among other things, some of the Debtors' vessels visited U.S. ports on a regular basis. The court determined, however, that "[h]aving some business in the United States (and even being physically present in the United States for 30% of the year) is insufficient to constitute having a place of business in the United States." *Id.* [Publication page references not yet available.]

To summarize, a foreign corporation need not have a formal office or signs in the U.S. to have a place of business here. The cases thus far have found sufficient a corporation's having nontransitory employees or representatives conducting the company's affairs in the U.S. and representing that fact to third parties. A court may even treat related entities doing business here as one huddled mass for purposes of § 109's place-of-business requirement, even if that huddled mass fails to comply with U.S. business laws.

D. PROPERTY

A person that has property in the United States may be a debtor under the Bankruptcy Code. A foreign corporation with real property in the U.S. would have little difficulty demonstrating its entitlement to relief under § 109, as such property is both easily locatable and quantifiable. But what about tangible and intangible personal property? How much property is "sufficient" to warrant bankruptcy protection? And exactly where is intangible personal property such as a savings account?

Courts have conflicting answers to the question of whether a peppercorn will suffice to warrant bankruptcy relief. In *In re Kava Bowl*, 41 B.R. 244 (Bankr. D. Haw. 1984), an American Samoan corporation filed for Chapter 11 protection in the District of Hawaii. Even though the debtor had some cash and accounting records in Hawaii, the court dismissed the case for lack of jurisdiction, noting that "[t]he 'property' which [the debtor] maintains in Hawaii is not even property in the sense that there is no value to the records to any entity other than [the debtor]. This 'property' is not sufficient for jurisdiction . . . ." *Id* at 247.

A contingent peppercorn in New York likewise is not sufficient for jurisdiction. *In re Head*, 223 B.R. 648 (Bankr. W.D. N.Y. 1998). Several non-U.S. citizens filed for Chapter 11 or 13 relief in the U.S. on the basis that they had done extensive business in the U.S. and that "doing business in" the U.S. should be considered the same as having "property" in the U.S. Concluded the court, "No amount of doing business in the United States will, of itself, provide a basis for eligibility under § 109." *Id.* at 651-52. The court also rejected the debtors' arguments that the debtors' substantial "debts" in the U.S. were the equivalent of having property in the U.S. Finally, the court rejected the argument that the debtors had property in the U.S. in the form of contingent claims against the surplus of a trust fund held for the benefit of a third party: "[T]here is a difference between having property in the United States and having some type of remote or inchoate claim against property that is in the United States. . . . Whatever interest the [debtors] might have in the fund is too tenuous, too inchoate, and too contrived." *Id.* at 652.

A noncontingent peppercorn will suffice in New York, however. In *In re McTague*, 198 B.R. 428 (Bankr. W.D. N.Y. 1996), a U.S. citizen that had resided in Canada for eleven years filed for Chapter 7 relief in New York on the basis that she had $194 in a bank account in New York. The U.S. Trustee filed a motion to dismiss, arguing that such property was too insignificant to support bankruptcy jurisdiction. Asked the court, "[W]ould $100 be enough? Would $10 be enough? Would $.10 be enough? Would a peppercorn be enough? . . . The Court today holds that it is without authority to examine the requisite quantity under 11 U.S.C. § 109(a) . . . ." *Id.* at 429.

And where was the debtor's intangible peppercorn? The court determined that the debtor's property was in New York, where the deposit account was "located": "[A]t least two courts have held that such an account is property 'in' the district in which the deposit account is located, even though bank deposits may be viewed as being 'in' the place of residence of the depositor for certain other purposes." *In re McTague*, 198 B.R. at 431-32.

One of the courts referred to in *McTague* was the court in *In re Berthoud*, 231 F. 529 (S.D N.Y. 1916), *appeal dismissed*, 238 F. 797 (2nd Cir. 1916). In that case, an involuntary petition was filed against an individual debtor who did not have his principal place of business, residence, or domicile in the United States, but instead had $30,000 in a bank account "in" New York. "The whole structure of the [bankruptcy] act indicates that under certain circumstances the proceeding was a sort of proceeding in rem." *Id.* at 532. In concluding that the obligation of the New York bank to pay its depositor, the debtor, was property in New York, the court noted that the situs of personal property--

> largely depends upon the question involved in its ownership. Courts and legislatures have placed the situs sometimes at the domicile of its owner, and sometimes at the place where the property is found. . . .

> I think that Congress in the Bankruptcy Law did not intend that there should be any fine distinctions. The Bankruptcy Law has set up a comprehensive machinery, whereby property throughout the United States with the aid of ancillary jurisdiction may be gathered in by the original court.
>
> . . . "In other words, a bankruptcy proceeding is a kind of equitable attachment, which should be held to reach whatever assets any available judicial process can reach."

Id. (quoting *In re San Antonio Land & Irrigation Co.*, 228 F. 984 (S.D. N.Y. 1916)). *See also In re San Antonio Land & Irrigation Co.*, 228 F. 984, 990 (S.D. N.Y. 1916) (concluding in dicta that a Canadian debtor corporation's stock in a wholly-owned subsidiary, which was pledged to a New York trust company, its interim bond certificates for another wholly owned subsidiary, which were pledged to the same New York trust company, and its balance of $8.06 in an account at the trust company, were all "property" in New York within the meaning of the Bankruptcy Act).

The second court referred to in *McTague* was the court in *Bank of America, N.T. & S.A. v. World of English, N.V.*, 23 B.R. 1015 (N.D. Ga. 1982). That court likewise had to determine whether two foreign debtor corporations' money in a California branch bank constituted "property in the United States" within the meaning of § 109. A secured creditor urged the court to follow the federal law of taxation when determining the location of the debtors' property. Under federal tax law, bank accounts are treated as personal property having its situs at the domicile of the owners, and for purposes of determining whether a tax lien is properly filed and valid, the situs of personal property subject to a lien is the residence of the taxpayer at the time the notice of lien is filed. *Id.* at 1021 (citing the IRC). The court found the creditor's reliance on federal tax law misplaced, as that law was concerned with providing a location of lien notice filing that could be easily identified and determined by third parties dealing with the taxpayer. *Id.*

For purposes of determining the location of personal property in bankruptcy cases, the court, relying on *Berthoud* and *San Antonio Land & Irrigation Co.*, concluded that "courts, when determining the situs of personal property, [should] examine who has control over such property." *Id.* at 1023. In the present case, a California branch bank had control over the debtors' assets in the form of bank accounts and certificates of deposit. Therefore, the debtors qualified for relief under § 109. *See also In re Global Ocean Carriers Ltd.*, No. 00-955(MFW) to 00-969(MFW), 2000 WL 1036044 (Bankr. D. Del. July 5, 2000) (holding that the foreign corporate debtors had property in the United States in the form of funds in various bank accounts: "[T]he bank accounts constitute property in the United States for purposes of eligibility under section 109 of the Bankruptcy Code, regardless of how much money was actually in them on the petition date."); *In re Iglesias*, 226 B.R. 721 (Bankr. S.D. Fla. 1998) (holding that a Chapter 7 Argentine debtor's bank account at a local Florida bank was property in Florida under § 109 and not at the residence of the depositor, Argentina); *In re Spanish Cay Co., Ltd.*, 161 B.R. 715 (Bankr. S.D. Fla. 1993) (concluding that a Bahamian debtor corporation's marketing and advertising materials and other improvements and equipment located on a houseboat in Florida, as well as the debtor's bank account in the U.S., were all "property in the United States" within the meaning of § 109).

The bank-account cases raise some interesting issues: First, who has control over a bank account in a multi-state or multi-national bank? Only the branch office that the debtor visited or called when opening the account? For example, what if a Swiss debtor opened a bank account at the Zurich branch of Ameri-Swiss Bank. If the debtor may access his account at the Dallas office of Ameri-Swiss, the corporate headquarters where the bank is managed, may the debtor file for bankruptcy in Dallas?

Second, an involuntary petition under 11 U.S.C. § 303 may be filed only against a person eligible for relief under Chapter 7 or 11, and as noted above, such a debtor qualifies merely by having property in the United States. If a bank account is viewed simply as an "IOU" of the bank, does this mean that any foreign debtor is eligible for relief under the Bankruptcy Code, voluntarily or involuntarily, so long as someone in the United States owes him money? *Cf. J&L Plumbing & Heating, Inc.*, 186 B.R. 388, 392 (Bankr. E.D. Pa. 1995) ("If accounts receivable are indeed the debtor's principal asset, such accounts would seem to generally be more properly pursued in the locus of the accounts debtor.").

One final query: What if a foreign debtor has no residence, domicile, or place of business in the United States, and no property in the United States except for the unearned portion of the retainer paid to American bankruptcy counsel shortly before the petition date? The *Global Ocean Carriers* case suggests that the retainer may be sufficient to establish § 109 eligibility. The foreign corporate debtors in that case argued that they were eligible for Chapter 11 relief because, among other things, they had an interest in the retainer paid by the debtors to the debtors' American bankruptcy counsel. The court was convinced:

> We agree. The retainers were paid on behalf of all the Debtors and, therefore, all the Debtors have an interest in those funds. It is not relevant who paid the retainer, so long as the retainer is meant to cover the fees of the attorneys for all the Debtors, as it clearly was in these cases. Thus, we conclude that the Debtors do have sufficient property in the United states to make them eligible to file bankruptcy petitions under section 109 of the Bankruptcy Code.

In re Global Ocean Carriers Ltd., No. 00-955(MFW) to 00-969(MFW), 2000 WL 1036044. [Publication page references not yet available.] The foreign debtors otherwise qualified for relief pursuant to § 109 because they had other property in the United States, so the outcome of *Global Ocean Carriers* is unremarkable. But the proposition established by *Global Ocean Carriers*–that a mere retainer paid to American bankruptcy counsel is sufficient to establish § 109 eligibility–promises to expand exponentially the number of eligible debtors.

To summarize, a foreign corporation need not have real property or tangible personal property in the United States to qualify for relief under § 109. Intangible personal property, such as a bank account (or possibly even a retainer), will also suffice, and the courts have determined that the location of such property is the situs of the account debtor. Courts disagree on how much property is enough to satisfy § 109, or even whether the courts should make that determination. This split in the cases is more theoretical than practical, however, because the wretched refuse seeking bankruptcy protection here on the basis of a peppercorn will often be sent packing back to the teeming shore.

IV.
THE WRETCHED REFUSED

Even the early cases such as *Berthoud* recognized that a foreigner's technical compliance with the eligibility requirements under U.S. bankruptcy law is no guaranty that the wretched refuse will enjoy the benefits and privileges of the American bankruptcy system. Recall that the debtor in *Berthoud* did not have his principal place of business, residence, or domicile in the United States, but instead had $30,000 in a bank account in New York. Although the court determined that the debtor had property in the United States within the meaning of section 2a(1) of the Bankruptcy Act, the court finished with these comments: "In arriving at the conclusions here stated, it must not be understood that the court will necessarily take jurisdiction if the creditors, as well as the alleged bankrupt, are all aliens residing abroad. It may very well be that the court would decline jurisdiction . . . . [T]hat question is left open until such time as the fact does appear." *In re Berthoud*, 231 F. 529, 534 (S.D. N.Y. 1916).

By what authority may a bankruptcy court deny relief to a foreign corporation that qualifies for relief under § 109? The court may (i) dismiss the bankruptcy case "for cause" pursuant to 11 U.S.C. § 707(a) or 1112(b); (ii) abstain from exercising jurisdiction over the bankruptcy case pursuant to § 305; or (iii) in appropriate instances in certain dual insolvency proceedings, retain jurisdiction over the case yet apply the substantive law of the foreign insolvency proceeding.

A. DISMISSAL FOR CAUSE PURSUANT TO § 707(a) OR § 1112(b)

Sections 707(a) and 1112(b) of the Bankruptcy Code permit a bankruptcy court to dismiss a Chapter 7 liquidation bankruptcy or a Chapter 11 reorganization bankruptcy "for cause." 11 U.S.C. §§ 707(a), 1112(b). Two of the cases discussed above dismissed or threatened to dismiss the debtors' respective bankruptcy cases on this basis when the debtors had few ties to the United States and simply desired to drag their foreign creditors to an inconvenient forum.

The court in *McTague*, which determined that a "peppercorn" satisfied § 109, noted that "the small quantity relied on by the Debtor here invites further inquiry under other provisions of the Code, such as sections 305 and 707." *In re McTague*, 198 B.R. 428, 429 (Bankr. W.D. N.Y. 1996). *See also In re Head*, 223 B.R. 648, 653 (Bankr. W.D. N.Y. 1998) (holding alternatively that a nonenumerated "cause" for dismissal under § 1112(b) existed when the non-U.S. citizens filed in the U.S. for the purpose of avoiding forum selection clauses in their contracts with Lloyd's of London requiring disputes to be resolved in England: "In essence, they have sought to use the bankruptcy courts of the United States as a 'flag of convenience' by which they endeavor to hammer Lloyd's into submission.").

B. ABSTENTION PURSUANT TO § 305

Section 305 permits a court to dismiss or suspend a bankruptcy case 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.

11 U.S.C. § 304.[3]

The factors considered under § 304(c) include the following:

(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(c).

The court in *McTague* aptly described the practical problems with retaining jurisdiction over a bankruptcy case when the debtor and his creditors have few ties to the U.S. Recall that the debtor, a U.S. citizen that had resided in Canada for eleven years, filed for Chapter 7 relief in New York on the basis that she had $194 in a bank account in New York. The debtor owed approximately $17,000 in unsecured debt to American credit card companies. The debtor also had three secured Canadian creditors: her mortgage lender, her home equity lender, and her automobile lender.

> Although it may be true that orders of this Court have 'extraterritorial effect,' it is fundamental that those orders can be enforced in a foreign nation only to the extent that the foreign nation grants those orders 'full faith and credit' as a matter of comity, treaty, or convention. Similarly, although it is true that the federal courts have 'exclusive jurisdiction of all of the property, wherever located, of the debtor,' 28 U.S.C. § 1334(e), this Court would need the aid of a foreign court to the extent that an exercise of that jurisdiction would require, for example, a recordable court order to clear title to real property located in a foreign country or to enjoin persons located in a foreign country from taking certain actions there.
>
> Totally apart, then, from the question of how the Chapter 7 Trustee would administer any asset in this case other than the $194, any order of discharge that this Court might eventually grant this Debtor would not be enforceable in Canada except to the extent that Canadian courts are moved by comity to grant it 'full faith and credit.' However, presuming that she is able to return here to seek further relief, the Debtor could seek to punish American creditors in this Court for any 'extraterritorial' violation of the discharge order. In other words, to say that the discharge order has 'extraterritorial effect,' . . . is merely to say that extraterritorial violations of the order may be punished in the United States if the violating party is otherwise subject to this Court's jurisdiction. Beyond that, the 'extraterritorial effect' of the discharge order is a matter for consideration by the foreign court.

Id. at 430-31.

The court in *Spanish Cay Co.* applied § 305 to the wretched refuse that came by sea. *In re Spanish Cay Co., Ltd.*, 161 B.R. 715 (Bankr. S.D. Fla. 1993). Recall that the debtor was a Bahamian corporation whose principal asset was an island in the Bahamas. Most of the debtor's creditors were Bahamian entities over which the court would have no personal jurisdiction. Moreover, the loan documents entered into by the debtor and its creditors specifically provided that Bahamian law would apply to the transactions. The creditor moving for dismissal argued that the court should abstain from exercising jurisdiction over the case pursuant to 11 U.S.C. § 305. The court first determined that abstention under § 305(a)(1) was not warranted because dismissal would not be in the interest of *both* the creditors and the debtor. Because Bahamian law did not provide for reorganization, a dismissal of the debtor's Chapter 11 case would result in a liquidation in the Bahamian proceedings.

The court then determined, however, that dismissal was warranted under § 305(a)(2) because both the debtor and its creditors reasonably expected that Bahamian insolvency law would govern their disputes. Although the section technically did not apply because there was not then pending a Bahamian liquidation proceeding, the court lifted the automatic stay to permit a secured creditor to commence such insolvency proceedings in the Bahamas, upon the commencement of which the court would dismiss the case pursuant to § 305(a)(2). *See also In re Xacur*, 219 B.R. 956, 969-70 (Bankr. S.D. Tex. 1998) (abstaining from an involuntary bankruptcy filed against a Mexican citizen and domiciliary when his Mexican creditors could still pursue bankruptcy relief in Mexico and when it appeared that Mexican courts would refuse to recognize the enforceability of U.S. bankruptcy court orders in Mexico); *In re Kava Bowl*, 41 B.R. 244 (Bankr. D. Haw. 1984) (concluding that an American Samoan corporation had no property in the U.S. under § 109, but noting that even if it had jurisdiction, it would abstain from retaining jurisdiction because the debtor was already undergoing receivership proceedings in American Samoa: "Because it now finds the laws of American Samoa not to its liking, it cannot now choose to place itself within the jurisdiction of the Bankruptcy Court in the District of Hawaii, to the detriment of the creditors who have transacted with [the debtor] as an American Samoan Corporation.").

One final case on dismissal. *In re Ionica PLC*, 241 B.R. 829 (Bankr. S.D. N.Y. 1999). The administrators of the debtor, a British telecommunications company, requested and received from the British court where insolvency proceedings were pending permission to file a Chapter 11 petition in the United States. Their goal was not to reorganize the debtor's defunct business, but instead to take advantage of favorable U.S. bankruptcy provisions to challenge the claims of the debtor's corporate parent through either equitable subordination or substantive consolidation. The debtor's only assets in the United States were securities used to secure the debt to its senior noteholders. After the debtor filed its Chapter 11 petition, the debtor's corporate parent moved to dismiss the bankruptcy case, arguing in part that the legal concepts of equitable subordination and substantive consolidation were not recognized in the United Kingdom. If the Chapter 11 case were dismissed and the debtor's assets distributed solely under English law, the corporate parent would receive more and the other general creditors would get less. According to the debtor's parent, this would create a conflict in distributional schemes violative of § 304(c)(4).

The bankruptcy court disagreed, noting that the unavailability of these claims did not make the British law repugnant to our own and did not prevent the distribution scheme from being substantially in accordance with U.S. bankruptcy law. Nevertheless, the court granted the motion to dismiss because all of the other relevant § 304(c) factors weighed in favor of dismissing the petition: The insolvency laws of the United Kingdom (i) have long been found worthy of comity (except in Belgium); (ii) do not discriminate against foreign creditors; (iii) do not prejudice or inconvenience American creditors in processing their claims; and (iv) do not foster preferential or fraudulent transfers of property. *Id.* at 836.

C. RETENTION OF JURISDICTION AND APPLICATION OF FOREIGN LAW

In certain dual insolvency proceedings, where a foreign debtor has instituted full-fledged bankruptcy proceedings both here and over there, a court may elect to apply the substantive law of the foreign proceeding. Authority for this legal maneuvering derives from the principle of comity. What is comity?

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

Hilton v. Guyot, 159 U.S. 113, 163-64, 16 S.Ct. 139, 143 (1895).

This general principle has since been echoed by other courts, with a recent reverberation coming from the Second Circuit:

> The doctrine does not impose a limitation on the sovereign power to enact laws applicable to conduct occurring abroad. Instead, it guides our interpretation of statutes that might otherwise be read to apply to such conduct. When construing a statute, the doctrine of international comity is best understood as a guide where the issues to be resolved are entangled in international relations.

Maxwell Communication Corp. v. Societe Generale (*In re Maxwell Communication Corp.*), 93 F.3d 1036, 1047 (2nd Cir. 1996) (citations omitted). "Absent a contrary legislative direction the doctrine may properly be used to interpret any statute." *Id.* at 1048. International comity applies only when there is a true conflict between U.S. law and that of a foreign jurisdiction. *Id.* (citing, *inter alia*, *Hartford Fire Ins. Co. v. California*, 509 U.S. 764, 798, 113 S.Ct. 2891, 2910 (1993); *Societe Nationale Industrielle Aerospatiale v. District Court*, 482 U.S. 522, 555, 107 S.Ct. 2542, 2561-62 (1987) (Blackmun, J., dissenting)).

The doctrine of international comity should be distinguished from the presumption against extraterritorial application of a U.S. statute. The presumption against extraterritoriality requires a clear expression from

Congress for a statute to reach nondomestic conduct. *Id.* International comity, by contrast, may apply to curtail the application of a statute that would otherwise apply to such conduct. In determining whether to refrain from exercising jurisdiction in the interest of comity, courts look to the following factors:

> "[A]ll relevant factors, including, where appropriate," such factors as the link between the regulating state and the relevant activity, the connection between that state and the person responsible for the activity (or protected by the regulation), the nature of the regulated activity and its importance to the regulating state, the effect of the regulation on justified expectations, the significance of the regulation to the international system, the extent of other states' interests, and the likelihood of conflict with other states' regulations.

Id. (citing Restatement (Third) of foreign Relations § 403(2) (1986)). The *Maxwell* court applied the above factors to the facts at hand, which were these:

The Debtor filed parallel reorganization proceedings in the U.S. and Great Britain, and the courts and trustees in each country were largely successful in producing a common system for an orderly liquidation of the debtor through a joint plan of reorganization and scheme of arrangement (the "Plan"). Certain European bank creditors that received prepetition payments from the debtor realized that they would be exposed to preference liability under the U.S. Bankruptcy Code, but not under the preference laws of Great Britain, which require intent on the part of the debtor to favor the transferee. The banks were ultimately unsuccessful in attempting to have the British court enjoin U.S. preference suits because the British judge declined to interfere with the U.S. court's determination of the reach of U.S. preference law. The British and American bankruptcy trustees thereafter filed preference suits against the banks, which the U.S. bankruptcy court dismissed based on the presumption against extraterritoriality and on the doctrine of international comity. The district court affirmed.

The Second Circuit first had to determine whether it should apply an international comity analysis. Recall that a comity analysis is appropriate only when (1) there is no legislative direction prohibiting a comity analysis; and (2) a true conflict exists between U.S. law and the law of a foreign jurisdiction. The Bankruptcy Code sections relied upon by the banks, such as §§ 103(a), 303(b)(4), and 304, were general in nature and did not prohibit an international comity analysis. Furthermore, a true conflict existed between the preference laws of U.S. and Great Britain because it was impossible to distribute the debtor's assets in a manner consistent with both rules. A comity analysis was appropriate, therefore, so the court then addressed whether the U.S. preference statute should reach the prepetition fund transfers to the banks.

Conducting its comity analysis, the court noted that (1) the debtor and most of its creditors were British; (2) most of the debtor's debt was incurred in Great Britain; (3) the underlying loan documents for the bank debt were negotiated in Great Britain; (4) the underlying loan documents required disputes arising under such agreements to be resolved under British law; and (5) the fund transfers were largely to and from bank accounts maintained in Great Britain. The ties to the United States, by contrast, were minimal: A payment to one of the banks was routed through a U.S. bank, and some of the money transferred to the banks came from proceeds of the sale of the debtor's U.S. subsidiaries. Considering such minimal contacts, the United States did not have a significant interest in applying its avoidance law. Finally, in the interest of maintaining cooperation and harmonization between the bankruptcy systems of the two countries, the court did not want to risk the "selfish application" of its own preference laws when the ties to Great Britain were so strong.

V.
ALTERNATIVE FORM OF RELIEF: SECTION 304–CASES ANCILLARY TO FOREIGN PROCEEDINGS

Section 304 of the Bankruptcy Code enables a trustee, administrator, or other representative of an estate in a foreign proceeding to commence a limited action, as opposed to a full-fledged bankruptcy proceeding, in the United States in order to administer assets located in this country and to prevent dilution of local assets by local creditors. As the title to § 304 suggests, the U. S. bankruptcy action is actually ancillary to the foreign proceeding. This Code provision provides a mechanism for U.S. courts to aid foreign bankruptcy proceedings, accommodate the extraterritorial effect of those proceedings within the United States, and prevent piecemeal distribution of the debtor's assets by local creditors. *In re Koreag, Controle et Revision S.A. v. Refco F/X Assocs.* (*In re Koreag, Controle et Revision S.A.*), 961 F.2d 341, 348 (2nd Cir. 1992), *cert. denied*, 506 U.S. 865, 113 S.Ct. 188, 121 L.Ed.2d 132 (1992). Section 304 is intended to be flexible. *Cunard S.S. Co. Ltd. v. Salen Reefer Servs. AB*, 773 F.2d 452, 454-55 (2nd Cir. 1985). However, a § 304 proceeding is a limited one, designed to function in aid of a proceeding pending in a foreign court. *In re Shavit*, 197 B.R. 763, 766 (Bankr. S.D. N.Y. 1996).

Section 304 provides as follows:

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

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

(1) enjoin the commencement or continuation of–

(A) any action against–

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

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

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

(3) order other appropriate relief.

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

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

prescribed by this title;

(5) comity; and

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

11 U.S.C. § 304.

A. FOREIGN PROCEEDING

What is a foreign proceeding?

> "[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.

11 U.S.C. § 101(23). A foreign proceeding need not involve a foreign federal *bankruptcy* statute, as the court concluded in *In re Fracmaster, Ltd.*, 237 B.R. 627 (Bankr. E.D. Tex. 1999). The § 304 petitioner in that case was subject to three different judicial proceedings in Canada, including a receivership proceeding under the provincial receivership statutes of Alberta. At the trial on the § 304 proceeding, certain creditors argued that the legislative history to § 304 indicates an intent to limit the scope of a foreign proceeding to foreign bankruptcy cases. The court rejected this argument and its reliance on legislative history, which was clearly refuted by the Bankruptcy Code's definition of "foreign proceeding." A foreign proceeding may qualify "whether or not under bankruptcy law . . . . " 11 U.S.C. § 101(23). The court also declined the creditors' invitation to deny § 304 relief on the grounds that the provincial receivership statutes unconstitutionally usurped federal jurisdiction. While such arguments may be entertained in determining what type of relief to afford under § 304, "Congress in its enactment of § 304 did not intend for American bankruptcy courts to adjudicate the constitutional legitimacy of a proceeding under foreign law in order to determine whether or not a foreign proceeding exists under ours." *In re Fracmaster, Ltd.*, 237 B.R. at 635. Finally, the § 304 proceeding was not rendered moot by the subsequent filing of an involuntary Chapter 7 bankruptcy petition against the debtor because the trial on that petition was yet to be heard, and there was no guarantee that an order for relief would be entered. *Id.*

Note, too, that a foreign proceeding need not be a judicial proceeding, but may be an administrative proceeding under the auspices of an administrative authority. *See*, *e.g.*, *Goerg v. Parungao* (*In re Goerg*), 844 F.2d 1562, 1568 (11th Cir. 1988), *cert. denied*, 488 U.S. 1034, 109 S.Ct. 850, 102 L.Ed.2d 981 (1989) (concluding that a German administrative proceeding of a decedent's insolvent estate was a "foreign proceeding" under § 304); *In re Ocana*, 151 B.R. 670 (S.D. N.Y. 1993) (recognizing that the reorganization of a Panamanian insurance company pursuant to statute and under the supervision of a governmental insurance commission was a "foreign proceeding" under § 304); *In re Banco de Descuento*, 78 B.R. 337 (Bankr. S.D. Fla. 1987) (concluding that a nonjudicial liquidation of an Ecuadorian bank conducted by a governmental bank supervisor was a "foreign proceeding" under § 304). *See also In re Ancillary Petition regarding Philippine Airlines, Inc., a Philippine corporation*, No. 98-3-2705-TC (Bankr. N.D. Cal. 1998) (available at www.canb.uscourts.gov/canb/Documents.nsf.)) (recognizing the Philippine rehabilitation law, which is supervised by the Philippine Securities and Exchange Commission, as worthy of comity under § 304).

The term was pushed past its limits, however, in *In re Tam*, 170 B.R. 838 (Bankr. S.D. N.Y. 1994). The Cayman Island corporation in this case appointed a liquidator to wind up the company's affairs, liquidate its assets, pay valid claims, and distribute the remaining assets or proceeds to shareholders. After a creditor in New York sought to attach the corporation's interest in a cooperative apartment there, the liquidator filed a § 304 petition and sought to enjoin the attachment proceeding. The bankruptcy court dismissed the § 304 petition, concluding that the Cayman Island liquidation was not a "foreign proceeding" because the liquidator operated free of supervision from the Cayman Island courts and regulatory agencies and virtually without creditor participation.

Note that the "foreign proceeding" must be in a foreign country in which the debtor's domicile, residence, principal place of business, or principal assets were located when the foreign proceeding was commenced. The district court in *In re Evans*, No. 97 Civ. 3059(LLM), 1997 WL 598477 (S.D. N.Y. Sept. 24, 1997), affirmed the bankruptcy court's order that permitted the § 304 petitioner to conduct jurisdictional discovery to determine whether the petitioner had its principal assets (causes of action) in the United Kingdom. *Id.* at *1-*2. It was permissible for the bankruptcy court "'to allow such limited discovery as will permit the trial court to determine whether it has jurisdiction and whether plaintiffs have standing to prosecute this action.'" *Id*. at *1 (quoting *Investment Properties Int'l, Ltd. v. IOS, Ltd.*, 459 F.2d 705, 708 (2d Cir. 1972)).

May a foreign proceeding exist if the case is technically closed? Yes, according to *In re Petition of Board of Directors of Hopewell Int'l Ins. Ltd.*, 238 B.R. 25, 44 (Bankr. S.D. N.Y. 1999). The § 304 petitioner in *Hopewell* was a Bermuda reinsurer whose "scheme of arrangement" under Bermuda law had been sanctioned or confirmed. Although the court's files were closed and sent to storage, the distribution to a certain class of creditors was not due to be completed until 2001. "Without a doubt, then, the objectives of this scheme have not been fulfilled as yet and, if all other conditions for the granting of comity are met, assistance should be granted to help implement the scheme of arrangement which the Bermuda court has sanctioned." *Id.* at 50.

B. ELIGIBILITY

Thus far there is a consensus among the courts that a debtor need not qualify as an eligible debtor under § 109(a) in order to file a more limited § 304 proceeding. *See Saleh v. Triton Container Int'l, Ltd.*, (*In re Saleh*), 175 B.R. 422, 425 (Bankr. S.D. Fla. 1994); *In re Goerg*, 844 F.2d at 1567; *In re Brierley*, 145 B.R. 151, 160 (Bankr. S.D. N.Y. 1992).

Is having property in the United States a requirement for § 304 relief? No, according to *Haarhuis v. Kunnan Enterprise, Ltd.*, 223 B.R. 252 (D.C. 1998), *aff'd*, 177 F.3d 1007 (D.C. Cir. 1999). The foreign debtor in this case had a breach-of-contract action against it pending in U.S. district court when it filed a § 304 petition, seeking to have the lawsuit enjoined. The debtor, which was undergoing a reorganization proceeding in Taiwan, had no property or "business presence" in the U.S. Nevertheless, the court held that a § 304 petition is not solely an *in rem* or *quasi-in rem* proceeding and that property in the U.S. is not a prerequisite for relief. The court granted the injunction, leaving the creditor to enforce its rights in the Taiwanese proceeding. *Accord Vesta Fire Ins. Corp. v. New Cap Reinsurance Corp.*, 244 B.R. 209, 213 (S.D. N.Y. 2000) (rejecting a creditor's argument that pending arbitration with the debtor was unrelated to the debtor's property in the United States and was thus outside of § 304's purview: "[T]he presence of debtor-owned property in the United States is not the 'sine qua non of bankruptcy court jurisdiction under § 304'") (quoting *Haarhuis v. Kunnan Enters., Ltd.*, 223 B.R. 252, 254-55 (D. D.C.1998)); *A.P. Esteve Sales, Inc. v. Manning* (*In re Manning*), 236 B.R. 14 (B.A.P. 9th Cir. 1999) (following and the "plain language of 304(b)(1)(A)(i) which states that a court may enjoin the commencement or continuation of any action against 'a debtor with respect to property involved in such foreign proceeding.' The statute does not limit this power of the bankruptcy court to situations where the debtor has property located in the United States").

A different answer was suggested in *In re Phoenix Summus Corp.*, 226 B.R. 379 (Bankr. N.D. Tex. 1998), where the debtor had a California state-court action pending against it when it filed a § 304 petition in Texas. The debtor allegedly had filed a bankruptcy proceeding in the Karitane Island, Dominion of Melchizedek. The debtor had no property in Texas, but only vague plans to acquire property there in the future. Said the court, "The entire tenor of § 304 is that the Debtor in the foreign proceeding have some property in the United States which needs to be administered or protected for the benefit of creditors. . . . Since [the debtor] has no property in the United States, and particularly within the State of Texas, the court has difficulty seeing any need for an ancillary bankruptcy proceeding." *Id.* at 381. The court also concluded that the sole purpose of the § 304 petition was to have the California lawsuit transferred to Texas, an impermissible attempt at forum shopping.

As an interesting aside, the Wall Street Journal recently published a story concerning the purported Dominion of Melchizedek and its founder, David Korem, who has been convicted and served time in jail twice for financial crimes. According to the story, officials in the U.S. and elsewhere say that Melchizedek is "the ultimate scam" and exists mostly in cyberspace. Philippine officials arrested three men for selling Melchizedek citizenships, and a U.S. State Department official quoted by the Journal said that Karitane's coordinates, listed on the web site, "seem to point to a seamount, an underwater mountain less than 1,000 feet below sea level." *See* G. Bruce Knecht, *A 'Nation' in Cyberspace Draws Fire From Authorities*, WALL STREET JOURNAL*,* February 9, 1999. This gives new meaning to the term "underwater lien."

Is § 304 relief off limits if the debtor is solvent or if the debtor is involved in a two-party dispute? No on both counts, according to *Rodgers v. Seaward*, No. 99 CIV. 10043(DC), 1999 WL 1129066 (S.D. N.Y. Dec. 9, 1999), *aff'd*, 216 F.3d 1073 (2d Cir. 2000). The debtor in this case filed a § 304 proceeding as ancillary to liquidation proceedings pending in the Isle of Man and obtained a bankruptcy court order enjoining lawsuits against the debtor and requiring turnover of artwork in the possession of a creditor. That creditor appealed, arguing that § 304 was not an appropriate form of relief because the debtor was solvent and because the dispute was between only two parties.

The district court affirmed the § 304 relief, concluding first that the cases relied upon by the creditor–that bankruptcy courts should not be used to resolve two-party disputes–did not apply in the context of a more limited § 304 proceeding: "[T]hat is an argument that must be made to the court in the Isle of Man." *Id.* at *1. Second, "[n]othing in § 304 or the sections defining 'foreign representative' and 'foreign proceeding' requires that the debtor be insolvent." *Id.* at *2.

C. SUBJECT MATTER JURISDICTION

As noted above, a § 304 proceeding is intended to be flexible, but it is also a limited proceeding, designed to function in aid of a foreign proceeding. This concept was demonstrated recently in *JCPL Leasing Corp. v. Treco* (*In re Treco*), 227 B.R. 343 (Bankr. S.D. N.Y. 1998). The plaintiff in this case filed an adversary complaint against the foreign debtor, which was undergoing liquidation proceedings in the Bahamas, as well as against two other, unrelated foreign debtors. The plaintiff argued that the court had subject matter jurisdiction over the claims against the other foreign debtors pursuant to 28 U.S.C. § 1334(b) because the outcome of the lawsuit could conceivably affect the size of the Bahamian foreign debtor's estate. The court disagreed, noting that a limited § 304 proceeding is not a full-fledged bankruptcy case for which an estate must be "administered." Therefore, the scope of the court's jurisdiction over an ancillary proceeding was narrower than the court's jurisdiction over a regular bankruptcy case:

> Thus, to the extent that the action preserves, protects or recovers property of the foreign debtor, we have jurisdiction under § 304 to adjudicate it. By contrast, claims that are unrelated to the preservation or recovery of property in aid of a foreign proceeding are outside the ambit of our limited § 304 jurisdictional mandate.

Id. at 349-50.

The concept of "property of the estate" also played a critical role in *Schimmelpenninck v. Byrne*, (*In re Schimmelpenninck*), 183 F.3d 347 (5th Cir. 1999). While the debtor in this case was undergoing Dutch liquidation proceedings, one of its creditors filed suit in Texas against the debtor's nonbankrupt, wholly-owned subsidiary, seeking to recover on its claim through various alter ego and reverse veil-piercing theories. The debtor filed a § 304 petition, seeking declaratory and injunctive relief to prevent the creditor from pursuing the claims against the sub. The bankruptcy and district courts refused that request after applying the Fifth Circuit's *S.I. Acquisition* test for determining whether a creditor's alter ego claims against nonbankrupt affiliated corporations are subject to the automatic stay. *See S.I. Acquisition, Inc. v. Eastway Delivery Serv.* (*In re S.I. Acquisition, Inc.*), 817 F.2d 1142 (5th Cir. 1987) (applying a two-part, disjunctive test: Does the creditor's cause of action either (1) belong to the corporate debtor; or (2) seek recovery or control of property of the corporate debtor).

On appeal, the Fifth Circuit first criticized the lower courts for applying only the first part of the *S.I. Acquisition* test. The court then criticized the lower courts for even evaluating the creditor's claim under *S.I. Acquisition* and § 362, which require that the creditor's claim affect "property of the debtor's estate" to be eligible for injunctive relief. "Property of the estate" is a concept outside the ambit of § 304. Instead, the lower courts should have applied § 304's more lenient standard, which permits relief against actions seeking to recover property merely "involved in" the foreign bankruptcy:

> Even assuming arguendo that [the debtor parent] is not the proper party to assert the veil-piercing action, that corporation, as the sole stockholder of [the sub], nevertheless has an equity or property interest in [the sub]–not unlike a reversionary interest–sufficient for [the sub] to be "involved in" [the debtor parent's] foreign bankruptcy.

In re Schimmelpenninck , 183 F.3d at 363. Because the sub was "involved in" the debtor parent's Dutch liquidation proceeding, and because the injunction was otherwise appropriate under § 304(c), the court reversed and remanded for entry of a judgment permanently enjoining the alter ego and reverse veil-piercing suit.

For a recent case demonstrating the flexibility of § 304, see *In re I.G. Servs. Ltd.*, 244 B.R. 377, 390 (Bankr. W.D. Tex. 2000) (employing § 304 to deny motion to vacate confidentiality order that protected from disclosure the names of the foreign debtor's Mexican creditors, based on those creditors' fears of personal injury in light of violent kidnappings and murders of wealthy individuals in Mexico: "[S]ection 304 of the Bankruptcy Code . . . [permits a court] to inter alia 'order other appropriate relief.' 11 U.S.C. § 304(b)(3) . . . to wit, eliminating a substantial impediment to active creditor participation, thus advancing the salutary end of just treatment of investor claims in the foreign proceedings.").

D. VENUE

The proper venue for a § 304 proceeding depends upon what relief is requested under § 304. If the foreign representative seeks to enjoin an action or proceeding in state or federal court or to enforce a judgment, the petition "may be commenced *only* in the district court for the district where the State of Federal court sits in which is pending the action or proceeding against which the injunction is sought." 28 U.S.C. § 1410(a) (emphasis added). If the foreign representative seeks to enjoin the enforcement of a lien against property, or to require turnover of estate property, the petition "may be commenced *only* in the district court for the district in which such property is found." 28 U.S.C. § 1410(b) (emphasis added). Finally, if the foreign representative seeks any other relief, the petition "may be commenced *only* in the district court for the district in which is located the principal place of business in the United States, or the principal assets in the United States, of the estate that is the subject of such case." 28 U.S.C. § 1410(c) (emphasis added).

What if a foreign debtor and its property are subject to attacks in several jurisdictions? Must the foreign representative, because of the word "only" italicized above, file a § 304 petition in each jurisdiction? Thus far the courts have rejected this literal interpretation of the statute as contrary to common sense and legislative history. *See In re Petition of Board of Directors of Hopewell Int'l Ins. Ltd.*, 238 B.R. 25, 44 (Bankr. S.D. N.Y. 1999) (hereinafter *Hopewell*); *Evans v. Hancock, Rothert & Bunshoft* (*In re Evans*), 177 B.R. 193, 197 (Bankr. S.D. N.Y. 1995); *Saleh v. Triton Container Int'l Ltd.* (*In re Saleh*), 175 B.R. 422, 426 (Bankr. S.D. Fla. 1994); *In re Kingscroft Ins. Ltd.*, 150 B.R. 77, 81 (Bankr. S.D. Fla. 1992).

The court in *Hopewell* was faced with an additional statutory riddle: Section 1410(a) directs that ancillary proceedings to enjoin the *commencement* of an action be filed in the district where that action is *pending*. In *Hopewell*, the § 304 petitioner, a Bermuda reinsurer, was *threatened* with litigation by various of its insureds in various parts of the United States, but no action was yet pending. No matter:

> [R]equiring a petitioner to foresee where circling creditors will land and simultaneously take steps to enjoin that attack in every single instance where one is planned would produce the same unwelcome results as requiring multiple § 304 petitions to enjoin litigation in multiple jurisdictions. Plainly this would inhibit judicial economy, administrative efficiency, decisional consistency, and perhaps most importantly, comity.

In re Hopewell, 238 B.R. at 45. The court instead looked to the location of the debtor's principal assets in the United States pursuant to 28 U.S.C. § 1410(c). The debtor's principal assets in the United States were its accounts receivable, the location of which the court determined was the situs of the account debtor. Because the majority of the account debtors were located in New York, venue was properly laid there as the location of the debtor's principal assets.

May a properly venued § 304 ancillary proceeding be transferred to a district where the § 304 petition could not originally have been filed? Yes, according to *In re Emerson Radio Corp.*, 52 F.3d 50 (3rd Cir. 1995). The foreign representative filed the § 304 proceeding in New York, ancillary to a Bahamian insolvency proceeding. Entities related to a Chapter 11 debtor in a New Jersey bankruptcy court moved for, and obtained, an order transferring venue of the ancillary proceeding to New Jersey pursuant to Bankruptcy Rule 1014(b). The foreign representative invited the court to conclude that Rule 1014(b) does not apply to § 304 proceedings because 28 U.S.C. § 1410 does not designate the court in which a bankruptcy case for an affiliate of the foreign debtor is pending as one of the possible venues for an ancillary case–i.e., that an ancillary case may not be transferred to a venue in which it could not have been initiated. The Third Circuit declined the invitation:

> The problem with this argument is that neither 28 U.S.C. § 1412 nor Rule 1014(b) includes a limitation that a case may be transferred only to a district in which it could have been brought. . . . [T]he absence of such a restriction is particularly significant given that 28 U.S.C. § 1404(a) provides that a district court may transfer "any civil action" "[f]or the convenience of the parties and witnesses, in the interest of justice . . . to any other district or division where it might have been brought." Both Rule 1014(b) and section 1412 largely include the same criteria for transfer of cases as section 1404(a), i.e., "the interest of justice" or "the convenience of the parties," yet they do not include the limitation that a transfer may be made only to a district where the action might have been brought. These omissions must have been intentional.

Id. at 55 (footnotes omitted).

E. OTHER PROCEDURE/EVIDENCE ISSUES

A foreign representative need not file an adversary proceeding to obtain injunctive relief pursuant to § 304. *In re Petition of Rukavina*, 227 B.R. 234 (Bankr. S.D. N.Y. 1998). The foreign representative in this case filed a § 304 petition, together with a request for a preliminary injunction, shortly before a U.S. district court was to enter a default judgment against the debtor, a Luxembourg corporation recently declared bankrupt under the laws of Luxembourg. The debtor's U.S. creditors argued that the debtor was required to file an adversary proceeding to obtain the injunction it requested, and that the debtor was guilty of laches for waiting until the thirteenth hour to file its § 304 petition.

The court first noted that Bankruptcy Rule 1018, which governs the procedure for § 304 proceedings, does not incorporate Bankruptcy Rule 7001(7), which requires the filing of an adversary proceeding to obtain injunctive relief. Therefore, a separate adversary proceeding was not required to obtain the injunction. The court, noting that full-fledged debtors often wait until the last minute to file, also determined that the foreign debtor was not guilty of laches.

Must evidence of the provisions of foreign law be admissible in evidence? No, according to *Haarhuis v. Kunnan Enterprise, Ltd.*, 223 B.R. 252 (D. D.C. 1998), *aff'd*, 177 F.3d 1007 (D.C. Cir. 1999). The court noted that, pursuant to Rule 44.1 of the Federal Rules of Civil Procedure, a bankruptcy court may properly consider any relevant material to educate itself about the law of the foreign proceeding, whether or not it would be admissible under the Federal Rules of Evidence. Therefore, the bankruptcy court's reliance on inadmissible excerpts of Taiwanese law was appropriate.

May a bankruptcy judge, consistent with due process, enter a preliminary injunction against unknown creditors of a § 304 foreign debtor? Yes, according to *In re Singer*, 205 B.R. 355 (S.D. N.Y. 1997). In this case, the joint provisional liquidators of an insurance company appointed by an English court filed a § 304 petition as ancillary to an English winding-up proceeding and sought to preliminarily enjoin all actions against the insurance company or its assets in the United States. The bankruptcy court denied the request with respect to unknown creditors, and the liquidators appealed. The district court reversed, likening the § 304 injunction to the automatic stay. Section 362 satisfies due process because creditors have an opportunity to obtain relief from the stay. In a similar vein, the proposed injunction order specifically provided procedures to notify subsequently identified creditors as well as procedures for those creditors to obtain relief from the injunction. Finally, the district court determined that the bankruptcy court had abused its discretion in refusing to grant the requested injunction as an exercise in comity. Pursuant to that doctrine, the injunction should have been granted after the foreign representative demonstrated that the English court was a court of competent jurisdiction and that the laws and public policy of the United States and the rights of its residents would not be violated, even though the English proceedings were not identical to U.S. bankruptcy proceedings. *Id.* at 357 (citing *Cunard S.S. Co. v. Salen Reefer Serv. AB*, 773 F.2d 452, 457 (2nd Cir. 1985)).

If a foreign debtor sues a creditor in the § 304 ancillary court for declaratory relief regarding ownership of the foreign debtor's property, may the creditor file a counterclaim against the debtor for affirmative monetary relief without violating the court's § 304 injunction that protects the debtor from suits? It's tempting to analogize to a regular bankruptcy case where counterclaims against the debtor in the bankruptcy court where the debtor initiated the action against the creditor would not violate the automatic stay. According to the court in *In re Bird*, 229 B.R. 90 (Bankr. S.D. N.Y. 1999), however, "[t]here is a danger in expanding the analogy to an equation, for my function in a domestic bankruptcy case is quite different from my function in an ancillary one." *Id.* at 95. That court dismissed one such counterclaim:

> [I]n the context of an ancillary proceeding, I do not determine the extent or validity of claims against the estate; proofs of claim are not even filed in this court. The administration of the debtor's estate, as a whole, is not within my province, for I am not the home court; the main proceeding is in the United Kingdom. It would offend principles of comity for me to decide, in lieu of the English court, whether the claims which [the creditors] seek to assert would unduly interfere with the provisional liquidation and the court proceedings which likely would follow it.

Id. at 95-96.

F. COMITY ISSUES[4]

The district court in *Singer*, discussed immediately above, granted comity to the courts on the other side of the Atlantic. Across the Pacific, the recent Asian financial crisis has spurred interest in insolvency and reorganization proceedings for Asian companies, and an increasing number of bankruptcy opinions here are recognizing foreign proceedings over there. For example, Bankruptcy Judge Thomas E. Carlson recently recognized the Philippine rehabilitation law as worthy of comity in an unpublished opinion, *In re Ancillary Petition regarding Philippine Airlines, Inc., a Philippine corporation*, No. 98-3-2705-TC (Bankr. N.D. Cal. 1998), available on the court's web page at <www.canb.uscourts.gov/canb/Documents.nsf>. Philippine Airlines, Inc. ("PAL"), the national airline of the Republic of the Philippines, filed a petition for suspension of payments and corporate rehabilitation with the Philippine Securities and Exchange Commission ("PSEC"). Thereafter, the foreign representative of PAL filed a § 304 petition in the Northern District of California, obtaining a preliminary injunction prohibiting actions against PAL and its property in the United States. Objecting creditors noted a 1981 presidential decree of President Marcos that transferred jurisdiction over suspension-of-payments proceedings from the Philippine courts to the PSEC. According to the objecting creditors, the suspension-of-payments proceeding was not subject to Philippine insolvency law, and thus not worthy of comity under § 304.

The court disagreed, noting first that Philippine insolvency law provides creditors procedures and protections similar to those found under the U.S. Bankruptcy Code, including priority of claims, appellate review, a first meeting of creditors, an automatic stay, voting on plan confirmation, and recovery of preferences and fraudulent transfers. The court then determined that the presidential decree merely transferred jurisdiction over suspension-of-payments proceedings from one tribunal to another and did not effect a repeal of the substantive insolvency law to be applied by the PSEC. Finally, the court noted that "the PSEC applies the Insolvency Act and Civil Code with reasonable reliability and is not at all the lawless agency objecting creditors portray it to be." Memorandum Decision, at 11.

Taiwan's reorganization proceedings are also worthy of comity, according to *Haarhuis v. Kunnan Enterprise, Ltd.*, 223 B.R. 252 (D. D.C. 1998), *aff'd*, 177 F.3d 1007 (D.C. Cir. 1999). A creditor resisting § 304 relief in this case read the following provision from Taiwan's bankruptcy law as a statutory mandate to ignore or repudiate any non-Taiwanese adjudication of a debtor's rights to property located in Taiwan: "A composition reached abroad or a bankruptcy adjudicated abroad shall not take effect in respect to the properties which the debtor or bankrupt possesses within the domain of Taiwan" *Id.* (citing Chapter I, Article 4, of Taiwan's bankruptcy law, as reported in Commercial, Business and Trade Laws: Taiwan (Bankruptcy) (CCH) (Sept. 1983)). The court instead interpreted the provision to mean that a Taiwanese court is not *bound* by a foreign judgment respecting a Taiwanese debtor's property in Taiwan; instead, a Taiwanese court may give it such recognition as it deserves as a matter of comity. This was no different than the comity test applied here.

Keep an eye out for published opinions on § 304 petitions ancillary to other Asian bankruptcy proceedings, as more Asian countries are adopting bankruptcy laws or revising their old bankruptcy laws. For example, a March 3, 1999 Associated Press story on the FORTUNE INVESTOR NEWS web page reported that Thailand's lower house of parliament passed a long awaited bill that amends their Bankruptcy Act and establishes a specialized bankruptcy court there. The bill, which was passed by the upper house of parliament less than a month before, need only be formally published in the royal gazette to become law. Under the new reorganization law, either creditors or debtors may file a petition if they can prove that (1) the company is insolvent; (2) the company's debt is more than 10 million baht; and (3) the entity is viable as a going concern. *Thailand May Establish Bankruptcy Court/Amend Bankruptcy Law*, BANKR. COURT DECISIONS, December 22, 1998, at A5. The new law includes an automatic stay and a provision for cram-down of unsecured debt. *Id.* If an involuntary is filed, a planner is appointed who takes control of the company and who must file a plan within three months, with two one-month extensions available. *Id.* An official receiver is appointed during plan development to calculate the liabilities of the company. *Id.* A majority of creditors, representing more than 75% of the total debt of the creditors attending and voting, must approve the plan. Currently, creditors are not classified, but each group of creditors must be treated fairly before the plan is confirmed. *Id.* Thailand is considering including the provisions in UNCITRAL's model law for cross-border insolvencies. *Id.*

Indonesia also has a new bankruptcy law, as reported on the TEMPO INTERAKTIF web page at <www.tempo.co.id>. The new law, approved by the House of Representatives in mid-1998 and effective on August 20, 1998, replaced the former law established in 1906 by Dutch colonial authorities. Whereas debtors were permitted to delay cases almost indefinitely under the old regulations, commercial courts now must complete bankruptcy cases within thirty days of filing, with an additional thirty days for an appeal process. The law also permits an ailing but potentially viable company to petition the court for 270 days to restructure its debts with the help of an administrator. *Id.*

On this side of the Pacific, Judge Karen Overstreet recently granted relief in three § 304 proceedings filed ancillary to Canadian insolvency proceedings. *In re Drake*, No. M-98-60005 (Bankr. W.D. Wash. 1998). The court enjoined all creditors and parties-in-interest from taking any action against the debtors or their property except as authorized in the Canadian insolvency proceeding, and also ordered that the rights and remedies of all creditors and parties-in-interest be determined exclusively in the Canadian insolvency proceeding. In an apparent about-face from that directive, however, the court then ordered that, pursuant to the Canadian bankruptcy plan, certain purchasers of the debtors' property took the property free and clear of liens and were good-faith purchasers under § 363(m) of the Bankruptcy Code. The court further ordered that the assumption, assignment, and rejection of any executory contracts were to be determined largely in accordance with § 365 of the Bankruptcy Code. The *Drake* case demonstrates an unusual sprinkling of American and Canadian bankruptcy law.

Other news on this side of the Pacific: On April 30, 2000, the Mexican Congress approved a group of important financial reforms called the Miscellany of Secured Lending (Miscelanea de Garantias or "MG"). The MG creates a new legal framework for granting security interests and giving secured creditors expeditious judicial and extrajudicial means to foreclose on those security interests in the event of default by the debtor.

In conjunction with the passage of the MG, the Mexican Congress also approved an initiative related to e-commerce and the modernization of the public registers of commerce. The new law regulating electronic commerce governs electronic payments and creates legal mechanisms for resolving disputes. Previously, development of e-commerce in Mexico was stifled by a requirement that only original signed documents were evidence of contractual obligations.

Finally, in May 2000, the Law on Commercial Insolvencies (Ley de Concursos Mercantiles or "LCM") was published in the Official Gazette (Diario Oficial) and became law in Mexico. The LCM replaces the antiquated Suspension of Payments Proceeding (Ley de Quiebras y Suspension de Pagos), creates new officers called visitors and conciliators, and promises to be a more sophisticated law for commercial reorganizations and liquidations.

A recent BAP case demonstrates a sprinkling of American and British bankruptcy law, with a Belgian twist. *A.P. Esteve Sales, Inc. v. Manning* (*In re Manning*), 236 B.R. 14 (B.A.P. 9th Cir. 1999). A nut-growing California corporation obtained an order from a Belgian court attaching almonds located in Antwerp, Belgium that were owned by the debtor, a British importing company. The almonds were sold and the proceeds held in the custody of the court while the creditor sued the debtor in California state court for breach of its contract to purchase almonds. The debtor then commenced insolvency proceedings in Britain, and the debtor's administrators sought relief from the almond attachment. The Belgian court denied that request, finding that the British insolvency proceeding did not have extraterritorial effect in Belgium and that the British insolvency system did not provide for equal treatment of foreign and domestic creditors. The administrators then filed a § 304 petition in the United States and obtained an injunction against further actions by domestic creditors against the debtor and its property in the United States. The frustrated nut grower appealed.

After first determining that the debtor need not have property in the United States to seek § 304 relief, the court then reviewed the propriety of the injunction. Although the almond proceeds were in Belgium, the injunction merely prevented the debtor's creditors from pursuing the debtor or its property in the United States. The injunction was therefore appropriate if the § 304(c) criteria weighed in favor of deferring to the British insolvency proceeding. The court then determined that the British Insolvency Act and Code are fundamentally similar to the U.S. Bankruptcy Code and that the British system did not discriminate in favor of local creditors. What do the Belgians know about bankruptcy, anyway?

The United States District Court for the Southern District of New York recently issued an opinion which demonstrates the wrong way to conduct parallel proceedings in different countries. *In In re Commodore Bus. Mach.*, 246 B.R. 476 (S.D. N.Y. 2000), CIL and CEL were Bahamian parent companies and CBM was a U.S. subsidiary. Liquidation proceedings had been filed in the Bahamas for CIL and CEL in 1994. Subsequently, creditors of CIL, CEL, and CBM filed involuntary liquidation proceedings in the United States for all three debtors. The Bahamian liquidators (the "Liquidators") then filed § 304 ancillary proceedings in the United States and a related motion to abstain from the involuntary cases in the United States since appropriate proceedings were already pending in the Bahamas.

A Protocol[5] was negotiated and signed by the Liquidators and the United States creditors to coordinate proceedings. The Protocol was approved by the Bankruptcy Court in the United States (and apparently recognized by the Bahamian Court).

During April 1995, both courts approved a sale of substantially all of the debtors' assets for $10 million, and the money was placed in an account in the Bahamas. When he ordered the deposit, the U.S. bankruptcy judge relied on the representation of the Liquidators' lawyer that the Liquidators were subject to the jurisdiction of the U.S. Court. The order said that the funds were not to be disbursed "except upon further order of a court of competent jurisdiction." Four more status conferences were held by the U.S. Court in an attempt to resolve issues related to the disbursement and allocation of the sale proceeds.

The Liquidators apparently became tired of status conferences and filed a request in the Bahamas seeking substantive consolidation of CBM with Italian and German subsidiaries of CIL. They also sought control over the $10 million account and an order restraining removal of the funds in the account without further order of the Bahamian Court. The affidavit of the Liquidators' lawyer, which was given to the Bahamian Court, said that no proceedings were pending in the United States with respect to disposition of the account. The Bahamian Court then issued an ex parte summons regarding the request of the Liquidators.

When they received the summons, the CBM creditors' committee "went ballistic" and sought from the U.S. court a restraining order and sanctions against the Liquidators. The U.S. court ordered the Liquidators to withdraw the summons and report if funds had been withdrawn from the account. The U.S. Court also enjoined the Liquidators from taking further action with respect to the account. He noted "a complete lack of candor with the Court" by the Liquidators and emphasized that his orders were necessary to insure that both the Bahamian and U.S. Courts were provided with full information relevant to the proceedings.

Instead of complying with the order, the Liquidators filed an ex parte motion with the Bahamian Court seeking an order that the Liquidators were subject only to the jurisdiction of the Bahamian Court and that they were not required to obey the orders of any other court.

The CBM committee, by now beyond ballistic, sought sanctions in the U.S. Court against the Liquidators and transfer of the funds in the account to an account in the United States. Judge Gerrity, the U.S. Bankruptcy

Judge, denied the motion to transfer the funds since the Bahamian Court had not had an opportunity to consider the issues, but he did issue a show cause order requiring the Liquidators to appear and show cause why they should not be sanctioned. The Liquidators appealed Judge Gerrity's rulings to the U.S. District Court and filed a motion with Judge Gerrity to reconsider his rulings.

While the appeal was pending, several status conferences were held regarding potential settlements and the fees of the Liquidators' counsel. After almost two years, the Liquidators filed a motion with the District Court for mandamus to require Judge Gerrity to rule on the motion to reconsider.

The District Court denied mandamus and affirmed Judge Gerrity's rulings. It noted that the Liquidators had engaged in "duplicative and duplicitous behavior." The Court found that the attorney for the Liquidators had represented to the Bahamian Court that no proceedings were pending in the U.S. Bankruptcy Court and had attended at least four conferences with Judge Gerrity and told Judge Gerrity that the Liquidators were subject to his jurisdiction. The District Court also found that the actions of the Liquidators "poured gasoline on the fire" and noted that Judge Gerrity had concluded that the Liquidators had violated the terms of the Protocol.

The scathing opinion of the District Court is surprising since the counsel for the Liquidators enjoy an excellent reputation. They contend that the Protocol provided that issues of Bahamian law were to be decided by the Bahamian Court and that the pleadings filed by the Liquidators in the Bahamian Court, which the U.S. Courts found to be offensive, were permitted pleadings to determine how to distribute assets under Bahamian corporate law. The Liquidators contend that they were not going to disburse the assets of CBM, the U.S. subsidiary, and that the Bahamian Court was the court of appropriate jurisdiction to determine disbursements relating to CIL and CEL. The Liquidators believe that the Protocol did not say that both Courts had to agree regarding disbursement of the funds.

The moral of the story is that you should never lead a court to believe, even inadvertently, that you are running off to another court to circumvent an order of the first court.

G. TURNOVER OF PROPERTY OF THE FOREIGN DEBTOR'S ESTATE

Section 304 gurus are familiar with *Koreag, Controle et Revision S.A. v. Refco F/X Assocs.* (*In re Koreag, Controle et Revision S.A.*), 961 F.2d 341, 348 (2nd Cir. 1992), *cert. denied*, 506 U.S. 865, 113 S.Ct. 188, 121 L.Ed.2d 132 (1992). The Swiss insolvency liquidator in that case filed a § 304 petition to stave-off a New York attachment proceeding against the Swiss debtor's New York bank account. The bankruptcy court, rejecting the creditor's request of a threshold finding as to who owned the property, applied Swiss law to determine that the account funds were included in property "involved in" the Swiss insolvency proceeding and directed turnover of the funds to the Swiss liquidator. After the district court affirmed, the Second Circuit concluded that the lower courts misconstrued the requirements for turnover under § 304. The reach of § 304(b)(1), which permits the court to *enjoin* actions against a debtor concerning "property involved in such foreign proceeding," or against such property, is broader than the *turnover* provision, § 304(b)(2), which applies to "property of such estate." That the property is *involved in* the foreign proceeding is not enough. Before the court requires turnover, it must first look to local law to determine whether the debtor has a valid ownership interest in the property. Then, and only then, may the court consider whether relief is appropriate under § 304(c). Under the local choice-of-law rules, the court held that ownership should be determined by the law of the jurisdiction with the greatest interest in the litigation, which in this case was that of New York.

The *Koreag* rationale was recently applied in *In re Grandote Country Club Co.*, 208 B.R. 218 (D. Colo. 1997). The trustee of a Japanese bankruptcy estate brought an action to quiet title to real property that was the subject of Colorado tax deeds. After withdrawal of the reference to district court, the action was joined with fraudulent transfer and turnover claims that the trustee brought in the § 304 proceeding. On the defendants' motions for summary judgment, the district court held that the validity of the tax deeds for Colorado real property in which the Japanese trustee claimed an interest under Japanese fraudulent transfer law should be determined under Colorado law rather than Japanese law. Section "304(b)(2) authorizes turnover only of 'property of such estate, or proceeds of such property.' This language presupposes an initial determination of property interests as a condition to the turnover of property to a foreign representative." Applying local choice-of-law rules, the court determined that "[a]llowing Japanese bankruptcy law to determine the validity of Colorado instruments of conveyance would undermine the bedrock property principle of title certainty." *Id.* at 224.

The Court of Appeals for the Second Circuit recently reversed a district court in New York that determined that a foreign representative's turnover rights are free of certain restrictions that apply to a bankruptcy trustee's turnover rights. *In re Treco*, 239 B.R. 36 (S.D. N.Y. 1999), *vacated and remanded*, 240 F.3d 148 (2nd Cir. 2001). The court-appointed liquidator of a Bahamian debtor corporation filed a § 304 petition in New York, requesting turnover of the debtor's property in the United States, including funds that were pledged to a secured creditor as collateral. The secured creditor resisted the turnover relief in part because (i) Bahamian law would permit liquidation-related administrative expenses to be paid ahead of its secured claim, in contravention of the U.S. Bankruptcy Code's priority scheme; and (ii) the request for turnover was not conditioned on the provision of adequate protection of the secured creditor's security interest. After the bankruptcy court ordered turnover, the secured creditor appealed.

As to the first argument, the district court held that under the circumstances of the case, where the secured creditor's claim will be recognized in the foreign proceeding as secured, but merely be subordinated to administrative expenses, the turnover order was not an abuse of discretion by the bankruptcy judge. The district court thus held that turnover relief was appropriate irrespective of whether the creditor's claim to the funds was secured. As to the second argument, the court noted that in a regular bankruptcy case, turnover relief against a secured creditor may be had only if the creditor receives adequate protection of its interest. 11 U.S.C. § 363(e). "Nothing in the bankruptcy code, however, provides that turnover orders in an ancillary proceeding pursuant to 11 U.S.C. § 304(b)(2) are subject to the requirement of adequate protection, and in fact the wide discretion accorded to the bankruptcy court in § 304 implies that no such requirement was intended." *In re Treco*, 239 B.R. at 43. The court also noted that the requirement of adequate protection was grounded in the Fifth Amendment's Due Process and Takings Clauses. There was no Fifth Amendment taking in this case, however, because the secured creditor's security interest was never absolute, but was always subject to Bahamian law and § 304 of the Bankruptcy Code. The creditor appealed.

The Second Circuit vacated the district court's opinion and remanded for a determination of whether the creditor's claim was secured, concluding that turnover of the funds would be improper because the distribution procedures under Bahamian law, under the circumstances of this case, would not be "substantially in accordance with the order prescribed by" the Bankruptcy Code. *In re Treco*, 240 F.3d at 151 (quoting 11 U.S.C. § 304(c)(4)). The Second Circuit noted the harm the creditor would suffer after turnover because of the strong possibility that the debtor's estate would have little or no funds after payment of administrative expenses. "The principle of comity has never meant categorical deference to foreign proceedings. It is implicit in the concept that deference should be withheld where appropriate to avoid the violation of the laws, public policies, or rights of the citizens of the United States." *Id.* at 157. Because of the special protected status given to secured creditors under U.S. law, and because the Bahamian law threatened to destroy the creditor's claim, the lower courts abused their discretion by ordering turnover after determining that the Bahamian law was substantially in accordance with the priority distribution scheme under the U.S. Bankruptcy Code. *Id.* at 160-61.[6]

Bahamian law and turnover relief were also at issue in *In re Thornhill Global Deposit Fund, Ltd.*, 245 B.R. 1 (Bankr. D. Mass. Feb. 1, 2000). The Bahamian debtor corporation, a high-risk international investment fund, instituted liquidation and compulsory winding-up proceedings in the Bahamas shortly after it was sued in Massachusetts state court for fraud and breach of contract. The creditor obtained a preliminary injunction order requiring the debtor to deposit $3 million into an escrow account within the United States pursuant to the terms of an escrow agreement to be negotiated by the parties' respective counsel. The debtor wired the money to its counsel's bank account, but before the parties agreed on the terms of an escrow agreement, the debtor filed its § 304 petition, requesting, among other things, turnover of the $3 million. The creditor argued that the funds were immune from turnover because they were no longer property of the debtor's foreign bankruptcy estate.

The court first noted the general *Koreag* rule that a court may consider turnover relief under § 304(c) only after it looks to local law to determine whether the debtor has a valid ownership interest in the property. The court, at the invitation of the parties, applied Massachusetts law to determine whether an escrow was created. Under that law, no escrow agreement was ever created; instead, the debtor merely transferred the funds into its counsel's account in anticipation of creating such an escrow agreement. Therefore, the funds were still property of the debtor's foreign estate and thus subject to turnover.

Turning to the merits of the § 304 petition, the court concluded that the provisions of Bahamian liquidation proceedings were in substantial conformity with U.S. bankruptcy law. Although the quick-moving creditor would lose its advantage over other creditors after the turnover order, such relief was the very purpose of § 304. Moreover, because the creditor was a multi-national sophisticated investor that chose to invest in a fund organized under Bahamian laws, no local interests needed protection.

H. OFFSHORE TRUSTS/CONTEMPT[7]

Woe are those debtors who pin their hopes on international comity as a means of protecting their dubious offshore trusts from local creditors. Their chances fall from slim to none when they repeatedly perjure themselves before the bankruptcy court. And things go from bad to worse when they refuse to comply with the court's turnover order relating to the trust. *Goldberg v. Lawrence* (*In re Lawrence*), 227 B.R. 907 (Bankr. S.D. Fla. 1998). The Chapter 7 trustee here filed a complaint objecting to the debtor's discharge and sought sanctions for the debtor's evasive answers to interrogatories concerning the debtor's creation and interest in a self-settled, spendthrift trust purportedly governed by the laws of the Republic of Mauritius. According to the debtor, Mauritian law imposed criminal penalties upon anyone, including the Mauritian trustee, who disclosed information about the trust. "Mauritius also has the added benefit of its location–the other side of the world. Candidly, it appears the Debtor would have set the trust up on Mars if he could have." *Id.* at 912 n.11. The debtor allegedly established the trust a short time before a $20 million arbitration award was entered against him. The debtor repeatedly lied to the court about the creation of the trust and his professed intent to establish the trust for retirement purposes.

The court refused to apply Mauritian law to the debtor's rights and obligations under the trust, recognizing the "growing body of case law surrounding debtors who have secreted their assets in distant jurisdictions with laws which would make the stereotypical Swiss banker proud." *Id.* at 917. The court then denied the debtor's discharge and referred the case to the U.S. Attorney for investigation: "A bankruptcy discharge for a debtor who engages in this type of conduct should be as rare as the dodo bird which once graced the shores of Mauritius." *Id.* at 916.

The court subsequently entered a turnover order requiring the debtor to turn over to the Chapter 7 trustee the res of the alleged trust and to provide a full accounting of all transactions concerning the trust. When the debtor failed to comply with that order, the court held the debtor in contempt, issuing another published opinion. *In re Lawrence*, 238 B.R. 498 (Bankr. S.D. Fla. 1999). The court rejected the debtor's defense of impossibility and his assertion that it was the Chapter 7 trustee's burden to establish that the debtor could, in fact, comply with the turnover order.

First, the court concluded that "it defies reason–it tortures reason–to accept and believe that this Debtor transferred over $7,000,000 . . . to a trust in a far away place administered by a stranger–pursuant to an Alleged Trust which purports to allow the trustee of the Alleged Trust total discretion over the administration and distribution of the trust res." *Id.* at 500. Second, the burden of establishing the impossibility would be on the debtor because "'[f]oreign trusts are often designed to assist the settlor in avoiding being held in contempt of a domestic court while only feigning compliance with the court's orders.' This is precisely the Debtor's intention before this Court. The Debtor has not met his burden." *Id.* at 500-01 (quoting *Federal Trade Comm'n v. Affordable Media, LLC*, 179 F.3d 1228, 1241 (9th Cir. 1999)). Finally, even assuming that repatriation of the alleged trust was impossible, the trust was the debtor's own creation, so he could not now claim the benefit of the impossibility defense. "Giving credence to the Debtor's argument would be tantamount to succumbing to the pleas for sympathy from an orphan who has killed his own parents!" *Id.* at 501.

In holding the debtor in contempt, the court meant business: Until he purged the contempt by turning over the trust res, the debtor was (i) ordered to pay $10,000 per day; and (ii) ordered incarcerated, with only a twelve-day respite before the incarceration. *Id.* at 501-02.

(Footnotes)

[1]The issue before the court was whether the eligibility requirements for § 109 also applied to a foreign debtor seeking relief pursuant to a § 304 ancillary proceeding, discussed in greater detail below. The court determined that they did not, but noted that even if § 109 applied to a § 304 proceeding, the debtor met those requirements. The court's comments, while dicta, are still instructive.

[2]Would an alien drug dealer conducting the "business" of selling cocaine in the U.S. qualify for relief under § 109?

[3]Section 304 is discussed in greater detail below in section V.

[4]For a discussion of comity gone too far, see the *Treco* case discussed *infra*, pages 28-29.

[5]Protocols are often used to determine the procedure that will be followed in parallel cases and provide for such things as recognition of committees of creditors, joint hearings and notice to creditors.

[6]The court did not reach the adequate protection and constitutional issues.

[7]This section really has nothing to do with § 304, but it has some cool international bankruptcy stuff and it adds some nice bulk to the paper.