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Sale of a Business in Cross−Border Insolvency: The United States and Germany

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Introduction

This paper describes the most important aspects of a cross−border insolvency case between the U.S. and Germany.

Insolvencies can be found in every civilized state or nation [2] since the Roman Empire, as early as 118 A.D. [3] Due to the increasing globalization based on the free flow of information (e.g. internet), capital, services, labor and the progressing creation of trans−national enterprises, cross−border insolvencies and worldwide defaults are an inevitable consequence. [4]

The paper discusses the situation that arises when a U.S. debtor in possession (or trustee) (hereinafter the "DIP") [5] attempts to sell all of its business' assets located in Germany outside a plan of reorganization under chapter 11 of the Bankruptcy Code (hereinafter the "Code"). Such major pre−plan asset sales have become a common and important device in business' reorganizations both in the United States and in Germany. [6]

The U.S. DIP faces the question of how to marshal and sell the assets in Germany. The standard for the sale of a business will either be governed by the Code or the German Insolvency Act (Insolvenzordnung, hereinafter "InsO"). As described below, this will depend on whether the approval of the sale of the business under section 363(b) of the Code [7] will be recognized in Germany and whether a parallel proceeding is filed in Germany.

The first part of this paper will outline the main reasons for a sale outside a plan and then thoroughly examine the applicable U.S. and German law governing the sale. The second part of the paper will discuss the impact of filing the petition for chapter 11 reorganization in the U.S. on the sale of the business' assets in Germany. The general principles of German International Insolvency Law, Article 102 of the Introductory Act to the Insolvency Act, (Einfuehrungsgesetz zur Insolvenzordnung, hereinafter "EGInsO") are also discussed. In particular, the paper explores problems of recognition, the effect on property of the estate in Germany, the automatic stay, the sales contract, the right to convey property of the estate, the effect on secured creditors, executory contracts, existing liabilities and employment contracts. Finally, the paper looks at the impact of the filing of a parallel proceeding in Germany.

In the case of a major multinational insolvency a quick sale of the business can be an essential strategy in preserving the value of assets on behalf of creditors. Successful reorganization and perhaps billions of dollars in capital may depend on the expedient resolution of these issues. The paper concludes that a cross−border insolvency case should be governed by the principles known as mitigated universality and unity in order to maximize the value of the business and to minimize administrative redundancy and potential litigation.

i. Sale of a Business Outside a Plan of Reorganization under The U.S. Bankruptcy and German Insolvency Law

A. Reasons for Selling an Enterprise Outside a Plan of Reorganization

The Code [8] expressly provides for the possibility of the sale of all property of the estate within a plan of reorganization. [9] However, in most cases the DIP or a potential purchaser do not want to wait until the

time−consuming plan confirmation is completed. [10] They prefer to consummate the sale as soon as possible once the bankruptcy is filed because the longer the DIP waits to sell the assets, the greater the risk that these assets may decline substantially in value. Furthermore, a financially distressed debtor often faces serious cash flow problems. To delay the sale of the business in Germany until the confirmation of a reorganization plan might result in a forced liquidation of the debtor's business due to a lack of adequate immediate funds with which to finance business operations. [11] If the U.S. corporation is permitted to continue its business with the proceeds of the sale, then the debtor and ultimately its creditors will be able to realize a going concern value as opposed to the much smaller sum that would be obtained through a liquidation. [12] Even if the business cannot continue to operate, a pre−plan sale is, in many cases, still preferable since the conversion of the case to a chapter 7 liquidation might only add to administrative expenses. [13] Furthermore, the requirements for a sale under section 363(b) of the Code are much less restrictive than for a sale under a plan of reorganization under chapter 11. Most notably, the DIP does not need the approval of the creditors and does not have to satisfy several repayment obligations in order to get the plan confirmed by the court. [14]

B. Major Asset Sales Outside a Plan of Reorganization under U.S. and German Law

1. U.S. Bankruptcy Law

Section 363(b) of the Code deals with the sale of property of the estate outside the ordinary course of business. [15] At first glance, the broad wording of section 363 (b) of the Code seems to permit the disposition of any property of the estate of a debtor under chapter 11. According to the plain language of section 363(b)(1) of the Code, sales outside the ordinary course of business require only court authorization after notice and a hearing. [16] Apart from these requirements, the DIP apparently only needs to prove that the sale price was the best offer within a reasonable period of time. [17] The legislative history and the case law, however, make clear that such a literal reading of section 363(b) of the Code would violate the concept of reorganization proceedings as embodied in chapter 11. For various reasons, the authority is split as to whether a major asset sale is lawful under section 363(b) of the Code.

a. Standards Under the Bankruptcy Act

Chapter 11 of the Code implemented many elements from chapter X and XI of the Bankruptcy Act (hereinafter "the Act"). [18] It is therefore helpful in understanding section 363(b) of the Code to analyze the law under the Act.

b. The Bankruptcy Act of 1867

The Act, as enacted in 1867, did not provide for a reorganization proceeding, but it did provide for the sale of property. [19] The Act provided in section 25 that "when it appears to the satisfaction of the court that the estate of the debtor, or any part thereof, is of perishable nature, [20] the court may order the same to be sold, in such manner as may be deemed most expedient…." [21] In *In re Pedlow*, [22] the Second Circuit Court of Appeals applied section 25 approving a sale of a bankrupt company's stock of handkerchiefs because the price paid exceeded its appraised value, and because the value of the handkerchiefs would decline considerably if the sale were not accomplished immediately.

c. The Chandler Act

In 1937, section 77 B(c)(3) was enacted and added to the Act of 1898, which was restated in an amendment passed in 1938 in section 116(3). Section 116 is the immediate predecessor of section 363(b) of the Code. Section 116(3) provided for the sale of any property of the debtor upon cause shown. [23] Despite the wording of section 116(3) of the Act, the Third Circuit Court of Appeals articulated the so−called "emergency exception standard" five years later in *In re Solar Mfg. Corp*. [24] The court held that pre−confirmation sales should be restricted to emergencies where there is danger that the assets of the business will be lost if they are not sold immediately. [25] The *Solar* emergency exception, however, was heavily criticized by legal scholars [26] and contradicted in subsequent pre−Code decisions. [27] The majority of the criticism focused on the fact that the *Solar* exception reflected "an overly restrictive view of the district court's power to authorize the sale or lease of a corporate debtor's property." [28] In fact, the Act did not contain any language that indicated that an emergency situation is required in order to sell property of the debtor outside a plan. The leading decision in this context is *In re Dania Corporation* [29] in which the Fifth Circuit rejected the emergency exception based on the arguments mentioned above and focused on the *upon cause shown* language in section 116(3).

2. Standards Under the Bankruptcy Code

Unlike section 116(3) of the Act, the wording of section 363(b) of the Code makes no reference to any kind of perishable standard, emergency situation, or cause shown. Additionally, no other statutory standard for a sale of substantially all assets outside a plan can be found in the Code. Apart from the notice and hearing requirement, it seems that courts have broad discretion to approve the use, sale or lease of property of the debtor outside the ordinary course of the business.

a. Minority View

The minority view argues that the Code specifically provides *only* for plans of liquidation in sections 1123(a)(5)(D), 1123(b)(4) and 1141(d)(3)(A). The sale of a major asset under section 363(b) of the Code should not be permitted outside a plan because it would amount to a liquidation, which should be carried out under chapter 7, not under chapter 11. [30] Furthermore, a section 363(b) sale would circumvent the strict and elaborate rules concerning the plan confirmation process [31] under chapter 11. [32] In *In re D.M. Christian Co.*, [33] the debtor operated a department store and the purchaser attempted to buy all of the debtor's inventory and fixtures. The bankruptcy court rejected the sale because it would have the effect of a complete liquidation of the debtor's tangible assets. The court concluded that such a liquidation sale could only be accomplished if there was compliance with the plan confirmation process of chapter 11. [34]

b. Moderate View

In *In re White Motor Credit Corp.*, [35] the court took a moderate view and returned to the emergency exception. The case concerned the sale of all of the debtor's truck manufacturing assets to a subsidiary of Volvo. [36] In deciding whether to authorize the sale, the court focused on the legislative history of the Code and the draft legislation of the Commission on the Bankruptcy Laws of the United States and the National Conference of Bankruptcy Judges. The court noted that both drafts recognized that "[a] sale or lease of all or substantially all of the property of the estate may be authorized by the court if in the best interests of the estate after notice and a hearing in accordance with the Rules of Bankruptcy Procedure." [37] The Court concluded that the absence of this express language in section 363(b) of the Code provided strong evidence that Congress wanted to prohibit major asset sales under section 363(b) of the Code. Pre−plan sales might therefore only be approved under the general powers of section 105 of the Code, provided that an imminent emergency exists. [38]

c. Majority View

The decisions following the *Christian* and the *White Motor* rulings all expressly rejected the arguments mentioned above. [39] In *In re Whet, Inc.*, [40] the debtor proposed to sell the entire enterprise, a radio station, as a going concern. The bankruptcy court relied on the plain language of section 363(b) of the Code and held that the wording of section 363(b) does not limit the quantity of property that may be sold. Furthermore, it does not follow necessarily that the abandonment of the *upon cause* standard of section 116(3) of the Act was intended to overrule the case law under that section. Except for the decisions in *V.Loewer's Gambrinus Brewery* and *Christian*, all cases unanimously recognized the lawfulness of the sale of all of the debtor's assets. In *In re Brookfield Clothes Inc.*, [41] the court concluded that the deletion of the *upon cause* standard of the former section 116(3) of the Act in section 363(b) of the Code was intended to provide the court with substantial discretion to decide, under the particular facts of each case, whether it would be best for the estate to engage in the sale of major assets of the debtor prior to a plan's confirmation. In other words as Judge Holmes put it: "Some play must be allowed for the joints of the machine." [42] It is therefore now very well established that a sale of all of the debtor's assets may be lawfully accomplished outside a plan of reorganization under section 363 (b) of the Code.

d. Requirements for the Sale Under Section 363 (b) of the Code

The procedural safeguards incorporated into chapter 11 conflict with the possibility of permitting a chapter 11 debtor to sell all of its assets under section 363(b) of the Code. In *In re Lionel*, [43] the court established the "sound business reason" requirement as the appropriate standard for approving major asset sales under section 363(b) of the Code. This

standard was adopted by a vast majority of courts. [44] In *Lionel*, the debtor sought to sell its most important asset, 82% stock holdings, for $50 million. The Second Circuit made clear that the bankruptcy court does not have limitless discretion to authorize a section 363(b) sale. The Second Circuit held that while section 363(b) of the Code gives the bankruptcy judge considerable discretion, the sale can only be approved if the DIP shows at the hearing that the sale would be a "sound business decision." [45] It is this principle that should guide the judge in deciding whether or not to approve the sale. The factors to be considered are: (1) objective and tangible reasons why the debtor could not propose a plan to the creditors within the normal chapter 11 framework and instead intends to sell the assets outside a plan, [46] (2) whether there is any improper or bad faith motive behind the sale effort, [47] (3) whether the purchase price is fair, reasonable and the product of good faith and whether the negotiations or bidding occurred at arm's length, [48] (4) whether an adequate pre−sale procedure has been established, including proper exposure to the market and accurate and reasonable notice to all creditors and *parties in interest* with respect to the terms of the proposed transaction, [49] and (5) whether the parties have attempted to structure the transaction so that it becomes more than the sale of property wherein the debtor's estate is converted into cash, such as a transaction that dictates the terms of any future reorganization plan. [50] Taking these factors into consideration, the Second Circuit held that the mere pressure of the creditors to sell the stock and the bankruptcy court's concern that the reorganization might be considerably delayed if the sale was not approved was an insufficient reason to grant the sale. [51]

3. The German Insolvency Law

a. Introduction

The new German Insolvency Act (Insolvenzordnung, hereinafter "InsO") came into effect on January 1, 1999. [52] It succeeded the old Bankruptcy Act (Konkursordnung), the Composition Act (Vergleichsordnung), and the Collective Enforcement Act (Gesamtvollstreckungsordnung) of the former German Democratic Republic.

The need for a reform was based on the fact that between 75% and 80% of all bankruptcy petitions were dismissed because of insufficient assets to pay the administrative expenses in the case. Furthermore, the average distribution to unsecured creditors was on average less than five percent and only one percent of all cases were resolved in a composition. [53] Due to a significant increase in insolvency filings, beginning in 1991, and still continuing the legislature was forced to act. [54] The InsO provides, for the first time, an elaborate set of rules governing the reorganization of a viable business through an insolvency plan deriving its main inspiration from chapter 11 of the Code. Section 1 InsO provides, as objectives of the insolvency proceedings, the collective satisfaction of creditors either by liquidation of the debtor's assets, *or* by reaching an agreement on an insolvency plan. As opposed to the Code that favours reorganization over liquidation, the drafters of the InsO relied on the concept that reorganization should not necessarily take precedence over liquidation. [55] Furthermore, contrary to the distinct procedures governing the liquidation and reorganization under chapter 7 and 11 of the Code, the InsO deals with the administration of the debtor's estate within a unitary set of rules.

All insolvency proceedings are commenced as liquidations. The liquidation proceedings can be converted to reorganization proceedings following the first meeting of creditors. By providing that all insolvency proceedings begin as liquidations, the debtor loses the advantage of filing for reorganization when success is unlikely and barring creditors from foreclosing until the court decides to convert the proceeding to a liquidation. [56] The disadvantage is, however, that fundamental decisions of the trustee (e.g. whether to assume executory contracts or dismiss employees) depend on whether the business is to be liquidated or to be reorganized. [57] Another important difference between the InsO and the Code is that proceedings under the former are mostly creditor−driven and the debtor possesses very limited rights in relation to the interests of its creditors. [58] Importantly, in most cases, the debtor is not left in possession of the estate. [59] In addition, the InsO does not give the debtor the exclusive right to file a plan for any period of time. [60]

b. Procedural Distinction Between the Code & the InsO

In order to understand the legal issues involved in a pre−plan sale of a business, it is first necessary to outline two procedural steps under the InsO of particular importance when considering major asset sales.

1) Opening Proceeding

Unlike the Code, the filing of a petition to begin an insolvency proceeding does give the debtor automatic protection from its creditors. Upon receiving the petition, an opening proceeding is initiated. During the 'opening proceeding' process, the insolvency court must, pursuant to section 16 InsO, examine whether there is a reason to open insolvency proceedings [61] and whether the assets of the debtor are sufficient to cover the costs of the proceeding. [62] If one of the requirements is not met, the insolvency court dismisses the petition to open the insolvency case.

During the "opening proceeding" process, the insolvency court has the obligation, pursuant to section 21(1) InsO, to take all measures on behalf of the creditors that appear necessary to avoid any detriment to the financial situation of the debtor. In most cases, the insolvency court will designate a temporary insolvency trustee pursuant to section 21(2) No.1 InsO. [63] If the insolvency court combines the appointment of a temporary trustee with a general restriction on the debtor's right to convey property, then the right to manage and transfer property of the estate will automatically be vested in the temporary trustee (known as the "strong trustee"). [64] Alternatively, if the insolvency court designates a temporary trustee without imposing a general prohibition of transfer on the debtor, the court shall determine the powers of such trustee using section 22(2) InsO. Pursuant to section 21(2) No.2 InsO, the court will commonly order that the debtor's transfers of property shall require the consent of the temporary trustee in order to become effective (known as the "weak trustee"). Thirdly, if the insolvency court should be of the opinion that the unconditioned continuation of the business by the debtor imposes no risk to the creditors, all rights remain with the debtor and the debtor can continue the operation of the business.

2) Report Meeting

The first major procedural step after opening the insolvency proceeding with particular importance to the sale of assets is the report meeting. The report meeting shall be held between 6 weeks and three months after the opening decision. [65] According to section 156(1) InsO, the insolvency trustee shall at the report meeting comment on the economic situation of the debtor and its causes. He shall assess any prospects of maintaining the debtor's enterprise in whole or in part, indicate any possibility of drawing up an insolvency plan, and describe the effects of each solution on the satisfaction of the creditors' claims. After the report meeting, the insolvency trustee shall, pursuant to section 159 InsO, immediately liquidate the property forming the assets involved in the insolvency proceeding, unless such disposition contradicts any decisions made by the creditors' assembly.

In order to determine when and under what circumstances major asset sales outside a plan of reorganization are permissible, it is therefore necessary to distinguish strictly between the opening proceeding and the insolvency proceeding itself. Furthermore, within the insolvency proceeding, a distinction is made between the time before and after the report meeting with regard to major asset sales.

c. Major Assets Sales in the Opening Proceeding by a Temporary Insolvency Trustee

In many cases, the debtor faces severe cash flow problems and thus needs to sell the business as a whole as soon as possible to avoid being forced to cease its operations. Time is therefore a very important consideration. Often the debtor does not have the luxury of delaying the sale until the court formally decides to open the insolvency proceeding. The possibility of selling the business during the opening proceeding is essential to sustaining the business, but the legality of such a sale is called into question by a reading of the InsO.

The InsO contains no explicit provision that allows [66] a temporary trustee to sell a business in the opening proceeding. [67] To the contrary, according to section 22(1) sentence 2 No.2 InsO, a temporary trustee is explicitly obligated to continue the operation of a business until the insolvency court decides on the opening of the insolvency proceeding, unless the insolvency court consents to a closedown of such business in order to avoid a considerable loss of the debtor's property. The InsO governs the sale of property of the debtor only after the insolvency proceeding has been opened and the report meeting has been held. As mentioned above, [68] section 159 InsO states that after the report meeting has been held, the trustee shall immediately liquidate the property forming the assets involved in the insolvency proceeding, unless such disposition contradicts any decision taken by the creditors' assembly. It appears, therefore, that prior to the report meeting, the business cannot be sold. Section 159 InsO, however, regulates only the

duty of the trustee to liquidate the assets (*shall liquidate*). The fact that this duty comes into effect only after the report meeting has been held does not necessarily mean that the trustee has no right to liquidate the assets before the report meeting. [69] The distinction between the duty and the right to liquidate property suggests, therefore, that it must be possible for the trustee to sell the business in the opening proceeding.

1) Standard for the Sale of the Business in the Opening Proceeding

(aa) Involvement of the Debtor

The "opening proceeding" is used by the court primarily to determine whether to open the insolvency proceeding rather than as a tool to liquidate the debtor's assets and repay its creditors. The temporary trustee is therefore only entitled to take such measures that can be considered reasonable for the debtor in the event the "opening proceeding" is withdrawn by the petitioner or rejected by the insolvency court. [70] The sale of the entire business is practically never appropriate for a debtor during the "opening proceeding". [71] One need only imagine a scenario in which, as a result of an involuntary filing, the temporary trustee sells the business only to subsequently discover that the filing of the insolvency proceeding was without justification and is dismissed by the court. Through no fault of his own, the debtor would be deprived of the entire business. This generally acknowledged principle applies even if an interested purchaser offers a very lucrative price [72] and an early sale would be the best measure to maximize the assets of the debtor [73] or even if the opening proceeding has progressed to such a point that a positive decision of the court to open the insolvency proceeding can be anticipated. [74] Even if the petition to open the insolvency proceeding was filed by the debtor himself, the temporary trustee must not sell the enterprise without the consent of the debtor. [75] The purpose of the debtor filing his petition could have been for the express purpose of working out a reorganization plan that would enable him to continue his business. [76]

The only narrow exception, in which the consent of the debtor is not necessary can be derived from section 22(1) Sentence 2 No. 2 InsO. If the continuation of the business by the temporary trustee would diminish the value of the property of the debtor to a considerable extent the insolvency court can approve the closedown of the business without the consent of the debtor. Since the closedown of a business is in many respects a much more drastic measure than the sale of the business, it follows that if the trustee can close down with the approval of the court and without the consent of the debtor, the trustee is able to sell the business with the approval of the court but in the absence of the debtors' permission if necessary to avoid a considerable loss of the value of the debtor's property. [77]

(bb) Involvement of the Creditors

The dilemma facing the temporary trustee is the question surrounding the balance between the consent of the debtor and the approval of the sale by the creditors. This question arises since the obligation to continue the operation of the business according to section 22(1) Sentence 2 No.2 InsO applies also to the creditors. [78] Adhering to the language of this section, the only alternative to the continuation of the enterprise is the court approved closedown, not the debtor approved sale of the business. Consequently, the creditors must be involved in the decision making process whether to sell the business. [79] In practice however, the problem becomes how the interests of the creditors can be taken into account during the opening proceeding.

(i) Formation of a Creditors' Assembly

Because the opening decision of the insolvency court has not yet been made, claims may not be filed by the creditors. [80] Consequently, the insolvency court has insufficient information about the existence, number and identity of the creditors and their claims. Neither the creditors nor their respective voting rights can be determined by the court, which effectively prevents the formation of a creditors' assembly. [81]

(ii) Formation of a Creditors' Committee

The situation concerning the formation of a creditors' committee seems, at first, to be less problematic. According to section 67(1) InsO, the insolvency court can establish a creditors' committee prior to the first creditors' assembly. [82] Additionally, pursuant to section 67(3) InsO, persons not holding the status of creditors may also be appointed as

members of the creditors' committee. It appears, therefore, that according to the wording of section 67(1) and (3) InsO, the insolvency court can establish a creditors' committee in the opening proceeding. [83] The problem with this interpretation, however, is that section 67 is not located within the provisions regulating the opening proceeding (section 11–34 InsO) but within sections 56–79 regulating the insolvency trustee and other bodies representing the creditors. Section 67 InsO therefore implies that the opening proceeding has come to an end and that the insolvency court has opened the insolvency proceeding. [84] Section 67 InsO, consequently, does not apply in the opening proceeding directly. The alternative view is to derive the power of the court to form a creditors' committee during the opening proceeding from the general provision of section 21(1) InsO based on the rationale of section 67 InsO. According to this provision, the insolvency court shall take all measures that appear necessary in order to avoid any detriment to the financial status of the debtor for the creditors until the insolvency court decides on the request to open an insolvency proceeding. [85] This provision can be interpreted broadly to include the power to establish a preliminary creditors' committee during the opening proceeding that can vote on the proposed sale of the business. However, the court's power to appoint a creditor's committee in the opening proceeding is limited.

(aaa) The Debtor's Disclosure

Once a creditors' committee has been appointed, the debtor is obligated to provide the creditors with all necessary information so as to enable them to make a decision on whether to approve the proposed sale of the business. [86] Due to the possibility that the court might eventually decide not to open the proceeding, the debtor is usually not willing to disclose business information until there is an irrevocable decision of the court to open insolvency proceedings. [87] This concept makes sense when some of the creditors are also business competitors of the debtor. In its decision on whether to appoint a creditors' committee, the court therefore has to consider carefully whether it is reasonable for the debtor to be obligated to disclose his business information at this stage of the proceeding to a merely preliminary creditors' committee.

(bbb) Creditors' Committee Representative

Next, the insolvency court must appoint a creditors' committee that adequately represents the interests of the entire creditor body without yet knowing the identity of all creditors. [88] Section 67 InsO does not require that in order to appoint a creditors' committee prior to the first creditors' assembly the deadline to file a proof of claim has been terminated. The InsO therefore recognizes that a creditors' committee can be formed even if not all creditors are known. The court must consider, on a case−by−case basis, whether it is reasonable, with regard to potentially unknown creditors, to appoint a creditors' committee in the opening proceeding. [89] If the court decides to appoint a preliminary creditors committee, its approval of the proposed sale of the business is always required. [90]

(iii) Proceeding Without a Creditors' Committee

If the court decides not to appoint a creditors' committee, then the question of who should represent the interests of the creditors with regard to the proposed sale of the business arises. [91]

(aaa) Approval of the Insolvency Court

The rationale of section 22(1), sentence 2, No.2 InsO, which requires the temporary trustee to continue to operate the business and which conditions the closedown of the business on the approval of the insolvency court, suggests that the sale of the business can only be consummated with the consent of the insolvency court. [92] This contravenes, however, the legislative history of the InsO. One of the main objectives of the InsO was to reduce to a minimum the involvement of the insolvency court in business decisions. [93] The legal committee expressly noted in section 177 of its draft that the insolvency court shall not be involved in the decision whether to sell the business prior to the report meeting. [94] Furthermore, the sale of the enterprise, when compared to its closedown, represents a much less drastic measure because, in a sale, jobs are preserved and the business keeps operating. Additionally, in contrast to a closedown, the sale of the business generates an immediate flux of cash. The sale thus seems to promote the best interests of the creditors more than a closedown. The approval of the sale by the insolvency court is therefore not required. [95]

(bbb) Determination of the Preliminary Trustee

The approval of the court is not required and, therefore it is within the discretion of the preliminary trustee whether or not to sell the business. The sale of an enterprise is a significant aberration of the concept of sections 157, 159 and 160 InsO. According to the rationale of these sections, crucial decisions concerning the future of the business shall only be made after the report meeting in compliance with the orders of the creditors. The decision of the temporary trustee, therefore, has to correlate to section 22(1) Sentence 2 No.2 InsO and to comply with the same standard that applies to the closedown of the business. [96] The temporary trustee can sell the enterprise only if, after a thorough investigation of all relevant facts, evidence demonstrates that the continuation of the enterprise would inevitably lead to a considerable loss of the debtors' property. [97] If it turns out later that this standard has not been met, the temporary trustee might be liable, according to section 60 and 22(2) No.1 InsO, if there is any harm to the creditors.

Neither the consent of the debtor nor the refusal of the insolvency court to appoint a creditors' committee relieves the temporary trustee from potential liability to the creditors. [98] The insolvency court can, however, according to section 21(1), 21(2) No.1 and 58 InsO, try to bar the temporary trustee from selling the enterprise. The insolvency court might prohibit the sale, however, only in the limited situation where the proposed sale is evidently inexpedient and, based on the facts, apparently does not comply with the standard required by section 22(1) sentence 2 No.2. [99] Otherwise, the insolvency court must not interfere with business decisions of the temporary trustee. [100]

d. Sale of the Business in the Opening Proceeding by a DIP

A sale of the business by the debtor itself might only take place if the court does not consider the appointment of a temporary insolvency trustee necessary in order to avoid any financial harm to the creditors. A DIP, therefore, remains in control of his business and all business−related decisions and does not need the approval of the creditors or the court to sell the enterprise during the opening proceeding. [101] The insolvency court has the power to bar the DIP from conveying his property in the event that the DIP entered into an agreement to sell his enterprise. The court can designate, according to sections 22(2) and 21(2) No.2 InsO, a temporary insolvency trustee and order that transfers of property shall require the consent of that temporary trustee in order to become effective. In the case where the transfer of property is conditioned on the approval of a temporary trustee, the trustee has to take the interests of the creditors into account when making his decision whether to consent to the proposed sale. [102] If a sale will most likely avoid a considerable loss of the property of the debtor, or would considerably increase the property of the estate, [103] or even avert the asserted reason for opening an insolvency proceeding, the trustee has to approve the sale. [104]

e. Sale of the Business in the Insolvency Proceeding

1) Sale of the Business Prior to the Report Meeting

The InsO does not contain a provision governing the sale of assets prior to the report meeting. Only the criteria under which a business may be closed are expressly regulated. If the trustee intends to close the business prior to the report meeting, the trustee must, pursuant to section 158(1) InsO, obtain the consent of the creditors' committee if one has been appointed. [105] Section 158 InsO asserts that a trustee is obligated to continue to operate the business until the report meeting. [106] A trustee who wants to sell the enterprise prior to the report meeting always needs the consent of the creditors and is therefore well advised to convince the insolvency court to appoint a creditors' committee as soon as possible. [107] If the insolvency court rejects the appointment of a creditors' committee, the trustee has two alternatives. The trustee can request, pursuant to section 75(1) No.1 InsO, the convocation of a special creditors' assembly, which decides only whether to sell the assets. [108] Alternatively, the trustee may seek to convince the purchaser to sign the sales contract conditioned upon subsequent approval of the creditors' committee. [109] According to section 276 InsO, the same principles apply to a DIP regarding his attempts to make such a sale.

2) Sale of the Business after the Report Meeting

The requirements for a sale *after* the report meeting can be derived directly from the language of the InsO. At the report meeting the creditors' assembly decides, according to section 157 InsO, whether the debtor's business shall be closed down or continued. Section 160(1) InsO requires the insolvency trustee to obtain the consent of the creditors'

committee if he intends to engage in transactions that are of particular importance to the insolvency proceeding. If no creditors' committee has been appointed, the trustee shall obtain the consent of the creditors' assembly. According to section 160(2) No.1 InsO, consent is particularly required for the sale of an enterprise or plant. In a case of a DIP, section 160 InsO applies according to section 267 InsO *mutatis mutandi*.

f. Sale of the Business to Persons with Specific Interests

According to section 162 InsO, the sale of the business requires the approval of the creditors' assembly if the purchaser or a person holding at least one−fifth of the purchaser's capital is: 1) in a close relationship to the debtor; [110] 2) is a creditor with a right to separate satisfaction; 3) or is a creditor with non−lower ranking claims whose rights to separate satisfaction and claims are assessed by the insolvency court to reach a total of one fifth of the sum of the value of all rights to separate satisfaction and of the amounts of the claims of all creditors of the insolvency proceedings with non−lower ranking claims. Section 162 InsO similarly reflects the case law under section 363(b) of the Code, whereby there must be no improper or bad faith motive behind the sale effort. [111]

g. Sale of the Business Below Value

Pursuant to section 163 InsO, at the request of the debtor or of a majority of creditors qualifying under section 75(1) No.3 InsO [112] and after testimony from the trustee, the insolvency court may order that the proposed sale of the business be approved by the creditors' assembly. The court will only order this if the requesting party proves that a sale to another purchaser would be more beneficial to the assets involved in the insolvency proceedings. [113] This requirement is also reflected under the case law of section 363(b) of the Code demanding that the purchase price has to be fair, reasonable and the product of good faith and negotiations or bidding at arm's length. [114]

C. Conclusion

In summary, it can be noted that the U.S. law opted to put the decision as to whether to sell the business in the hands of the bankruptcy judge. The German law, on the other hand, puts the emphasis on the interest of the creditors and confers to them the right to decide which solution serves their interests best and to enforce it against the debtor and equity holders.

II. Cross−Border Insolvency Law

A. Introduction

According to the definition under both the American and the German law, Cross−border−Insolvency [115] is the term that designates those cases of insolvency in which the assets and liabilities of an insolvent debtor are located in two or more separate jurisdictions with different laws. [116] Having laid down the rules governing the sale of an entire business outside a plan of reorganization, it has become clear that both U.S. and German law provide for the possibility of the sale of all assets of the debtor before a plan is confirmed. The statutes differ, however, concerning the standard and requirements for such a sale. Most importantly, the InsO requires the actual approval of the creditors committee (or if no committee has been appointed, the consent of the creditors' assembly), whereas under the Code the approval of the bankruptcy court is sufficient. This distinction can have a crucial effect on the entire chapter 11 reorganization in the United States. Should the approval of the sale by the U.S. bankruptcy court not be recognized in Germany and the approval of the German creditors become necessary to consummate the sale, then the German creditors (assuming they have the required majority in the creditors' committee) would have the power to block the sale and jeopardize or even bar the entire reorganization in the United States. Even if the creditors are willing to approve the sale, the power of a potential objection gives them a strong bargaining tool in the reorganization process.

Thus, the question of how the German insolvency law deals with cross−border cases and whether the effects of a foreign insolvency proceeding will be recognized in Germany must be addressed first. The next consideration will be to apply German cross border insolvency law to the approval of the sale of the business in Germany by the U.S.

bankruptcy court under chapter 11 of the Code. This includes reconciling subtle differences in the laws of the U.S. and Germany. Additionally, this paper discusses other problems of recognition that a U.S. DIP under chapter 11 reorganization with assets in Germany might commonly face. Subsequently, this paper will examine the effect on the property of the estate, the automatic stay, the right to convey property of the estate in Germany, and the effect on secured creditors, executory contracts, existing liabilities, employment contracts, and the filing of a parallel proceeding in Germany.

B. Universal Approach of the German Insolvency Law

For more than 100 years German courts have taken the view that foreign bankruptcy proceedings had only territorial effect [117] and thus did not reach assets located in Germany. [118] In 1985, the Federal Court of Justice (Bundesgerichtshof (BGH)) (hereinafter "Federal Court of Justice") finally reacted to the criticism of its jurisprudence by overruling those decisions and applying the principle of universality [119] to foreign proceedings [120] (known as Wendeentscheidung: turning−point−decision).

On January 1, 1999, the InsO and an Introductory Act to the InsO (Einführungsgesetz zur Insolvenzordnung (hereinafter "EGInsO")) came into effect. While the Government Insolvency Reform Bill of March 3, 1992 (Regierungsentwurf (hereinafter RegE)) [121] contained a detailed set of rules for international insolvencies based on the draft of the European Union [122] Insolvency Convention (RegE §§ 379−399), the German legislature did not implement these rules in view of the expected completion of the work on that Convention. [123] Instead, the government opted to enact a new Article 102 EGInsO. [124] That article contains two general principles: The recognition of foreign insolvency proceedings [125] and, at the same time, the possibility of domestic insolvency proceedings with territorial effect covering only assets situated in Germany.

C. Definition of Recognition of Foreign Insolvency Proceedings

Recognition means that the effects of a main foreign proceeding will be exported to Germany. [126] The proceeding will be governed by the law of the opening state (*lex fori*) unless specific exceptions apply [127] and as long as no territorial secondary proceeding has been opened in Germany. [128]

D. Requirements for the Recognition of a Foreign Insolvency Proceeding

The recognition of foreign insolvency proceedings under Article 102 (1) EGInsO is, however, not without limitations. In particular, the following requirements have to be met under Article 102 EGInsO. [129]

1. Jurisdiction of the Foreign Bankruptcy Court

Article 102 (1) No.1 EGInsO states that recognition of the foreign proceeding is dependent on the affirmation of the jurisdiction and authority of the foreign court. The competency of the foreign bankruptcy court is determined by the applicable German law and not under the law where the bankruptcy proceeding is pending. [130] According to section 3 InsO, the insolvency court has jurisdiction in the district where the debtor has his usual venue [131] or where the center of the debtor's self−employed business activity is located. [132] In contrast to U.S. law, [133] the mere existence of property is insufficient to permit the commencement of a full insolvency proceeding. [134] Consequently, a chapter 11 case, where the debtor has only property in the U.S., would not be recognized under Article 102 EGInsO. This contravenes the universal approach of the Code as embodied in section 541(a). According to section 541(a) of the Code, the commencement of the case creates an estate comprised of all property wherever located and by whomever held. In the scenario of a U.S. debtor incorporated and having its administrative headquarters in the U.S., the U.S. bankruptcy court would also have jurisdiction under section 3 InsO. Problems arise in the event the debtor is incorporated in Germany, but has assets in the U.S. and files a chapter 11 bankruptcy case. In that scenario, due to the lack of jurisdiction of the U.S. bankruptcy court under section 3 InsO, the U.S. bankruptcy case would not be recognized in Germany. Effectively, the business in Germany does not become part of the U.S. estate and cannot be sold according to section 363(b) of the Code. Otherwise, German debtors and creditors would be readily subject to a worldwide operating U.S. trustee or DIP even if no insolvency proceeding could be commenced under German law. [135] The recognition of foreign proceedings is therefore limited for the protection of the interests of German debtors

and creditors. [136]

2. *Ordre Public* [Public Policy]

The most important limitation concerning the recognition of foreign insolvency proceedings is contained in Article 102 (1) No.2 EGInsO. [137] According to this provision, a foreign proceeding will not be recognized in Germany if it contradicts fundamental principles of the applicable German law (*ordre public* restriction). [138] The Federal Court of Justice noted that a decision of a foreign bankruptcy court must not be recognized if it was reached in a foreign insolvency proceeding that deviates so significantly from the fundamental principles of German law that basic rights of the German creditors are violated. [139] The deviation must be so egregious that the decision of the foreign insolvency court cannot be considered the result of a sound proceeding, [140] and thus becomes void. [141] The party objecting to the recognition has the burden of proof. [142]

3. *Ordre Public* and Chapter 11 Reorganizations

It is generally acknowledged that chapter 11 cases under the U.S. Bankruptcy Code are recognized under Article 102 EGInsO, [143] unless the *ordre public* is violated. [144] A violation of the *ordre public* does not necessarily mean that the foreign proceeding is not recognized in its entirety, [145] but that only certain effects of the foreign bankruptcy proceeding will not be recognized, [146] such as, for instance, the approval of the sale of the business by the U.S. bankruptcy court.

a. Violation of the Ordre Public by Authorizing the Sale by the U.S. Bankruptcy Court under Section 363(b) of the Code

The law of the state where the insolvency proceeding has been opened determines the disposition and distribution of the property of the estate, unless it violates the *ordre public*. [147] The issue of whether the U.S. bankruptcy court's approval of the sale of the business outside a plan of reorganization under section 363(b) of Code will be recognized in Germany is of particular interest due to the different requirements for the sale under U.S. and German insolvency law. Indeed, section 363(b) of the Code requires only court approval in order to accomplish the sale of the business, whereas section 160 InsO requires the consent of the creditors' committee, or if no committee has been appointed the consent of the creditors' assembly. The issue is, therefore whether this difference is so significant that it contradicts a fundamental principle of the German Insolvency Act and whether the missing approval of the creditors violates their basic rights and must therefore be regarded as a violation of the *ordre public*.

The purpose of section 160 InsO is to protect the interests of the creditors by conferring upon them the right to decide whether or not the business should be sold. Evidently, under the InsO, the sale of the entire business was regarded by the German legislature as such a drastic measure that neither the business judgment of the trustee, nor the approval of the court could provide a sufficient substitute for the actual approval of the creditors' committee in order to protect their interests. By entrusting the creditors with the authority to sell the business, section 160 InsO protects the interests of the creditors to a greater extent than does section 363(b) of the Code. A violation of the *ordre public* is indicated if the foreign trustee or DIP can dispose of the assets without any involvement of the creditors.

On the other hand, the DIP cannot sell the business under section 363(b) of the Code without providing sound business reasons justifying the sale. [148] The strict requirements concerning the sound business reason, as developed in extensive case law throughout the years, [149] might not supplement an actual consent of the creditors but can nevertheless be regarded as a sufficient safeguard of the creditors' interests. Section 363(b) of Code deviates from and limits the rights of the German creditors as granted to them under the InsO. Due to the sound business reason safeguard, implied in section 363(b) of the Code, this aberration can, however, not be regarded as so fundamental that it amounts to a violation of the *ordre public*. The Federal Court of Justice has made it clear that non−recognition is the exception, [150] and a violation of the *ordre public* is much more than a mere aberration. A non−recognition due to a violation of the *ordre public* is limited to an *ultima ratio* measure. [151] The *ordre public* restriction does not require adherence to a particular procedure, provided that the deviation is reasonable. [152]

Absent the unlikely event that the U.S. bankruptcy court totally disregards the interests of the creditors in its decision whether or not to approve the sale**,** the approval of the sale of the business under section 363 (b) of the Code will be recognized in Germany under Article 102 (1) EGInsO. German law fully recognizes the powers of the foreign trustee [153] or DIP. [154] These powers need not to be identical to the powers a trustee would have under German law and may be broader or narrower. [155] The powers are to be determined under the law of the forum state where the proceeding is pending. [156] The foreign DIP can take all necessary actions concerning the property of the estate that the foreign law empowers him to. [157] On condition that no territorial, secondary insolvency proceeding has been opened, [158] the trustee may, at his discretion, possess assets of the debtor, remove them to the main forum, or sell them with the exception of assets encumbered by a security interest or reservation to title. [159] Thus, the U.S. DIP may sell the business in Germany based upon the authorization of the U.S. bankruptcy court.

b. Other Problems of Recognition Commonly Faced Within a Chapter 11 Reorganization With Assets in Germany

Even if the decision of the bankruptcy court to approve the sale of the business is recognized in Germany, it does not necessarily follow that the U.S. DIP has *carte blanche* to use and dispose of the assets in Germany. The U.S. debtor often faces other objections to the recognition of the U.S. chapter 11 case. The most important and frequent objections are discussed below.

1) No Discrimination

The German creditors must be treated equally in the foreign proceeding throughout the entire reorganization without any discrimination. [160]

2) Right to be Heard

Article 103 (1) of the German Constitution (Grundgesetz, GG) embodies the right to be heard before a court. The German creditors must have had the opportunity to be heard in the foreign proceeding. [161] Section 363(b) of the Code requires a hearing before the court prior to the sale of any assets outside the ordinary course of business. A non−recognition of the sale of the business, based on a violation of the right to be heard, could only occur in the unlikely scenario that the German creditors were not notified of the hearing as prescribed under Bankruptcy Rule 2002 (a) (2).

3) Opening of the Foreign Proceeding

(aa) Opening Decision

In its leading decision in 1985, the Federal Court of Justice spoke of the recognition of the opening of a foreign insolvency proceeding. [162] However, under the Code, the bankruptcy court does not formally open a bankruptcy case. [163] The filing of a voluntary petition automatically triggers the commencement of the case. [164] Article 102 EGInsO did not adopt the language of the Federal Court of Justice and makes it clear that the lack of a formal decision of a foreign insolvency court to open the insolvency proceeding has no effect on the recognition of the foreign proceeding.

(bb) Right to Notice of the Commencement of the Foreign Proceeding

How and to what extent the creditors are to be informed about the commencement of the foreign proceeding is to be determined under the *lex fori concursus* [law of the state where the proceeding is pending]. [165] The right to notice of the commencement of the foreign bankruptcy case is of particular interest with regard to U.S. cases since it differs from the InsO in that it does not require the publication of the commencement of the case. [166] Notably, the decision of the Higher Regional Court (Oberlandesgericht, (OLG)) Saarbrücken, which dealt with the recognition of a French reorganization plan, [167] established a case precedent. In this case a German creditor did not file its claim. The consequence under the French law was that the creditor lost its entire claim. Because he was not officially informed of the commencement of the foreign proceeding, the creditor claimed that the reorganization plan was not binding on him, and that he was consequently entitled to 100% payment of his claim. The court rejected that argument and held that the possibility to take note of the foreign proceeding based on the publication abroad was sufficient. [168]

The decision was heavily criticized. The mere publication of the commencement of the case abroad provides domestic creditors with constructive notice of the commencement of the proceeding, it has, however, too often the consequence that foreign creditors do not have any knowledge of the case until the proceeding has concluded. [169] Since the entitlement to notice is a fundamental right of every creditor, [170] it can be argued that the publication of the commencement of the case only within the state where the case is pending is insufficient for the recognition of the foreign proceeding in Germany. [171] With regard to the Code, which does not even require the publication of the commencement of the case in the U.S., it is recognized that the actual notification of the creditors (including all foreign creditors) of the commencement of the case substitutes the lack of publication and satisfies the right to notice. [172] The missing requirement of publication is therefore not considered a violation of the *ordre public*. [173]

4) Reason to Open Insolvency Proceedings

(aa) Possible Abuse of Chapter 11 Filings

As mentioned earlier, [174] the InsO requires, according to section 16 InsO, a reason to open insolvency proceedings. The reason can be illiquidity, [175] imminent illiquidity, [176] or over−indebtedness. [177] On the other hand, under the Code, a voluntary case is commenced automatically with the filing of the petition without the requirement for cause to open the case. Some authors argue that the filing of a petition under the Code is often misused to trigger the automatic stay and the 120 days exclusivity period solely to prevent creditors from foreclosing on the assets without the intent to pursue a genuine reorganization. [178] Under the InsO, the filing of the petition does not provide an automatic stay such as under section 362 of the Code.

This absence of a standard for opening a case in the U.S., and the well−known abuses of chapter 11 filings, may constitute a violation of the *ordre public*. Since the problem of bad faith chapter 11 filings is raised not only by scholars in Germany, [179] but also acknowledged by U.S. scholars, [180] it is necessary to scrutinize in detail whether this possible misuse violates the *ordre public* to such an extent that chapter 11 proceedings should not be recognized under Article102 EGInsO.

First, it seems unlikely that a debtor files a chapter 11 solely in order to obtain a breathing space from impending foreclosure of his creditors. It is certainly easy to commence a chapter 11 case just by filing a petition. It is, however, comparatively more difficult to dismiss the case. The petition cannot be simply withdrawn by the debtor. According to section 1112(b) of the Code, the court can dismiss the case only for cause. [181] Should the debtor not present a reorganization plan within 120 days after the filing of the petition, the court can, upon the motion of a creditor, convert the case to a chapter 7 liquidation for cause if it is in the best interest of the creditors pursuant to section 1112(b)(4) of the Code. A debtor who files solely to buy time is facing a considerably risky undertaking. A debtor who undertakes such a risk opens himself to the possibility of facing a sudden liquidation of the business' entire assets without any alternative. [182] Furthermore, if the debtor should attempt to free himself from an impending liquidation under chapter 7 by conceding that the information given in the chapter 11 petition was false, he faces charges of perjury under the federal law. [183] Finally, the court has the option of dismissing the case on the grounds of bad faith if, for instance, the court is of the opinion that the debtor had filed its petition solely to delay its creditors from foreclosing on its assets. [184] These safeguards should provide more than enough protection from the misuse of chapter 11 filings and comply with the ordre public restriction. [185]

(bb) Filings of Solvent Debtors

With regard to the *ordre public* restriction, it might be further argued that chapter 11 filings of financially solvent debtors should not be recognized under Article 102 EGInsO since German law explicitly requires illiquidity. [186] In the decision of *Johns−Manville*, [187] the court held that the solvency (or lack of balance sheet insolvency) of the debtor is not to be regarded as a reason to dismiss the case. Insolvency of the debtor is expressly not required under the Code. [188] It cannot be ignored that delaying a petition until the debtor is insolvent might jeopardize the entire reorganization. Because the German legislature foresaw this risk and incorporated imminent illiquidity in section 18(2) InsO as a sufficient reason to open insolvency proceedings, it can no longer be argued that filings of solvent U.S. debtors constitute a violation of the *ordre public*. [189] The enactment of section 18(2) InsO brought the InsO in line with the Code.

5) Tax Claims and Punitive Damage Claims

Another problem concerning a violation of the *ordre public* restriction is the special treatment of tax claims and punitive damage claim holders under the Code. [190] Confirmation of a plan does not discharge a debtor from any tax liability contained in sections 523(a)(1) and 1141(d)(2) of the Code or protect them from punitive damage claims. In certain cases, the vast majority of the debtor's assets are consumed by outstanding tax and punitive damage claims, so that there are no assets left to be distributed to German creditors.

(aa) Tax Claims

With regard to tax claims, it is argued that no court should be required to recognize or enforce foreign tax claims. [191] Most states argue that the recognition of foreign tax claims violates their *ordre public* restriction. [192] With regard to Article 102 EGInsO, the priority treatment of tax claims violates the abandonment of priority claims under the InsO. [193] This might constitute a violation of the *ordre public*, and can thus not be recognized under Article 102 (1) EGInsO [194] and it can be argued that a priority treatment of foreign tax claims shall only be recognized if a treaty between the states contains such a provision. [195]

(bb) Punitive Damage Claims

Since German law does not know the concept of punitive damage claims at all, such claims will never be recognized in Germany. [196] It is therefore consistent not to recognize a foreign reorganization where the assets of the debtor are so significantly consumed by punitive damage claims that only a marginal amount would be left for distribution to German creditors. [197]

E. Effects of the Recognition of the U.S. Case with Regard to the Sale of the Business in Germany

In the following section, this paper will look at the effects of chapter 11 filings in the U.S. as it relates to the sale of the business in Germany. It is self−evident that a foreign DIP may not exercise his powers in a way that would be contrary to the law of Germany. The foreign DIP has to observe the local−non−insolvency law. [198] Assets can only be sold in accordance with procedures provided by the German law. [199]

F. Property of the Estate

Article 102 I EGInsO expressly states that assets of the debtor located in Germany become property of the estate where the bankruptcy case is pending. Article 102 EGInsO is therefore in compliance with section 541(a) of the Code. [200] The business and all other assets in Germany become property of the estate created under the applicable provisions of the Code. [201] Exemptions to the property of the estate are determined under the law where the property is located, in this case, the German exemption law. [202]

G. Automatic Stay

Due to the recognition that the assets in Germany become part of the U.S. estate, the automatic stay under section 362 of the Code automatically protects them. [203] Any entity, which holds property of the estate in violation of the automatic stay, is obligated to return the property to the foreign estate. [204]

H. The Sales Contract

1. Execution of the Sales Contract

The parties of any contract may determine under which law the contract should be governed. [205] An important question, which has to be resolved by the DIP and a potential purchaser, is the determination of the applicable law for the execution of the terms of the sales contract. The parties are well advised to include an explicit clause in the contract determining the applicable law in the case of subsequent quarrels concerning the content and mutual obligations under the contract. [206] Furthermore, it is also recommended to state whether subsequent conflicts should be

decided by a state court or court of arbitration. [207] U.S. parties usually insist on a clause that determines that a U.S. court has jurisdiction to decide any subsequent disagreements under the contract. The reason is that U.S. courts often award higher breach of contract and damage claims including punitive damages, which are not recognized under German law. On the other hand, a U.S. party should take into consideration that a judgment of a U.S. court cannot easily be enforced in Germany. Prior to any execution, the judgment of the foreign court must be recognized before a German court, pursuant to sections 328, 722–723 of the Code of Civil Procedure (Zivilprozessordnung, (ZPO)). [208] Punitive damage awards and extremely high monetary damage awards will not be recognized under section 328 No.4 ZPO. [209] The establishment of the jurisdiction of a German court between the seller and the buyer would therefore avoid a costly and time consuming proceeding for the recognition of the judgment of a U.S. court in Germany. Another clear advantage is that German legal proceedings are faster and less expensive than U.S. proceedings.

2. Disclosure Requirements of the Seller

In a recent decision, the Federal Court of Justice [210] outlined the disclosure requirements for the sale of a business. The court established stringent guidelines that, due to the difficulty in evaluating the value and the viability of an entire business for an outsider, the seller is required to disclose the entire economic and financial situation of the business. [211] The seller is obligated to disclose all facts that might influence the decision of a potential purchaser whether to buy the business. [212] If the U.S. debtor does not comply with this duty, he might be liable for compensation of damages caused due to his failure of a proper disclosure.

I. Right to Convey Property of the Estate

Following the commencement of the bankruptcy case, the debtor loses its right to dispose of the assets located in Germany. The right passes over to the DIP, [213] or if appointed, to the trustee in bankruptcy. [214] In the case of the sale of an entire business such a sale inevitably involves the conveyance of both real property and personal property to another entity. Such transfers are governed by the law where the property is located (*lex rei sitae).* [215] The l*ex rei sitae* governs the content, conveyance, alteration, extinction, and good faith purchase [216] of any right in property. The trustee or DIP, therefore, needs to comply with the applicable German property law in order to convey the assets of the business to a third party. In the case of real property, this requires a notary certified purchase contract, [217] an agreement with the purchaser before a notary concerning the conveyance of ownership, [218] an entry in the land register [219] and the right of the trustee or DIP to convey the property. [220] In the case of personal property, an agreement to transfer title and actual physical handover is required. [221]

J. Good Faith Purchaser

Since the assets in Germany become part of the U.S. estate, transfers of property in Germany after the commencement of the case in the U.S. would be void according to section 549 of the Code. The applicable law concerning the conveyance of ownership is the *lex rei sitae,* and German law governs the good faith purchase of a post−bankruptcy transfer. [222] German property law protects third parties who acquire title or another interest in land in reliance and in good faith against the effects of insolvency generally. [223] The trustee must prove that an entry of the commencement of the insolvency proceeding in the land book had been made or that the purchaser had actual knowledge of the commencement of the foreign proceeding. [224] It is essential for a foreign trustee to assure that the commencement of the bankruptcy proceeding is entered into the land book in Germany as soon as possible to avoid any depletion of the property of the estate post petition due to a good faith purchase. The authority of the foreign representative was contained in section 386 RegE. This provision has not, however, been enacted and the authority is consequently to be derived from the general administrative powers of the trustee or DIP.

K. Effect on Secured Creditors

Another important consideration that the DIP has to take into account regarding the sale of the business is the existence of liens or security interests in the property to be sold. Security interests [225] of third parties in assets of the debtor situated in a state other than the opening state at the time of the opening of the proceeding (foreign situated collateral) [226] will not be affected by the proceedings. [227] Furthermore, reservation of title is equal to a security interest. [228] Under the concept of reservation of title, which is routinely used in Germany, [229] title to goods remains

with the seller until the purchase price is paid in full. As a consequence, the holder of a security interest in collateral situated in Germany is treated and may proceed as if no insolvency proceeding were pending. [230] Secured creditors are thus not affected by the automatic stay under section 362 of the Code and are not subject to the right of the DIP to sell property free and clear of any interest in such property under section 363(f) of the Code. [231] The secured party may sell collateral or foreclose on a mortgage assuming it complies with the law of the state where the collateral is located. [232] In such a case the creditor need not return the proceeds of what it obtained to the DIP of a recognized main proceeding. The possibility of filing a secondary territorial proceeding in the state where the collateral is situated, however, mitigates the special role of secured creditors in the foreign main proceeding. If a secondary proceeding is filed in Germany, the disposal and distribution of assets situated in Germany is governed exclusively by German law. [233] Creditors become therefore subject to the stay under section 89 InsO and the debtor may sell the business under the InsO.

L. Effect on Executory Contracts

The next question is, which law applies to the assumption or rejection of executory contracts. [234] Notably, a potential buyer might subject the purchase of the business to a prior rejection of unbeneficial contracts or the assumption of profit generating contracts, respectively. The InsO deals with executory contracts in section 103. Under section 103 InsO, which is similar to section 365 of the Code, the trustee has the right to perform such a contract and claim the other parties' consideration. [235] If the trustee refuses to perform such a contract, the other party shall be entitled to its claims for non−performance as a creditor of the insolvency proceeding. [236] Section 103 InsO differs from section 365 of the Code in that the trustee does not need the approval of the insolvency court. Due to the desire for an efficient administration of the estate, the rules of the opening state apply with regard to the rejection, assumption and assignment of executory contracts, irrespective of the law that governs the execution of the terms of the contract in question. [237] There is, however, an exception for employment contracts [238] and similarly, the assumption or rejection of leases of real property. [239]

M. Effect on Existing Liabilities

Former section 419 of the Civil Code (Buergerliches Gesetzbuch (BGB)) (hereinafter "BGB") contained a major obstacle for the sale of a business. According to former section 419 BGB, a purchaser automatically inherited the existing liabilities of the enterprise. This strict regulation often prevented effective reorganizations by means of selling the business to a third party. The legislature saw this problem and abandoned section 419 BGB, since the InsO came into effect on January 1999, [240] because a potential purchaser is often not willing to assume responsibility for former liabilities of the business. All creditors of the business, which were present before the commencement of the insolvency proceeding, are entitled to their claims only as creditors of the insolvency proceeding and cannot enforce their claims against the purchaser.

N. Effect on Employment Contracts

Another obstacle, which could prevent an effective reorganization by selling the business, might be that a potential buyer may place conditions upon his purchase, such as a prior shut down of existing uneconomical parts of the business and a termination of the related uneconomical employment contracts in order to make the business competitive. The question is, therefore, what effect the sale of the business would have on existing employment contracts and under what circumstances could such contracts be altered or terminated.

1. Applicable Law

According to Article 30 (2) of the Introductory Act of the Civil Code (Einfuehrungsgesetz zum Buergerlichen Gesetzbuch, (EGBGB)) (hereinafter EGBGB), the law of the state where the actual work is done governs contracts of employees. The protection of the employees under the law of the state where the work is performed is compulsory and cannot be deprived by a choice of law clause according to Article 30(1) EGBGB. The content, duties, rights and the termination of an employment contract are exclusively governed by German employment law. [241]

2. Section 613a of the Civil Code

The effect of a transfer of a business on existing employment contracts is exclusively governed by section 613a BGB and not the *lex fori concursus*. [242] The general applicability of section 613a of the BGB in insolvency proceedings follows now from sections 113(2), 128(2) InsO. According to these provisions, termination of employment does not occur because of the transfer of the plant

a. Transfer of Existing Employment Contracts

According to section 613a BGB, if a business [243] is conveyed [244] to a third party, the purchaser becomes subject to the rights and obligations of existing employment contracts. Employment contracts can neither be terminated nor altered by the ex−employer nor by the purchaser for the sole reason of the ownership change of the business**.** The termination or alteration of employment contracts remains, however, possible if a sound business reason other than the mere change of ownership can be proven.

b. Limitation of Liability

The purchaser is not liable for claims arising from transferred employment contracts that became due prior to the commencement of the proceeding. Otherwise, pre−petition employees' claims would have preferential treatment over regular creditors' claims. Furthermore, the other creditors would be additionally disadvantaged since the purchaser would probably try to compensate for his obligation to pay pre−petition employees claims by reducing the offer price. The crucial moment for the limitation of the liability of the purchaser is not the time of the transfer of the business, but the time of the commencement of the case. The effect is that the purchaser is liable for all claims arising in between the commencement of the case and the completion of the sale. Therefore, the purchaser is provided an incentive to close the sale as soon as possible once the insolvency proceeding is opened. [245]

O. Parallel Proceeding in Germany

Having outlined the effects of a chapter 11 case in the U.S. on the sale of a business in Germany, it is now necessary to examine the effect of the filing of a parallel proceeding in Germany on such sale.

1. Parallel Full Main Proceeding

Prior to the recognition of a foreign proceeding, a full main proceeding can be opened in Germany if the debtor has its usual venue in Germany. [246] The insolvency proceeding in Germany under the InsO supersedes any subsequent foreign proceeding. [247] In the case of a parallel main proceeding in Germany the InsO therefore disregards the fact that the Code in section 541(a) claims a worldwide range of application even if the actual property of the debtor is located abroad. The appearance of two competing full proceedings is, however, limited. If the U.S. proceeding is filed only on the basis that assets are located in the U.S., the U.S. proceeding will not be recognized under Article 102 EGInsO. [248] Correspondingly, a full proceeding in Germany is not available if the debtor has only assets in Germany. Two full, competing proceedings are therefore only possible if the debtor has its venue under section 3 InsO both in the U.S. and in Germany. [249] However, once the opening of a foreign proceeding has been recognized in Germany, the debtor or its creditors are barred from opening a main proceeding in Germany. [250]

2. Secondary Territorial Proceeding

In the case of a recognized pending foreign proceeding Article 102(3) EGInsO contains the right to file a petition to open a secondary territorial proceeding in Germany.

a. Territorial Scope

A parallel proceeding under Article 102 (3) EGInsO reaches only property of the debtor located in Germany. [251] All assets outside the borders of Germany will not be affected by the secondary proceeding. The assets located in Germany, however, become part of a separate estate under the InsO. Article 102(3) EGInsO therefore totally disregards section 541(a) of the Code. The administration, disposal, exploitation and distribution of the assets situated in Germany are exclusively governed by the InsO. [252] The only impact of the bankruptcy case in the U.S. is that any

assets, which creditors received in the U.S. proceeding, will be credited and deducted from their claims filed in the secondary proceeding in Germany. Any surplus generated under the secondary proceeding in Germany must be transferred for distribution in the U.S. case. [253] Thus, the filing of a secondary proceeding results in the entire sale of the business being governed exclusively by German law. Consequently, the U.S. debtor needs, according to section 160 InsO, the approval of the creditors for the sale of the business. If creditors opposing to the sale have the majority, the filing of a secondary proceeding in Germany consequently provides them with a tool to block the entire sale of the business, which might have drastic consequences on the reorganization in the U.S.

b. Requirements for a Secondary Territorial Proceeding

1) Existence of Property in Germany

In order to file a secondary territorial proceeding in Germany, it is necessary that property of the debtor is located in Germany. [254] Furthermore, a secondary territorial proceeding can only be filed if a full insolvency proceeding is not available. [255] This is the case if the debtor does not have its usual venue in Germany. [256] Assuming the debtor is incorporated in the U.S., and has only assets in form of a business establishment in Germany, a parallel territorial proceeding under Article 102(3) EGInsO would be perfectly possible. Furthermore, once a main proceeding has been opened abroad, the showing of insolvency for the opening of a requested secondary territorial proceeding is not required anymore (Article 102(3) EGInsO).

2) Eligibility

According to sections 13, 14 InsO, the debtor and the creditors are eligible to file a secondary territorial proceeding. [257] In addition, the foreign trustee has this right. [258] It is not required that the petitioner be German in nationality or, in the case of a corporate debtor, be incorporated in Germany. [259] According to section 14(1) InsO, the only requirement for filing a parallel proceeding is that the petitioner has to present a legal interest as to why a parallel territorial proceeding should be opened. This is always the case if a participation in the foreign proceeding must be considered unreasonable. [260] With regard to German creditors, a legal interest can particularly be assumed if they are granted less rights [261] or would receive significantly less in the U.S. case compared to a proceeding under the InsO. [262] This could, for instance, be the case if huge priority or punitive damage claims, which do not exist under German law, consummate most of the assets so that there is nothing left to be distributed to the German creditors.

A petition by a U.S. debtor or creditor, however, would be the exception. The opening of a parallel proceeding in Germany deprives the U.S. estate of the assets located in Germany, and therefore the filing would constitute a violation of the automatic stay, which can cause a heavy fine according to section 362(h) of the Code and thus practically prevents creditors from filing a secondary proceeding in Germany. Thus, the approval of the bankruptcy judge is necessary. [263]

c. Secondary Territorial Proceeding Prior to Foreign Main Proceeding

Subject to debate was the question whether Article 102(3) EGInsO contains the right to file an secondary territorial proceeding in Germany before a full foreign proceeding has been commenced. [264] Article 102(3) EGInsO waives the requirement that the debtor has to be insolvent or over indebted in case a full insolvency proceeding has been commenced in another state. This leads to the conclusion that the filing of a parallel proceeding prior to the commencement of a full proceeding abroad is possible if the illiquidity or overindebtness of the debtor can be proven. [265] Any other interpretation would have the effect that in the case of an involuntary filing the creditor, who pursues a parallel territorial proceeding in Germany, is forced to file first a full proceeding abroad. [266] This would drag the creditor inevitably into an insolvency proceeding abroad with the effect that a parallel territorial proceeding could be dismissed on the grounds of a missing legal interest according to section 14 InsO. An independent territorial proceeding is thus possible. [267]

3. Coordination Between Main and Secondary Proceeding

The trustees in the main and secondary proceeding shall exchange any information that might be relevant to the other proceeding and shall cooperate in the administration of their estates to maximize the total value of the debtor's assets [268] . Furthermore, the foreign trustee has a right to take part in the creditors' assembly. The foreign trustee has, however, not a right to demand a stay of the secondary proceeding and can only suggest how the assets hall be used by the local trustee. [269]

P. Conclusion

In order to achieve the freedoms of establishment of business, the free flow of goods, labor, services, and capital, and to integrate national markets into a unitary market, a functioning cross−border insolvency law is indispensable. [270] This necessity is mirrored in the Federal Bankruptcy Law for all American States and in the European Union Regulation and UNCITRAL Model Rules on Cross Border Insolvencies respectively. [271]

1. The Problem of Cross−Border Insolvency Law

Having analyzed the restrictions upon the recognition of foreign bankruptcy proceedings, and the limited effect of a foreign bankruptcy proceeding on particular branches of the law, [272] it has become clear that the establishment of the universality principle in Article 102 (1) EGInsO is not as universal as one might think on the first view. Bankruptcy law is deeply rooted in national traditions of individual jurisdictions. [273] This problem of multi−national bankruptcy case management is well illustrated in the case of the sale of a business, which affects nearly all branches of the law. As it has been outlined above, security interests, employment contracts or leases, for instance, are of such special sensitivity that the German government was not willing to subject those branches of the law to the rules of a foreign state where an insolvency proceeding may originate. The laws of other jurisdictions, even within the European Union, take quite different approaches to the treatment of secured creditors, employees or tenants in insolvency proceedings. For example, some procedures [274] substantially interfere with rights of security holders by imposing considerable losses on secured creditors for the benefit of the debtor and its reorganization. Other insolvency laws leave the rights of secured creditors largely unaffected. [275] The U.S. debtor is therefore well advised to hire competent counsel in Germany to properly consummate the sale in Germany even if the bankruptcy proceeding, under which the sale is accomplished, is exclusively pending in the U.S. The consequence of these limitations upon a universality principle is more than obvious. The administration of the estate, disposal of property, distribution to creditors and sale of the business, in particular, are significantly complicated due to different applicable laws depending on where the assets are located. The inevitable effect is that the proceeding is delayed and administrative expenses are accumulated which not only reduces the amount to be distributed to the creditors, but might also jeopardize the entire reorganization in the main proceeding. This problem of cross−border insolvencies is not limited to the sale of a business, but occurs in nearly all cases where more than one jurisdiction is concerned. The question is whether anything can be done at the present time to overcome these obstacles.

2. Solution

a. Mitigated Universality

Professor Westbrook of the University of Texas makes the point that a necessary prerequisite to obtain the full benefits of universalism is general similarity of laws. [276] The risk that another countries' law will be applied to such sensitive areas as the sale of an entire business with security interests, employment contracts and leases involved is for the parties much easier to accept, if that law produces results at least basically similar to those where the property is located. [277] On the other hand, no cross−border insolvency system can impose a single body of law applicable to every aspect of a transnational default. [278] Due to fundamental differences in legal culture of common law and civil law systems, [279] and in weighing of the competing interests of the survival of a viable business versus maximum creditor satisfaction and the protection of labor versus economic efficiency, the creation of a single body of law dealing with cross−border defaults appears improbable.

Inevitably, a distinction must be made between matters to be governed exclusively by the law of the main proceeding and those to which the rules of other countries need to be applied. [280] The wholesale exportation of the effects of insolvency proceedings into other states may conflict with interests of local creditors, which the German jurisdiction

recognizes as worthy of protection and which needed to be exempted in order to make recognition acceptable at the present state of economic integration and legal unity within the world. In particular, with regard to the sale of the business, local creditors have rights, which can be exercised in a local insolvency proceeding but not in the foreign main proceeding in the U.S. For example, the right to block the sale of the business not approved by the creditors committee.

A foreign main proceeding might therefore affect the rights of German creditors negatively when the law of the main forum puts the emphasis on the rehabilitation of the debtor over the interests of the German creditors. It is thus more than understandable that a country reserves the right not to recognize a foreign proceeding if the outcome would deviate significantly from its own domestic law, legal convictions and principles. After all, it must be admitted that a limited or mitigated universality approach, as it has been adopted by Germany in Article 102(1) EGInsO, or similarly by the United States with its ancillary proceedings under section 304 of the Code is currently the best solution available in the management of cross−border insolvencies. [281]

b. unity

Whereas some limitations to the universality approach are unavoidable, the author cannot agree with the present possibility of an independent secondary proceeding in Germany. [282] As is has been explained in the above arguments, a secondary proceeding in Germany effects the assets situated in Germany in that they would be governed by a separate German insolvency proceeding exclusively governed by German law. [283] The possibility of a secondary proceeding thus undeniably aims at protecting the interests of local creditors. [284] On the other hand, the possibility of a parallel proceeding discards the principle of universality significantly in scope. The insolvency of the U.S. debtor would be resolved not only by a U.S. but also by a German court, each applying its own rules to questions of administration and distribution. These rules, as it was mentioned earlier, can be very different concerning the standard of approval for the sale, [285] security interests, [286] employment contracts [287] and leases related to the business and thus produce very different outcomes and add to the complexity of the case.

The inability to predict whether creditors might file a secondary proceeding and the results of the application of the local law to such a secondary proceeding on the reorganization in the main forum might destroy the value of assets that would otherwise be preserved for the reorganization of the business. [288] A successful reorganization is not promoted if one corporation is dismembered in two distinct insolvency proceedings, applying two different bodies of law, disregarding the natural economic unity. [289] Furthermore, even if a legal interest must be proved to open a secondary proceeding, the threat of abuse can never be totally removed.

The filing of a secondary proceeding in Germany confers the power upon the creditors to block the entire sale of the business, assuming those dissenting creditors have the majority in the creditors' committee. Thus, creditors can block or at least delay and, therefore, jeopardize the entire reorganization in the foreign main proceeding. Even without the actual intent to disapprove the sale of the business, the mere threat to block the sale by filing a secondary proceeding in Germany gives the creditors a very powerful bargaining tool in the reorganization proceeding in the U.S. Furthermore, taking into account the limitations of recognition of the effects of foreign proceedings as embodied in the *ordre public* restriction, the interests of local creditors are sufficiently protected without the need to provide further safeguards by implementing the possibility of a secondary proceeding. It makes little sense if the legislator establishes on the one hand a system of universality in Article 102(1) EGInsO but at the same time provides for the possibility of a secondary territorial proceeding in Article 102(3). That would deprive parties of all the benefits of the universality principle. Cross−border cases should be resolved in one central main forum, and courts in all other countries should act in an ancillary capacity to the home country court. Efficient cross−border insolvency law must guarantee that bankruptcy proceedings will be mutually recognized by all states embodying the principle of universality subject to an *ordre public* limitation which mitigates the principle of universality and that a bankruptcy proceeding opened in one state would bar all other states from opening secondary proceedings creating a system of unity.

FOOTNOTES:

[1] Gerald I. Lies is the American Bankruptcy Institute Scholar for 2001. This thesis was prepared during the LL.M. in Bankruptcy Program at St. John's University, School of Law, New York, 2001−02. Prior to his participation in the LL.M. program, the author studied and interned in Germany, Austria, England and Japan. He received his First Juridical State Examination (J.D. equivalent) before the Court of Appeals Cologne, in September, 2000. Mr. Lies will start his clerkship at the Court of Appeals, Bremen, Germany, in October 2002. The author would like to thank Prof. Robert N. Zinmam, Prof. Christopher F. Graham, Prof. Adam L. Rosen and Prof. Edward D. Re for their advice and guidance. Special thanks to Prof. Francis G. Conrad as the author's thesis mentor and the staff of the American Bankruptcy Institute Law Review. Back To Text

[2] See Cross−border insolvency: national and comparative studies: reports delivered at the XIII International Congress of Comparative Law, Montreal, 1990 at 1 (Ian F. Fletcher ed., Tubingen 1992); see also In re Corporation, 34 B.R. 845, 850 (Bankr. Md. 1983) (noting widespread use by debtors of bankruptcy provisions); In re Hawkins, 33 B.R. 908, 912 (Bankr. S.D.N.Y. 1983) (declaring abuse of fresh start policy is not widespread). Back To Text

[3] See generally Vern Countryman, A History of American Bankruptcy Law (1976); F. Noel, A History of Bankruptcy Law (1919); Charles Warren, Bankruptcy in the United States History (1935). Back To Text

[4] See Manfred Balz, The European Convention on Insolvency Proceedings, 70 Am. Bankr. L.J. 485, 486 (1996) (outlining issues arising "when a case has links with more than one jurisdiction"); Jay Lawrence Westbrook, Theory and Pragmatism in Global Insolvencies: Choice of Law and Choice of Forum, 65 Am. Bankr. L.J. 457, 458 (1991) (observing "legal treatment of troubled multinationals is primitive and chaotic"); see also Edgar J. Habscheid, Grenzueberschreitendes (internationales) Insolvenzrecht der Vereinigten Staaten von Amerika und der Bundesrepublik Deutschland [Cross−Border International Insolvency Law of the United States of America and the Federation Republic of Germany], 8 (1998). In particular, the economies of the United Sates of America and Germany are closely intertwined. U.S. enterprises often have a stake in German enterprises and vice versa. The most spectacular case was the bankruptcy of the Herstatt−Bank in 1974. See generally Gert Spennemann, Insolvenzverfahren in Deutschland – Vermögen in den U.S.A, [Insolvency Proceeding in Germany – Assets in the U.S.A] (1981). This case had an enormous impact on the 1978 bankruptcy reform in the United States and lead to the enactment of section 304 of the Bankruptcy Code (hereinafter the "Code") which provides for the filing of cases in the United States ancillary to foreign proceedings. Back To Text

[5] The appointment of a trustee under section 1104 of the Code is the exception and the debtor remains in most cases in possession (debtor in possession, hereinafter the "DIP") and has, according to section 1107 of the Code, all the rights and powers and shall perform all the functions and duties of a trustee. In this paper, only the expression "DIP" is used. See 11 U.S.C. § 1104 (1994) (providing for appointment of trustee or examiner); id. § 1107 (dictating rights, powers and duties of debtor in possession); see also In re Hempstead Realty Associates, 34 B.R. 624, 625 (Bankr. S.D.N.Y. 1983) (dealing with need for appointment of special counsel to assist debtor in possession). Back To Text

[6] See Reginald W. Jackson, Sale of Substantially all Assets Outside of Plan, New York City Bankruptcy Conference Educational Materials, 67 (2001); Wolfgang Marotzke, Das Unternehmen in der Insolvenz, Fortführung und Veräußerung zwischen Eröffnungsantrag und Berichtstermin [The Insolvent Business, Continuation and Sale Between the Petition to Open Insolvency Proceedings and the Report Meeting], Rn. 1 (2000); see also Fred Feingold and Mark E. Berg, Whither The Branches?, 44 Tax L. Rev. 205, 226−27 (1989) (discussing tax ramifications with respect to liquidation of foreign corporations). Back To Text

[7] See 11 U.S.C. § 363(b) (1994) (allowing Trustee to "use, sell, or lease, other than in the ordinary course of business, property of the estate"); see also Kopp v. All American Life Ins. Co. (In re Kopexa Realty Venture Co.), 1997 Bankr. LEXIS 2345, at *6 (B.A.P. 10th Cir. Feb. 28, 1997) (explaining ability to challenge sale to good faith purchaser); In re America West Airlines, 166 B.R. 908, 912 (Bankr. Ariz. 1994) (stating "[w]hen a transaction is out of the ordinary course of business, after notice and a hearing, it falls to the Bankruptcy Court to determine whether to approve the transaction based on the facts and history of the case."). Back To Text

[8] Whereas liquidating plans are now explicitly authorized in chapter 11 cases under the Bankruptcy Code, the lawfulness of such liquidating plans under the Bankruptcy Act was subject to much controversy. See 11 U.S.C. § 1123

(a)(5)(D) (1994) (allowing plan to include "merger or consolidation of the debtor with one or more persons"); id. § 1123 (b)(4) (noting plan can "provide for the sale of all or substantially all of the property of the estate, and the distribution of the proceeds of such sale among holders of claims or interests"); id. § 1141(d)(3)(A) (stating confirmation of plan does not discharge debtor if, among other requirements, "the plan provides for the liquidation of all or substantially all of the property of the estate"). See generally Patent Cereals v. Flynn, 149 F.2d. 711, 713 (2d Cir. 1945) (allowing liquidation in furtherance of reorganization proceeding). Back To Text

[9] See 121 U.S.C. §§ 1123(a)(5)(D), 1123(b)(4), 1141(d)(3)(A) (1994). Back To Text

[10] See Marotzke supra note 5, Rn.1, 44. Back To Text

[11] See John J. Hurley, Chapter 11 Alternative: Section 363 Sale of all of the Debtor's Assets Outside a Plan of Reorganization, 58 Am. Bankr. L.J. 233, 236−41 (1984) (providing historical background of sale of debtor's assets outside plan under Bankruptcy Code) [hereinafter Hurley]; see also In re Pullman Construction Industries, 107 B.R. 909, 943 (Bankr. N.D. Ill. 1989) (discussing case where going concern value of enterprise equaled forced liquidation value of same); In re Hoff, 54 B.R. 746, 752−53 (Bankr. D. N.D. 1985) (speculating debtor may be forced into liquidation prior to confirmation of plan). Back To Text

[12] The method of valuation of a business as a going concern is an assessment based on future earning capacity, rather than the utilization of a procedure based on either the market value of outstanding stocks and bonds or the book value of the corporation's assets. See Grant W. Newton, Bankruptcy and Insolvency Accounting 462 (Wiley 6th ed. 2000); see also Whittaker v. Citra Trading Corp. (In re International Diamond Exchange Jewelers), 177 B.R. 265, 269 (Bankr. S.D. Ohio 1995) (challenging insolvency based on calculation of going concern value); In re Vadnais Lumber Supply, Inc., 100 B.R. 127, 132 (Bankr. D. Mass. 1989) (using annual earning capacity to calculate going concern value). Back To Text

[13] See Hurley, supra note 10, at 248; see also In re Keck, Mahin & Cate, 241 B.R. 583, 591 (Bankr. N.D. Ill. 1999) (expressing concern over additional administrative costs associated with conversion of case to chapter 7); In re Digital Impact, 223 B.R. 1, 6 (Bankr. N.D. Okla. 1998) (stating "liquidation would result in additional administrative expenses"). Back To Text

[14] See 11 U.S.C. § 363 (1994) (stating requirements for use, sale, lease of property of bankruptcy estate in general); see also id. § 507(a) (listing order of priority claims for repayment in confirmation plan).

The requirements for the confirmation of a plan are payments in cash on the effective date of the plan of claims for administrative expenses allowed pursuant to section 507(a)(1) and unsecured claims arising under sections 507(a)(2) and section 502(f). See id. § 1129 (a)(9)(A). Furthermore, the plan must provide for cash payments on the effective date of the plan, or deferred cash payments, on claims for wages, salaries or commissions, section 507(a)(4) claims for contributions to employee benefit plans, section 507(a)(4), claims of farmers and fishermen under section 507(a)(5), consumer deposits under section 507(a)(6) and alimony and maintenance claims under section 507(a)(7). See id. § 1129(a)(B). Finally, the plan must provide for payment within six years of the date of assessment of claims of governmental units under section 507(a)(8). See id. § 1129(a) (9) (C). Back To Text

[15] See Indian Motorcycle Assoc. v. Drexel Burnham Lambert Group (In re Drexel Burnham Lambert), 157 B.R. 532, 537 (S.D.N.Y. 1993) (adopting vertical and horizontal analyses to determine whether debtor's activity was within or outside ordinary course of business); see also Armstrong World Industries v. Phillips (In re Phillips), 29 B.R. 391, 394 (S.D.N.Y. 1983) (stressing vertical analysis is essentially creditor's expectation test that benchmarks debtor's action against usual, internal modus operandi of debtor's business and interests of hypothetical creditor); Committee of Asbestos−Related Litigants and/or Creditors v. Johns−Manville Corp (In re Johns−Manville Corp), 60 B.R. 612, 616 (Bankr. S.D.N.Y. 1986) (claiming vertical analysis requires court to "examine the debtors transaction from the vantage point of a hypothetical creditor and to inquire whether the transaction subjects the creditor to economic risk of a nature different from those he accepted when he decided to extend the credit"); Johnston v. First Street Com. (In re Waterfront Companies), 56 B.R. 31, 35 (Bankr. D. Minn. 1985) (using horizontal analysis to compare debtor's business to other similar businesses, to decide whether type of transaction is in course of that debtor's business or in

course of some other business). That the sale of an entire business is not in the ordinary course of business is evident. Back To Text

[16] See 11 U.S.C. § 102(1)(A) (defining "after notice and hearing" to mean after such notice is appropriate in such particular circumstances, and such opportunity for hearing as is appropriate in such particular circumstances); see also id. § 102(1)(B) (authorizing action without actual hearing if such notice is given properly and if such hearing is not requested timely by party in interest or if there is insufficient time for hearing to be commenced before such act must be done, and court authorizes such action); Federal Rules of Bankruptcy Procedure [hereinafter, the "Bankruptcy Rules"] 6004(a), 2002(a)(2) (2000) (requiring notice to be mailed and have lead time of at least twenty days unless court, for shown cause, shortens time or directs another method of giving notice); Bankruptcy Rule 6004(f)(1) (allowing sales to be performed by private or public auction); Bankruptcy Rule 2002(c)(1) (providing notice should include time and place of any public sale, terms and conditions of any private sale, time fixed for filing objections, and general description of the property); Bankruptcy Rule 6004(b) (requiring, unless otherwise fixed by court, objections must be filed at least five days before date set for act); Bankruptcy Rules 7001, 9014 (providing debtor in possession's request for approval of proposed sale may be in form of motion and does not require complaint, unless proposed sale is to be of debtor's and any co−owner's interest in property pursuant to section 363(h) of the Code). Back To Text

[17] See In re Wilde Horse Enter., 136 B.R. 830, 841 (Bankr. C.D. Cal. 1991) (stating "[t]he ultimate purpose of any sale of property of the estate is to obtain the highest price for the property sold."); see also Institutional Creditors of Continental Air Lines, Inc. v. Continental Air Lines, Inc. (In re Continental Air Lines. Inc.), 780 F.2d 1223, 1227−28 (5th Cir. 1986) (demonstrating when debtor proposes to sell property free and clear of liens or interests, section 363(f) of Code imposes various additional requirements, and, if applicable, sections 363(d) and (e) of Code impose additional restrictions on asset transfers); Holland v. First Federal Savings (In re Terell), 27 B.R. 130, 132 (Bankr. W.D. La. 1983) (declaring it is trustee's duty to obtain highest sales price possible). Back To Text

[18] See H.R. Rep. No. 95−595, at 224 (1977); see, e.g., Dep't of Medical Assistance Service v. Shenandoah Realty Partners (In re Shenandoah Realty Partners), 248 B.R. 505, 513 (W.D. Va. 2000) (relying on chapter XI of Bankruptcy Act to interpret 11 U.S.C. § 1141(c) in connection with section 363(b)); In re Lehigh Valley Professional Sports Club, Inc., 2000 WL 290187 at *11−12 (Bankr. E.D. Pa. Mar. 14, 2000) (discussing relevance of chapter XI of Bankruptcy Act to shed light on legislative intent behind 11 U.S.C. § 1121). Back To Text

[19] See generally Bankruptcy Act of 1867, 14 Stat. 517 (1867) repealed by, 20 Stat. 99 (1878); see also John C. Anderson and Peter G. Wright, Liquidating Plans of Reorganization, 56 Am. Bankr. L.J. 29, 29−30 (1982) (referring to absence of reorganization proceedings under former Bankruptcy Act); William L. Cary, Liquidation of Corporations in Bankruptcy Reorganizations, 60 Harv. L. Rev. 173 (1946) (highlighting lack of reorganization proceeding under former Bankruptcy Act). Back To Text

[20] Bankruptcy Act of 1867, § 25, 14 Stat. 517, 528:

And be it further enacted, That when it appears to the satisfaction of the court that the estate of the debtor, or any part thereof, is of a perishable nature, or liable to deteriorate in value, the court may order the same to be sold, in such manner as may be deemed most expedient, under the direction of the messenger or assignee, as the case may be, who shall hold the funds received in place of the estate disposed of...

Id. (emphasis added and in original). See In re Lional Corp., 722 F.2d 1063, 1067 (2d. Cir. 1983) (recalling "perishable" is not limited to its physical meaning, but includes property subject to deterioration in price and value); Hill v. Douglass, 78 F.2d 851, 854 (9th Cir. 1935) (acknowledging liberal construction of "perishable" to include not only property which may physically deteriorate, but also that which deteriorates in price and value); In re Pedlow, 209 F. 841, 842 (2d Cir. 1913) (interpreting meaning of "perishable" to include property liable to deteriorate in price and value). Back To Text

[21] Bankruptcy Act of 1867, § 25, 14 Stat. 517, 528; see also General Order in Bankruptcy, No. XVIII (3), 89 F. viii (November 28, 1988) adopted by the Supreme Court in 1898 (repealed 1978) (containing same requirements that property must be of perishable nature and subject to loss if not sold immediately); In re Lionel Corp., 722 F.2d at

1066−67 (discussing section 25 of Bankruptcy Act of 1867). Back To Text

[22] See In re Pedlow, 209 F. 841 (2d Cir. 1913). Back To Text

[23] The first major decision interpreting this provision was Flynn v. Brewery Management Corp. (In re V. Loewer's Gambrinus Brewery Co.), 141 F.2d 747, 748 (2d Cir. 1944) (approving sale of virtually all of income producing assets of debtor, including vats, kettles and other brewing machinery). The Court rejected the argument that the sale would most probably prevent any adoption of a plan of reorganization and would consequently contradict the very purpose of the reorganization chapter. The Court stated that section 116(3) of the Act allows the sale of all assets and authorized the sale because due to a lack of use and refrigeration, the property will deteriorate rapidly in the warm weather and lose substantially all its value. See Patent Cereals v. Flynn, 149 F.2d 711, 712 (2d Cir. 1945) (stressing it made no difference whether sale of property of estate preceded or was made part of reorganization plan). Back To Text

[24] 176 F.2d 493 (3d Cir. 1949). In this case the trustee proposed to sell all of the assets of the debtor except cash and inventory to a competitor. The court noted that such pre−confirmation sales are "not surrounded by the rather elaborate safeguards which Congress has provided to protect the interests of those whose money is tied up in the tottering enterprise." The court held that the only reason for the sale was that the purchaser did not want to wait until the plan confirmation which does not qualify as an emergency exception. See In re Sire Plan, Inc., 332 F.2d 497, 499 (2d Cir. 1964) (pointing to deteriorating state of asset as grounds for emergency sale); In re V. Loewer's Gambrinus Brewery Co., Inc., 141 F.2d 747, 749 (2d Cir. 1944) (articulating need for emergency provision within Chandler Act). Back To Text

[25] In re Solar Mfg. Corp., 176 F.2d at 494; see In re Lionel Corp., 722 F. 2d 1063, 1068 (2d Cir. 1983) (finding sale of non−perishable property did not fit into definition of emergency sale); In re Pure Penn Petroleum, 188 F. 2d 851, 851 (2d Cir. 1951) (holding burden on debtor to make showing of emergency need for sale). Back To Text

[26] Collier's treatise properly noted: "The use of the word 'emergency' as a standard or justification for sales generally should not be allowed to distort the statute so that sales may be effected only if near catastrophe threatens. Section 116 (3) says upon cause shown, which conceivably could be evoked by conditions other than those normally thought of as emergencies." 6 Collier on Bankruptcy, ¶¶ 3.13, 3.27 at 626−27 n.25 (Lawrence P. King et al. eds., 15th ed. Rev. 1999). Back To Text

[27] See In re Wonderbowl, Inc., 424 F. 2d 178, 179 (9th Cir. 1979) (citing litany of cases criticizing limiting view in Solar); In re Equity Funding of America, 492 F.2d 793, 794 (9th Cir. 1974) (recognizing court's power to order sale in less than emergency circumstances); International Bank of Miami v. Brock, 400 F.2d 833, 836 (5th Cir. 1968), aff'd, 393 U.S. 1118, (noting statutory standard was upon cause shown, not "emergency"); Irving V. Capehart, 394 F.2d 900, 903 (7th Cir. 1968) (holding judge has broader power to order sale), aff'd, 393 U.S. 801; In re Marathon Foundry and Machine Co., 228 F. 2d 594, 597−98 (7th Cir. 1955) (finding question of ordered sale's propriety resolved by examining circumstances). Back To Text

[28] In re Wonderbowl, 424 F.2d at 180. Back To Text

[29] 400 F.2d 833 (5th Cir. 1968), cert. denied sub. nom., International Bank of Miami v. Brock, 393 U.S. 1118 (1969). Even though no emergency existed the court affirmed a sale of approximately 175,000 shares of stock whose values were deteriorating rapidly. The court regarded the fact that the sale would generate "substantial equity" for the debtor as sufficient to meet the requirement for cause shown. Back To Text

[30] In re Alves Photo Service, Inc., 6 B.R. 690, 692 (Bankr. D. Mass. 1980) (finding liquidation should be recognized as such when it causes damage to estate under chapter 11). Back To Text

[31] These requirements include: the filing of a written disclosure statement, and a hearing upon notice to creditors and parties in interest to determine the adequacy of the information contained in the disclosure statement. Pursuant to section 1125(b) of the Code, solicitation of the votes on the plan from holders of claims against or interests in the debtor. Pursuant to section 1126 of the Code, a hearing on confirmation of the plan is held to determine if all

requirements for confirmation have been met under section 1129 of the Code. See 11 U.S.C. §§ 1125 (b), 1126, 1129 (1994). Back To Text

[32] See Hurley, supra note 10, at 236−41; see also, In re Brookfield Clothes, Inc., 31 B.R. 978, 981 (Bankr. S.D.N.Y. 1983) (honing in on good faith requirement of sale under section 363); In re Ancor Exploration Company, 30 B.R. 802, 808 (Bankr. N.D. Okla. 1983) (exploring three factors in determining permissibility of section 363 sale). Back To Text

[33] In re D.M. Christian Co., 7 B.R. 561, 562−63 (Bankr. N.D. W.Va. 1980). Back To Text

[34] See id. at 562; see also In re Ancor Exploration, 30 B.R. at 806 (discussing conflicting views on chapter 11 compliance requirements before asset sales). Cf. Hurley, supra note 10, at 235 (noting principle arguments against allowing asset sale before confirmation of plan). Back To Text

[35] 14 B.R. 584 (Bankr. N.D. Ohio 1981). Back To Text

[36] See id. at 587. Back To Text

[37] H.R. Doc. No. 93−137, at 238−39 (1973); In re White Motor, 14 B.R. at 589 (noting Congressional desire to preserve "emergency doctrine"); see also In re Brookfield Clothes, Inc., 31 B.R. 978, 984 n.8 (S.D.N.Y. 1983) (discussing legislative intent to retain "emergency doctrine" in situations where exigent circumstances exist). Back To Text

[38] See In re White Motor, 14 B.R. at 590; see also Hurley, supra note 10, at 241 (discussing bankruptcy court's power to approve sale under section 105 powers) See generally In re Allison, 39 B.R. 300, 302 (Bankr. N.M. 1984) (noting general principles that guide courts' allowance of pre−plan asset sales in cases of emergency). Back To Text

[39] See Connel v. Coastal Cable T.V., Inc. (In re Coastal Cable T.V., Inc.), 24 B.R. 609, 611 (B.A.P. 1st Cir. 1982) (holding sale of all or most of debtor's assets is permitted under chapter 11, even before confirmation of plan), vacated by 709 F.2d 762 (1st Cir. 1983); In re Boogart of Florida, Inc., 17 B.R. 480, 484 (Bankr. S.D. Fla. 1981) (allowing pre−confirmation sale based on asset depreciation an estate suffering); In re Searles Castle Enterprises, Inc., 12 B.R. 127, 129 (Bankr. D. Mass. 1981) (stating chapter 11 debtor in possession was entitled to sell its entire business as "going concern" and this sale could not be vetoed by majority stockholder), aff'd, 17 B.R. 440 (B.A.P. 1st Cir. 1982); In re WFDR, Inc., 10 B.R. 109, 111 (Bankr. N.D. Ga. 1981) (holding current management of bankrupt radio station was entitled to sell radio station without approval of chapter 11 plan); Circus Time, Inc. v. Oxford Bank and Trust (In re Circus Time, Inc.), 5 B.R. 1, 3 (Bankr. D. Me. 1979) (permitting sale free and clear of creditor's liens). Back To Text

[40] 12 B.R. 743 (Bankr. D. Mass. 1981). Back To Text

[41] 31 B.R. 978 (Bankr. S.D.N.Y. 1983). Back To Text

[42] Missouri, Kansas & Texas Railway Co. v. May, 194 U.S. 267, 270 (1904). Back To Text

[43] 722 F.2d 1063 (2d Cir. 1983). Back To Text

[44] In re Stephens Indus., Inc., 789 F. 2d 386, 390 (6th Cir. 1986) (stating approval of sale of assets of radio station under Lionel standard, due to trustee's inability to run radio station at profit and inability to meet its payroll and other operating expenses); In re Pub. Serv. Co., 90 B.R. 575, 581 (Bankr. D. N.H. 1988) (stating appropriate standard for approval or disapproval of transactions by reorganization courts is whether good cause has been shown to implement transaction); see also In re Ancor Exploration Company, 30 B.R. 802, 806 (Bankr. N.D. Okla. 1983); Honorable William T. Bodoh, The Parameters of the Non−Plan Liquidating Chapter Eleven: Refining the Lionel Standard, 9 Bankr. Dev. J. 1, 12−13 (1992) (discussing Hunt Energy Co. v. United States (In re Hunt Energy Co.), 48 B.R. 472 (Bankr. N.D. Ohio 1985). Back To Text

[45] In re Lionel, 722 F.2d at 1071; see In re Fin. News Network Inc., 980 F.2d 165, 170 (2d Cir. 1992) (noting bankruptcy court's discretion must be sufficiently broad so it can consider finality of bidding process and fairness to bidders balanced against interests of creditors); In re Integrated Res. Inc., 147 B.R. 650, 656 (Bankr. S.D.N.Y. 1992) (stating business judgment rule is standard applied to debtor). Back To Text

[46] For cases where sale was denied: see In re Plabell Rubber Prods., Inc., 149 B.R. 475, 479 (Bankr. N.D. Ohio 1992) (stating proof of urgency of transaction to one of several potential bidders was missing); In re Au Natural Rest., Inc., 63 B.R. 575, 580 (Bankr. S.D.N.Y. 1986) (noting debtor did not prove sufficiently why sale could not have been made part of liquidating chapter 11 plan).

For cases where sale was approved: In re Ionosphere Clubs, Inc., 100 B.R. 670, 676 (Bankr. S.D.N.Y. 1989) (noting debtor demonstrated need for substantial cash as soon as possible to keep business operating); In re Boogart of Fla., Inc., 17 B.R. 480, 483 (Bankr. S.D. Fla. 1981) (citing rapidly depreciating value of assets). Back To Text

[47] See In re Plabell Rubber Products, Inc., 149 B.R. at 479−80 (citing unfair advantage of ESOP and questionable role of debtor's vice president); In re Industrial Valley Refrigeration and Air Conditioning Supplies, Inc., 77 B.R. 15, 22−23 (Bankr. E.D. Pa 1987) (noting unfair subsidies to insider); In re Crutcher Res. Corp., 72 B.R. 628, 632 (Bankr. N.D. Tex. 1987) (noting parent and lender's attempt to rush sale to avoid examination of subsidiaries); see also In re Stroud Ford, Inc., 163 B.R. 730, 733 (Bankr. M.D. Pa. 1993) (stating sale denied due to collusion of purchaser with higher bidders by buying out their objection and thus preventing estate from receiving adequate compensation). Back To Text

[48] See In re Searles Castle Enter., Inc., 17 B.R. 440, 441 (B.A.P. 1st Cir. 1982) (stating price agreed to pay was approximately $ 57,000.00 more than fair market value of property); In re Weatherly Frozen Food Group, Inc., 149 B.R. 480, 483 (Bankr. N.D. Ohio 1992) (stating misconduct that would destroy a purchaser's good faith status at judicial sale involves fraud, collusion between purchaser and other bidders or attempt to take grossly unfair advantage of other bidders); In re Titusville Country Club, 128 B.R. 396, 399 (Bankr. W.D. Penn. 1991) (finding assets were purchased in good faith at public auction conducted in open court after appropriate notice); In re Oneida Lake Dev., Inc., 114 B.R. 352, 357 (N.D.N.Y. 1990) (stating under circumstances proposed sale price must be at best price obtainable); Circus Time, Inc. v. Oxford Bank & Trust (In re Circus Time, Inc.), 5 B.R. 1, 3 (Bankr. D. Me. 1979) (stating fair and reasonable price must be determined in view of difficulties experienced by debtor). Back To Text

[49] See In re Country Manor of Kenton, Inc., 172 B.R. 217, 220−21 (Bankr. N.D. Ohio 1994) (noting property had not been advertised nor put on real estate market and proposed purchase price was less than half scheduled value); In re Eng. Prods. Co., Inc., 121 B.R. 246, 249 (Bankr. E.D. Wis. 1990) (stating persons in interest must be given adequate notice of sale and opportunity to be heard and object); In re Naron & Wagner Chartered, 88 B.R. 85, 88 (Bankr. D. Md. 1988) (stating appropriate notice should be functional substitute for adequate information which would be contained in disclosure statement concerning proposed transaction). Back To Text

[50] In re Braniff Airways, Inc. 700 F. 2d 935 (5th Cir. 1983). In Braniff the court hold that the requirements under the purchase agreement (secured creditors had to vote a portion of their deficiency claims in favour of any plan approved by the unsecured creditors' committee and all parties were obliged to release claims against Braniff, its secured creditors and its officers and directors) constituted much more than the sale of Braniff's property authorized by section 363 (b) of the Code. To the contrary, by altering the liens and encumbrances the sale had instead the practical effect of dictating some of the terms which could only be resolved in a future reorganization plan. Consequently, the court held that the sale was not within the scope of section 363 (b) of the Code and could therefore not be authorized. Id. Back To Text

[51] In re Lionel, 722 F.2d 1063, 1071 (2d Cir. 1983) (stating "[t]he need for expedition, however, is not a justification for abandoning proper standards") (quoting Ferry, Inc. v. Anderson, 390 U.S. 414, 450 (1968)). Back To Text

[52] For a general explanation of the new law, see: Reinhard Bork, Einfuehrung in das neue Insolvenzrecht [Introduction to the New Insolvency Law] (1995); Eberhard Braun & Wilhelm Uhlenbruck, Unternehmensinsolvenz [Business Insolvency] (1997); Ulrich Breuer, Das neue Insolvenzrecht [The New Insolvency Law] (1998); Hans Haarmeyer, et

al., Handbuch zur Insolvenzordnung [Insolvency Law Manual] (1998); Ludwig Haesemeyer, Insolvenzrecht [Insolvency Law] (1998); Wolfgang Henckel & Gerhard Kreft, Insolvenzrecht [Insolvency Law] (1999); Harald Hess, et al., InsO '99 – Das neue Insolvenzrecht [InsO '99 – The New Insolvency Law], RWS−Skript 1999, 296; Manfred Obermueller, Et al., Insolvenzordnung [Insolvency Act] (1999); Stefan Reinhart, Die neue Insolvenzordnung [The New Insolvency Act], MDR 1999, 203; Stefan Smid, Grundzuege des neuen Insolvenzrechts [Fundamentals of the New Insolvency Law] (1999); Wilhelm Uhlenbruck, Das neue Insolvenzrecht [The New Insolvency Law] (1994); Klaus Wimmer, Erste Erfahrungen mit der Insolvenzordnung [First Experiences with the Insolvency Act], ZInsO 556 (1999). Back To Text

[53] See Hans−Peter Kirchhof, Leitfaden zum Insolvenzrecht [Insolvency Law Guideline] (2000), Rn. 82; see also the statistic in ZinsO 707 (1999). Back To Text

[54] Insolvenzen weiter gestiegen [Considerable Increase in Insolvencies], Frankfurter Allgemeine Zeitung, June 4, 1996, at 15. Back To Text

[55] See Klaus Kamlah, The New German Insolvency Act: Insolvenzordnung, 70 Am. Bankr. L.J. 417, 422 (1996) (noting chapter 11 favors reorganization over liquidation); Amtliche Begruendung [Official Explanation of the Legislative Draft of the InsO], reprinted in 1/92 BR−DS 75, 77 (Mar. 1, 1991) (stating chapter 11 influenced this legislation). Back To Text

[56] See Wolfram Henckel, Deregulierung im Insolvenzverfahren? [Deregulation in Insolvency Proceedings?], 1992 KTS 477, 494 (1992); Kamlah, supra note 54, at 424 (stating "the debtor loses the tactical advantage of filing for reorganization when success is unlikely and holding off creditors until the court decides to convert the proceeding to a liquidation."). Back To Text

[57] See Kamlah, supra note 54, at 424 (recognizing without knowing whether insolvency will proceed as liquidation or reorganization, planning business relationships is not feasible); Henckel, supra note 55, at 487. Back To Text

[58] See Balz, supra note 3, at n.23. Back To Text

[59] See id. at n.61. According to section 270 InsO, the debtor may remain in possession only if the insolvency court orders personal management of the debtor while deciding on the opening of the insolvency proceedings. The order allowing the debtor to remain in possession requires the debtor's request, section 270(2) No.1 InsO. If a creditor has requested the opening of insolvency proceedings, the consent of the creditor to the debtor's request is necessary, section 270(2) No.2 InsO. Lastly, section 270(2) No. 3 InsO requires that, in accordance with the circumstances, it is to be expected that the order of the court will not lead to a delay in the proceedings or other disadvantages to the creditors. Furthermore, according to section 272 InsO, the court shall repeal its decision ordering personal management if requested by the creditors' assembly, by a secured creditor or by a creditor of the insolvency proceedings, and if the prerequisite under section 270 (2) No. 3 InsO has been removed. The German law is therefore in sharp contrast to the U.S. law. According to section 1104(a) of the Code, the bankruptcy court shall order the appointment of a trustee only on request of a party in interest after notice and a hearing and only for cause shown or if the appointment is in the best interest of the creditors. Furthermore, even if the court grants under the InsO the debtor's request to remain in possession, a custodian shall be appointed instead of the insolvency trustee, according to section 270(3) InsO. The most important function of the custodian is to verify the debtor's economic situation and monitor the management of the business, section 274(3) InsO. If the custodian gets knowledge of circumstances suggesting disadvantages to the creditors, he must disclose such circumstances immediately to the creditors' committee and to the insolvency court. The custodian is therefore comparable to the examiner under section 1104(c) of the Code. Back To Text

[60] See Balz, supra note 3, at n.6; Harald Ehlers, Amerikanische Erfahrungen mit Chapter 11 und die Insolvenzreform in Deutschland [American Experiences with Chapter 11 and the Insolvency Reform in Germany], ZIP 2025 (1998). Back To Text

[61] See InsO §§ 16−19. The general reason to open an insolvency proceeding, pursuant to section 17 InsO, is illiquidity of the debtor. The debtor is deemed illiquid if he is unable to meet his mature obligations to pay. Illiquidity shall be presumed as a rule if the debtor has stopped payments. Further reasons to open an insolvency proceeding, pursuant to sections 18 and 19, are imminent illiquidity and over−indebtness of the debtor. The debtor shall be deemed to be imminently illiquid if he is likely to be unable to meet his existing obligations to pay on the date of their maturity. The inability to pay 10% of the debts and a 50% likelihood is sufficient. Creditors can, however, not use imminent illiquidity as a reason to open an insolvency proceeding. The legislator wanted to exclude the possibility of involuntary filings at such an early time. See Kirchhof, supra note 52, Rn.113. Over−indebtness shall exist if the assets owned by the debtor no longer cover his existing obligations to pay. According to section 19(2) InsO, the continuation of the enterprise shall be taken as a basis, if, according to the circumstances, such continuation is deemed highly likely. This standard is comparable to the decision of Assoc. Commercial Corp. v. Rash, 520 U.S. 953 (1997) (noting that valuation should be determined in light of proposed disposition or use of property). Back To Text

[62] See InsO § 26. The insolvency court shall refuse a request to open insolvency proceedings if the debtor's assets will probably be insufficient to cover the costs of the proceeding. Such refusal can be avoided if a sufficient amount of money is advanced. Back To Text

[63] The appointment of a trustee is normal procedure under the InsO, unlike the Code. See supra note 58. The broad powers of a DIP under the Code are heavily criticized by German scholars. See, e.g., Reinhard Bork, Der Insolvenzplan [The Insolvency Plan], ZZP, 473, 482 (1996). Back To Text

[64] See InsO § 22(1). The powers of a strong temporary insolvency trustee are thus comparable with those of a trustee under section 1106 of the Code. See 11 U.S.C. § 1106 (1994). Back To Text

[65] See Kirchhof, supra note 52, Rn. 334. Back To Text

[66] Whereas the U.S. bankruptcy court is a court of equity and a U.S. judge asks under the concept of common law whether there is anything in the Code that restrains him from granting the order, the German judge needs under civil law principles a provision in the Act which allows him to grant the action in question. This distinction is based on the difference between common law and civil law. Common law prefers broad discretion of the judge, whereas civil law puts the emphasis on the language of the statute and predictability. This statement emerged from a discussion with Professor Francis G. Conrad during the class on multinational case management of the LL.M in bankruptcy program at St. John's University, School of Law, NY. See Robert Adriaansen, At the Edges of the Law: Civil Law v. Common Law A Response to Professor Richard B. Capalli, Temple Int'l. & Comp. L.J., 107, 107−08, (1998) (arguing common law lawyer cannot understand how "dry" Code which is severely limited but comparable to "black letter" law, can solve multitude of practical situations. On the other hand, a civil law lawyer cannot understand how a common law judge can be a source of law without risking anarchy and arbitrariness. If there is no explicit statutory provision dealing with the issue in question, a civil law judge can only attempt to interpret the statute to say what it does not really say). Back To Text

[67] The reason that the InsO contains no provision concerning the sale of the enterprise in the opening proceeding might be that the legislature considered the involvement of the creditors in the decision whether to sell the enterprise as so important that it did not even consider the possibility of a sale during the opening proceeding since there is neither a creditors' assembly nor committee present at this stage which could represent the interests of the creditors. Back To Text

[68] See supra section I(B)(2)(b)(2). Back To Text

[69] See InsO § 159; Detlev Beckmann, RWS Forum 14, 94 (1999). For a different opinion see Heinz Vallender, Masseverwertung schon im Eroeffnungsverfahren? [Exploitation of Property of the Estate in the Opening Proceeding?] RWS−Forum 14, at 71−72, 76−77, 91−92, 96 (arguing that preliminary trustee has no right to liquidate assets). Back To Text

[70] See Michael Jaffe and Joos Hellert, Keine Haftung des vorlaeufigen Insolvenzverwalters bei Anordnung eines allgemeinen Zustimmungsvorbehalts [No Liability of The Temporary Insolvency Trustee in Case of an Order Requiring That Transfers of Property of the Debtor Shall Need the Consent of the Temporary Trustee], ZIP, 1204, 1206 (1999). See, e.g., Regional Court (Landgericht, (LG)) (hereinafter Regional Court) Dortmund, Rpfleger 1983, 450; Federal Court of Justice (Bundesgerichtshof, (BGH)) (hereinafter Federal Court of Justice), NJW 1959, 1085; BGHZ 36, 18; BGHZ 110, 253, ZIP 1990, 805, BGHZ 36, 18. Back To Text

[71] See Federal Court of Justice, BGHZ 104, 151,155; Ulrich Pohlmann, Befugnisse und Funktionen des vorläufigen Insolvenzverwalters (Authorities and Functions of a Preliminary Trustee), Rn. 405−06 (1998); Vallender, supra note 68, at 71, 76, 84. Back To Text

[72] But see Volker Kammel, Ausgewaehlte Probleme des Unternehmenskaufs aus der Insolvenz [Problems of Business Purchases in Insolvencies] NZI, 102, 103f. (2000); Federal Court of Justice, BGHZ 104, 141, 156. Back To Text

[73] Marotzke, supra note 5, Rn. 47 Back To Text

[74] Id. Rn. 48. Back To Text

[75] Id. Rn. 47; Federal Court of Justice, BGHZ 104, 151, 156 Back To Text

[76] See Marotzke, supra note 5, Rn. 49 Back To Text

[77] See Hans−Peter Kirchhof, Heidelberger Kommentar zur Insolvenzordnung, HK−InsO [Heidelberger Commentary on the Insolvency Act], § 22, Rn. 12 (1999); Ulrich Schmerbach, Frankfurter Kommentar zur Insolvenzordnung, FK−InsO [Frankfurter Commentary on the Insolvency Act], § 22 Rn. 25, 27 (1999). Back To Text

[78] See Marotzke, supra note 5, Rn. 52. Back To Text

[79] See Vallender, supra note 68 at 71, 83, 92, 96; see also Christoph G. Paulus, Germany: Lessons to Learn from the Implementation of a New Insolvency Code, 17 Conn. J. Int'l L. 89, 92 (2001) (emphasizing strengthening of creditors' autonomy under new Code). Back To Text

[80] See InsO § 28 (1999) (stating "[i]n the order opening the insolvency proceedings the creditors shall be required to file their claims in compliance with section 174 [of the InsO] with the insolvency trustee within a definite period of time. Such period shall be fixed to extend not less than two weeks and not more than three months"); see also Kamlah, supra note 54, at 426 (recognizing creditors are required to make claims). Back To Text

[81] See InsO § 76(2) (providing "[a] decision of the creditors' assembly shall be valid if the sum of the claims held by backing creditors exceeds one half of the sum of claims held by creditors with voting rights."); see also Christoph G. Paulus, The New German Insolvency Code, 33 Tex. Int'l L.J. 141, 151 (1998) (outlining requirements for creditors' acceptance of plan). Back To Text

[82] According to subsection 2 of section 67 InsO, such a creditors' committee shall represent the creditors with a right to separate satisfaction, the creditors of the insolvency proceeding holding the maximum claims and the small sum creditors. The committee shall include a representative of the debtor's employees if the latter are involved as creditors of the insolvency proceeding holding considerable claims. Back To Text

[83] See First Report of the Commission for Insolvency Law, RWS−Verlag, 106 (1985); Hans Haarmeyer, Wolfgang Wutzke & Karsten Foerster, Handbuch zur Insolvenzordnung [Insolvency Act Manual], Ch. 4 Rn.24, 312 (1997); Bruno M. Kuebler & Hanns Pruetting, Kommentar zur InsO [Insolvency Act Commentary], § 67 Rn.11 (1999); Wilhelm Uhlenbruck, Zwei Modellverfahren im Ablauf mit Erläuterungen [Two Model Proceedings with Comments] 206 Rn. 79 (1997); see also Kirchhof, supra note 76, § 22, Rn.7, 11, 30. Back To Text

[84] See Marotzke, supra note 5, Rn. 61. Back To Text

[85] Section 21(1) InsO is comparable to section 105 of the Code, giving the court the power to issue any order, process, or judgement that is necessary to carry out the provisions of the Code. See generally InsO § 21(1) (1999); 11 U.S.C. § 105 (1994). See Patrick Ziechmann & Arthur D. Little, Business Bankruptcy in Germany, 16 Am. Bankr. Inst. J. 10, 23 (1997) (discussing measures that must be taken to protect debtor's assets). Back To Text

[86] According to sections 97 and 22(3) InsO, the debtor must grant the inspection of his books and business documents, and he must disclose any necessary information. See Paulus, supra note 78, at 148 (discussing information that must pass from debtor to creditors). Back To Text

[87] Pohlmann, supra note 70, Rn. 311. Back To Text

[88] See id. Rn. 306−07; Vallender, supra note 68, at 84, 96. Back To Text

[89] See Marotzke, supra note 5, Rn. 77. Back To Text

[90] See id., Rn. 92. See generally Matthew Bender & Co., Inc., Business Transactions in Germany § 17.07 (2001), available at 2−17 BTGERM § 17.07 (explaining purpose of creditor's committee is supervision and support of insolvency administrator). Back To Text

[91] See Vallender, supra note 68, at 71, 83, 92, 96 (stating consequence resulting is that sale of business is generally prohibited). Back To Text

[92] See Gerhard Pape, Zu den Schwierigkeiten des Sequesters ohne Verwaltungsmacht [The Difficulties of the Sequester without the Power to Manage the Estate), ZIP, 89, 92 (1994); Wolfgang Lohkemper, Keine Haftung des Erwerbers beim Betriebsuebergang [No Liability of the Purchaser of the Business], ZIP, 1251, 1252 (1999); Schmerbach, supra note 76, § 22 Rn.25, 27; Pohlmann, supra note 70, Rn. 280, 308, 407, 425, 605, 619. Back To Text

[93] Report of the Legal Committee on Insolvency Proceedings, BT−Drs.12/7302, 151−52; see also Manfred Balz, Market Conformity of Insolvency Proceedings: Policy Issues of the German Insolvency Law, 23 Brook. J. Int'l L. 167, 171 (1997) (indicating other objectives of new German insolvency law, such as to establish a new system providing market conformity in insolvency proceedings, to maximize value of the debtor's assets, and to have insolvency law not supercede market processes, but rather stimulate efficient market exchange processes). Back To Text

[94] See Marotzke, supra note 5, Rn. 88; Ziechmann, supra note 84, at 24 (explaining report meeting occurs after adjudication order which officially opens insolvency case). Back To Text

[95] See Marotzke, supra note 68, Rn. 89, 90. Back To Text

[96] See id.Rn.94. Back To Text

[97] See Pohlmann, supra note 70, Rn. 423 (describing stricter view); see also Ziechmann supra note 84, at 8 (explaining how trustee in report meeting states whether debtor's business can be maintained as one unit, split up, sold or liquidated). Back To Text

[98] See Marotzke, supra note 5, Rn. 96. Back To Text

[99] See Kuebler/Pruetting, supra note 82, § 58 Rn.10. Back To Text

[100] See Marotzke, supra note 5, Rn. 96. Back To Text

[101] See Kamlah, supra note 54, at 432−33 (stating "debtor−in−possession must obtain supervisor's consent to incur liabilities outside the ordinary course of business. Further, the debtor−in−possession must obtain the consent of the creditors' committee with respect to any act which would have a material impact on the proceeding, if the creditors so require at the meeting of creditors."); see also Marotzke, supra note 5, Rn.114. Back To Text

[102] See id., supra note 5, Rn. 256 (stating opportunity of lucrative offer to purchase property of debtor is considered property of estate) Back To Text

[103] See Higher Regional Court (Oberlandesgericht (OLG) (hereinafter Higher Regional Court) Duesseldorf, ZIP, 345 (1992); Pohlmann, supra note 70, Rn. 421; Vallender, supra note 68, at 71, 74, 81. Back To Text

[104] See Marotzke, supra note 5, Rn.117; see also Kamlah, supra note 54 at 433 (indicating insolvency practitioners have expressed disdain of supervisor type concept). Back To Text

[105] Additionally, according to section 158(2) InsO, before the creditors' committee makes its decision or, if such committee has not been appointed, before closing down the business, the trustee must inform the debtor thereof. At request of the debtor and after a hearing the court shall refuse a close−down of the business if the close down can be suspended until the report meeting without considerably reducing the assets of the debtor. See Paulus, supra note 80, at 148 (providing "[P]ursuant to section 160 InsO, the sale of an enterprise needs the consent of the creditor's committee (or if there is no committee, the creditors' assembly)."). Back To Text

[106] See Wolfgang Lüke, RWS−Forum 9, Haftung des Insolvenzverwalters in der Unternehmensfortfuehrung [Liability of the Trustee during the Continuation of the Business], 67, 76, 89; see also Kamlah, supra note 54, at 426 (indicating filing of petition does not guarantee debtor protection from creditors, but once case is filed court may issue any interim order it deems necessary in order to preserve estate). Back To Text

[107] See Marotzke, supra note 5, Rn. 122, 151. Back To Text

[108] See Uhlenbruck, supra note 82, Rn. 278. Back To Text

[109] Wilhelm Uhlenbruck, RWS Forum 14, Insolvenzrecht [Insolvency Law], 97−98 (1998/99). Back To Text

[110] Section 138(2) InsO contains a list of persons with a close relationship to the debtor if the debtor is a corporation. The concept is similar to the concept of an "insider" under the Code. See 11 U.S.C. § 101(31) (1994) (defining insider); Christoph G. Paulus, The New German Insolvency Code, 33 Tex. Int'l L.J. 141, 149 (1998) (indicating "consent of the assembly is always needed if the sale would affect persons with specific interests, for example, close relatives or creditors with a right to separate satisfaction."). Back To Text

[111] See, e.g., In re Stroud Ford, Inc., 163 B.R. 730, 733 (Bankr. N.D. Pa. 1993) (denying sale due to collusion of purchaser with higher bidders by buying out their objection and thus preventing estate from receiving adequate compensation); In re Plabell Rubber Products, Inc., 149 B.R. 475, 479−480 (Bankr. N.D. Ohio 1992) (denying trustee authority to sell business to company owned by debtor's employees through employee stock option plan (ESOP), because of unfair advantage and questionable role of debtor's vice president); In re Industrial Valley Refrigeration and Air Conditioning Supplies, Inc., 77 B.R. 15, 22−23 (Bankr. E.D. Pa. 1987) (finding lack of good faith due to unfair subsidies to debtor's insiders); In re Crutcher Res. Corp., 72 B.R. 628, 632 (Bankr. N.D. Tex. 1987) (refusing to allow sale where parent and lenders attempted to rush sale to avoid examination of subsidiaries). Back To Text

[112] See InsO § 75(1) No.3 (1999):

At least five creditors with a right to separate satisfaction or non−lower−ranking creditors of the insolvency proceedings whose rights to separate satisfaction and claims together are assessed by the insolvency court to represent one fifth of the sum resulting from the value of all rights to separate satisfaction and of the claims of all non−lower−ranking creditors of the insolvency proceedings.

Id. See Matthew Bender & Co., Inc, Collier International Business Insolvency Guide § 23.04[10][a] (2001), available at 2−23 INTBIG ¶ 23.04 (noting when ordering commencement of insolvency proceedings, examination hearing may coincide with information hearing, but with all other creditors' assemblies, courts must convene all other creditor's assemblies within two weeks after trustee, creditors' committee, or certain percentage of general unsecured creditors, or creditors with right to separate satisfaction, request that it do so); see also Matthew Bender & Company, Inc.,

Business Transactions in Germany § 17.07 [3][a] (2001), available at 2−17 BTGERM § 17.07 (describing creditors meetings and requirements of InsO section 75). Back To Text

[113] See InsO § 163 (1999) (allowing courts to require sale be approved by creditor's assembly if proven that sale to another party would be more beneficial); Matthew Bender & Company, Inc., Business Transactions in Germany § 17.16 (2001), available at 2−17 BTGERM § 17.16 (noting requesting party shall be entitled to reimbursement of costs incurred for such requests by assets involved in insolvency proceedings as soon as court issues its order). Back To Text

[114] See, e.g., In re Weatherly Frozen Food Group, Inc., 149 B.R. 480, 483 (Bankr. N.D. Ohio 1992) (noting sales under 11 U.S.C. § 363(b) may be authorized when dictated by sound business purpose); Titusville Country Club v. Pennbank (In re Titusville Country Club), 128 B.R. 396, 399 (Bankr. W.D. Pa. 1991) (describing following test for "sound business purpose:" 1) sound business reason, 2) accurate and reasonable notice, 3) adequate price, and 4) good faith); In re Oneida Lake Dev., Inc., 114 B.R. 352, 357 (N.D.N.Y. 1990) (stating for court to approve sale, proposed price must be best price obtainable, and court must find special circumstances justifying sale if secured creditor objects and sale price does not cover outstanding liens); Circus Time, Inc. v. Oxford Bank & Trust (In re Circus Time, Inc.), 5 B.R. 1, 2−3 (Bankr. Me. 1979) (allowing sale where immediate sale was urgent and prospective purchaser's offer was best offer obtainable). Back To Text

[115] See Paul Heinrich Neuhaus, Grundbegriffe des Internationalen Privatrechts [Basic Principles of Private International Law], 126 (1976) (noting under German law, cross−border insolvency law is part of private international law and autonomous body of the national law) Gerhard Kegel, Internationales Privatrecht [Private International Law], 187 (1985); see also Carl Felsenfeld, A Comment About a Separate Bankruptcy System, 64 Fordham L. Rev. 2521, 2523 (1996) (stating although bankruptcy law is federal, bankruptcy judges derive their power from Article I as opposed to Article III, and therefore bankruptcy courts are separate court system); cf. 11 U.S.C. § 304 (1994) (allowing foreign debtors to protect themselves from local creditors by filing petitions to have their U.S. assets administered by federal bankrutcy courts). Back To Text

[116] See Ian F. Fletcher, Cross Border Insolvency: National and Comparative Studies 1 (1992) (stating uniform rules dealing with cross−border insolvencies based on comity and equality of creditors have long been demanded by commentators); Elizabeth Warren & Jay L. Westbrook, The Law of Debtors and Creditors 873, 997 (1996) (finding long tradition in civil law nations of dealing with recognition of foreign insolvency proceedings in "all−or−nothing" manner); Bruce Leonard, The International Law Year in Review, ABI Journal Vol. XX No.10, at 34 (Oct. 2001) (stating Mexico, South Africa and Japan have enacted UNCITRAL Model Law, while U.K. has passed legislation contemplating it's adoption, and U.S. has included substance of UNCITRAL Model Law in it's proposed amendments to Bankruptcy Code); Kurt H. Nadelmann, Compositions, Reorganizations and Arrangements in the Conflicts of Laws, 61 Harv. L. Rev. 804 (1948) (examining problems and benefits of recognizing binding effects of foreign insolvency compositions); Richard Lee Wynne, The UNCITRAL Model Rule on Cross−Border Insolvency, 22 Los Angeles Lawyer, 24, 24 (1999) (opining U.S. will adopt UNCITRAL model law); see also Manfred Balz, The European Union Convention on Insolvency Proceedings, 70 Am. Bankr. L.J. 485, 494−97 (1996) (noting European Union states held Convention in attempt to form unified law on insolvency proceedings); Leonard, supra at 36 (describing how European Union Convention was frustrated when U.K. refused to sign on account of other E.U. countries banning British beef due to mad cow disease, but noting Convention has been converted into regulation, scheduled to come into effect on May 31, 2002, which shall, under European Law, be effective in all member states without the necessity of each country's signature). See generally Kurt H. Nadelmann, Solomons v. Ross and International Bankruptcy Law, 9 MOD. L. Rev. 154 (1946) (describing effects of 18th Century English case on cross border insolvencies in 20th Century); 1933 Nordic Convention on Bankruptcy for Denmark, Finland, Iceland, Norway and Sweden, 155 L.N.T.S. 115, art. 1 (1933) (providing example of early attempt to form uniform rules on cross−border−insolvency). Back To Text

[117] Under the territorial approach a foreign insolvency proceeding has only effects in the jurisdiction where proceedings have been opened. A foreign trustee has no standing and authority abroad. The local court of each country where the debtor has property grabs the assets and distributes them to those creditors who participate in the local proceeding, who naturally tend to be primarily local creditors (the "grab" rule). Only if there is a surplus of assets after

the local creditors have been satisfied is there any turnover to the bankruptcy estate where the proceeding had been opened. See Warren, supra note 115, at 874; see also Claudia Tobler, Note, Managing Failure in the New Global Economy: The U.N.C.I.T.R.A.L. Model Law on Cross−border Insolvency, 22 B.C. Int'l & Comp. L. Rev. 383, 395−99 (1999) (noting countries with territoriality approaches do not recognize foreign insolvency proceedings as legitimate, or recognize them only in limited respects). Back To Text

[118] Federal Court of Justice, NJW, 774 (1990); BGH NJW, 152 (1962); Hahn, Die gesammelten Materialien zu den Reichsgesetzen (Collected Materials of the Reichsgesetze) IV (1898); Josef Kohler, Lehrbuch des Konkursrechts [Textbook on Insolvency Law] 623 (1891). Back To Text

[119] Under the universality approach all countries defer to and cooperate with a single home country court (the country of the main proceeding). Every country recognizes the effects of the foreign insolvency proceeding and all assets of the debtor become property of the estate where the main proceeding is pending. The universality approach does not, however, apply with regard to countries that adhere to the territorial principle. Some countries, such as France, Belgium, and Luxembourg mitigate the universality principle by a requirement of reciprocity or, more liberally, by a requirement of comity. See Hans Arnold, Internationales Insolvenzrecht [International Insolvency Law] in Gottwald, Insolvenzrechtshandbuch [Insolvency Law Manual], § 122 No. 61 (1990); Balz, supra note 3, at 488. Other countries like the United States with its cases ancillary to foreign proceedings, or Switzerland with its parallel bankruptcies have taken an intermediate position between the principles of universality and territoriality. They provide for domestic bankruptcies once a foreign bankruptcy case has been opened in order to protect certain local interests while at the same time taking account of and accommodating some legitimate interests of the foreign bankruptcy forum. See Swiss Law on Private International Law, arts. 166−175, SR 291, AS 988, 1776; see also Hans Hanisch, Einheit oder Pluralität oder ein kombiniertes Modell beim grenzüberschreitenden Insolvenzverfahren? [Unity or Plurality or a Combined Model for Cross−Border Insolvency Proceedings?]. Back To Text

[120] The Federal Court of Justice, July 11th 1985, IX ZR 178/84, BGHZ 95, 256. See Eltje Aderhold, Auslandskonkurs im Inland [Foreign Insolvencies in the Home Country] (1992); Alex Flessner, Entwicklungen im internationalen Konkursrecht, besonders im Verhaeltnis Deutschland – Frankreich [Developments in International Bankruptcy Law, in particular between Germany and France], ZIP (1989), 749; Hans Hanisch, Cross−Border Insolvency: National and Comparative Studies, 104 (1992); Hans Hanisch, Die Wende im deutschen internationalen Insolvenzrecht, [The Change in German International Insolvency Law], ZIP, 1233−1243 (1985); Dieter Leipold, Et al., Auslaendischer Konkurs und inlaendischer Zivilprozess – Harmonie oder Dissonanz in der Rechtsprechung des BGH [Foreign Bankruptcy and Domestic Civil Law Suits – Harmony or Dissonance of the BGH] (1990); Alexander Lüderitz, Anmerkungen zum internationalen Konkursrecht [Notes on International Bankruptcy Law], JZ, 91 (1986), Das neue Gesicht des deutschen internationalen Konkursrechts aus auslaendischer Sicht [The New Face of the German International Insolvency Law From a Foreign Prospective], in FS Merz, 93 (1992); Cornelia Summ, Anerkennung ausländischer Konkurse in der Bundesrepublik [Recognition of Foreign Insolvencies in the Federation Republik of Germany] (1992); Alexander Trunk, Auslandskonkurs und inlaendischer Zivilprozess [Foreign Bankruptcy and Domestic Civil Proceeding], ZIP, 279 (1989). Back To Text

[121] BT−Drucks. 12/2443, 68 (1992). Back To Text

[122] The implementation of the universality principle in Article 102 EGInsO was an answer to the increasing number of transnational insolvency cases and one objective of the new insolvency law. See Manfred Balz & Hans−Georg Landfermann, Die neuen Insolvenzgesetze [The New Insolvency Law] XLVII (1995); Klaus Wimmer, Die UNCITRAL−Modellbestimmungen über grenzüberschreitende Insolvenzen [The UNCITRAL Model Law concerning Cross−Border Insolvencies], ZIP, 2224 (1997). Article 102 of the EGInsO does not, however, apply with regard to the member states of the European Union that will be governed by the Regulation of the European Union on Cross−Border Insolvencies once the Regulation becomes effective in May 31, 2002. The regulation applies to debtors who have its center of main interest in a member state of the European Union. To establish jurisdiction under the regulation it is not enough that the debtor has an establishment or place of business within a member state. Back To Text

[123] The German government intended to put a clause in the InsO stating that the provisions of the European Union Insolvency Convention shall also apply with regard to non−member states. See BT−Drucks. 12/7303, 117; see also Klaus Wimmer, Vorschläge und Gutachten zur Umsetzung des EU−Übereinkommens, [Proposals and Advisory Opinion for the Conversion of the EU−Convention] ZIP, 2224 (1997). The reason why the European Union Insolvency Convention (or now the Regulation) is to be applied exclusively among the member states of the European Union is that the Convention is based on the existing high standard of due process and justice in the member states. With regard to non−member states it has to be decided on a case−by−case basis whether the foreign law adheres to the basic principles and rights granted under the jurisdictions of the member states. The Convention was, however, often utilized for the interpretation of Article 102 EGInsO. Federal Court of Justice, NJW 657 (1997), ZIP 150 (1997) (interpreting avoidance law provision of Article 102 (2) EGInsO by looking at European Convention). Back To Text

[124] The provision was heavily criticized by German scholars and it was in particular argued that the wording could not be more imprecise. See Dieter Leipold, Miniatur oder Bagatelle: das internationale Insolvenzrecht im deutschen Reformvorhaben [The International Insolvency Law in the German Reform Proposal], FS Wolfram Henckel 533, 535 (1995); Hanns Prütting, Aktuelle Entwicklungen des Internationalen Insolvenzrechts [Current Developments of International Insolvency Law], ZIP, 1277, 1279 (1996). Back To Text

[125] The term "insolvency proceeding" equals the bankruptcy "case" under the Code. An insolvency proceeding is defined as every judicially or administratively supervised proceeding which serves the purpose of collective satisfaction of a debtor's creditors by liquidation of the debtor's assets and by distribution of the proceeds or by reaching an arrangement in an insolvency plan. See Federal Court of Justice, BGHZ 134, 89; see also Stefan Reinhart, Zur Anerkennung auslaendischer Insolvenzverfahren [Recognition of Foreign Insolvency Proceedings], ZIP, 1736 (1997). Back To Text

[126] Federal Court of Justice, BGHZ 95, 256, 261, 273. Back To Text

[127] See infra sections II(M−N). Back To Text

[128] See infra section II(F). Back To Text

[129] Neither the Federal Court of Justice nor Article 102 EGInsO provide for a particular procedure for the recognition of a foreign insolvency proceeding by a German court. Should a German court become involved in any kind of legal action which concerns a foreign bankruptcy proceeding it is generally acknowledged that the German judge has to examine prior to his decision whether the foreign proceeding is to be recognized in Germany and how this effects his decision. See Kirchhof, supra note 76, art. 102, Rn. 5. For example, if a creditor requests 100% payment of his claim before a German court the judge has to examine whether to recognize the U.S. reorganization plan. If the judge recognizes the plan the creditor will only be entitled to the amount of the claim awarded to him under the U.S. reorganization plan. Back To Text

[130] See id. art. 102, Rn. 6; Uwe Gottwald, Grundfragen der Anerkennung und Vollstreckung auslaendischer Entscheidungen in Zivilsachen [Basic Problems of Recognition and Enforcement of Foreign Judgments in Civil Proceedings], ZIP, 272 (1990); see also Federal Court of Justice, BGHZ 95, 270. Back To Text

[131] According to section 17 (1) of the Code of Civil Procedure (Zivilprozessordnung, (ZPO)) (hereinafter "ZPO") the usual venue of a corporation is the place of its administrative headquarters. Back To Text

[132] If several courts have jurisdiction, the court first requested to open the insolvency proceeding shall exclude any other jurisdiction. See InsO § 3 (2) (1999). Back To Text

[133] See 28 U.S.C. § 1408 (1994) (stating location of principal assets in United States is sufficient to establish District Court jurisdiction); see also ICMR, Inc. v. Tri−City Foods, Inc., 100 B.R. 51, 54 (Bankr. Kan. 1989) (holding Iowa should be venue when majority of principal assets were located in Iowa); In re Kona Joint Venture I, Ltd., 62 B.R. 169, 171 (Bankr. Haw. 1986) (concluding Hawaii was proper venue because it was debtor's principal place of business and where principal assets were located). Back To Text

[134] See supra section II(N) (discussing possibility of filing parallel proceeding in Germany). See also InsO § 3 (1999) (listing basis for commencing proceedings and excluding existence of property). Back To Text

[135] Habscheid, supra note 3, at 323. Back To Text

[136] See id.; see also 11 U.S.C. § 109 (1994) (establishing who is proper debtor); Kurt Hans Nadelmann, The Bankruptcy Reform Act and Conflict of Laws: Trial−And−Error, 29 Harv. Int'l L.J. 27, 33 (1988) (criticizing Code section 109(a) as imperialistic and arguing against the possibility of the commencement of a bankruptcy case based on the mere existence of assets in the jurisdiction). Back To Text

[137] The same principle is embodied in Article 6 of the Introductory Act to the German Civil Code (Einfuehrungsgesetz zum BGB, EGBGB) (hereinafter EGBGB). Back To Text

[138] Federal Supreme Court, BGHZ 90, 256, 269−70. Back To Text

[139] Id. at 50, 370, 375. Back To Text

[140] Id. at 48, 55, 327,331, 357,359. Back To Text

[141] Id. at 50, 370, 375. Back To Text

[142] Id. at 134, 91f; Kirchhof, supra note 76, art. 102, Rn. 8. Back To Text

[143] For the old view see Higher Regional Court Hamburg, IPRax 170 (1992) (recognition if chapter 11 case denied). See also Eric Jayme in FS−Riesenfeld, Sanierung von Grossunternehmen und internationales Konkursrecht [Reorganization of Major Corporations and International Insolvency Law], 117, 127. Back To Text

[144] See Stefan Reinhart, Sanierungsverfahren im internationalen Insolvenzrecht [Reorganizations in International Insolvency Law], 164−65, 175−76; see also Matthew Bender & Company, Inc., Business Transactions in Germany § 17.03 (2001), available at 2−17 BTGERM § 17.03 (stating recognition of foreign proceedings in Germany has to meet standards of German ordre public according to Article 6 EGBGB and section 328 (1) No. 4 ZPO). Back To Text

[145] BT−Drucks.12/2443, 241; Habscheid, supra note 3, at 315 Back To Text

[146] Kirchhof, supra note 76, art. 102, Rn. 7. Back To Text

[147] Id. art. 102, Rn. 12; see Matthew Bender & Co., Inc, Collier International Business Insolvency Guide § 23.03[1] (2001), available at 2−23 INTBIG ¶ 23.04 (stating exclusive jurisdiction rests with district court). Back To Text

[148] See supra section I (B)(2)(a). Back To Text

[149] See id. Back To Text

[150] See Federal Court of Justice, BGHZ 134, 92. This follows already from the wording of Article 102 EGInsO: "A foreign proceeding is recognized unless…".; See Klaus Wimmer, Frankfurter Kommentar zur Insolvenzordnung [Frankfurter Commentary on the Insolvency Act], art. 102, Rn. 275. Back To Text

[151] See id. Art. 102, Rn. 275 (1999). Back To Text

[152] Dieter Blumenwitz, Staudinger Kommentar zum Buergerlichen Gesetzbuch [Staudinger Commentary on the Civil Code], Art. 6 EGBGB, Rn. 101. Back To Text

[153] The foreign trustee may prove his appointment by presenting a certified copy of the appointing decision or by any other certificate of the appointing jurisdiction. See Christoph G. Paulus, The New German Insolvency Code, 33 Tex.

Int'l L.J. 141, 154 (1998) (stating avoiding powers of foreign trustee are not always exclusively dependent on foreign insolvency law (lex fori concursus)). Back To Text

[154] See Federal Court of Justice, BGHZ 95, 260−61; BGHZ 125, 200; see also Balz, supra note 3, at 516 (noting German courts research foreign law on their own or request amicus curiae briefs from experts, in particular with regard to powers of DIP or trustee under laws of foreign state). Back To Text

[155] See Wimmer, supra note 149, Art. 102, Rn. 304; see also European Convention On Insolvency Proceedings, 35 I.L.M. 1223, Nov. 23, 1995 (Identical provisions in art. 14 II c of Treaty). Back To Text

[156] Wimmer, supra note 149, Rn. 136. Back To Text

[157] Id., art. 102, Rn. 304; see also 11 U.S.C. § 1107 (1994) (providing rights, powers, and duties of debtor in possession). But see Zeichmann, supra note 84, at 7 (noting, in Germany, "only in unique circumstances will it be possible for the debtor to continue to administer its assets (like the DIP in U.S. Law) under the supervision of a 'creditor's trustee'"). Back To Text

[158] See supra section III (E). Back To Text

[159] See supra section III (2)(N); see also Manfred Balz, Bankruptcy in the Global Village: Market Conformity of Insolvency Proceedings: Policy Issues of the German Insolvency Law, 23 Brook. J. Int'l L. 167, 175 (noting German law, despite automatic stay, affords protection to secured creditors through regular payments of agreed interest on their secured claims). Back To Text

[160] See ZZP, 525 (1995) (providing explanatory memorandum to section 384 of German Insolvency Law Commission 1992). Back To Text

[161] See Wimmer, supra note 149, art. 102, Rn. 285 (noting all constitutional rights constitute fundamental principles of German law and must be taken into account by foreign proceeding). Back To Text

[162] See Federal Court of Justice, BGHZ 95, 259. Back To Text

[163] See supra section II (2)(a) (noting German law requires that formal decision of insolvency court is necessary to open insolvency proceeding); see also Ziechmann, supra note 84, at 6 (stating "[C]ourt will only open the insolvency proceeding if all legal requirements for [such a proceeding] are fulfilled and the remaining assets of the debtor will cover the costs and expenditures of the insolvency proceeding."). Back To Text

[164] See 11 U.S.C. 301 § (1994) (providing "[a] voluntary case under a chapter of this title is commenced by the filing…of a petition under such chapter by an entity that may be a debtor…[and] the commencement of a voluntary case…constitutes an order for relief under such chapter."); see also H.R. Rep. No. 95−595 to accompany H.R. Res. 8200, 95th Cong. (1st Sess. 1977), at 321 (noting term "adjudication" replaced by "order for relief" in keeping with Congress "power to permit voluntary bankruptcy without the necessity for adjudication"). In an involuntary case relief is not automatic. See 11 U.S.C. § 303 (stating "[i]f the petition is not timely controverted, the court shall order relief against the debtor. . .[o]therwise, after trail. . . if the debtor is generally not paying such debtors' debts as such debts become due unless such debts are the subject of a bona fide dispute; or [if] within 120 days before the date of filing of the petition, a custodian, other than a trustee, receiver, or agent appointed or authorized to take charge of less than substantially all of the property of the debtor for the purpose of enforcing a lien against such property, was appointed or took possession."). Back To Text

[165] See Wimmer, supra note 149, art. 102, Rn. 308. Back To Text

[166] According to section 9 InsO, publication shall be made in the gazette intended for official publications of the court and such publication may be restricted to excerpts. Documents to be published shall mention the debtor's particulars with special reference to his address and his branch of business. Such publication shall be deemed effected when two

additional days following the day of publication have expired.

The insolvency court may occasion additional and repeated publications. Publication shall suffice as evidence of service on all parties to the proceedings even if any provision additionally orders individual service. See InsO § 9 (1999). Back To Text

[167] Higher Regional Court Saarbrücken, ZIP, 1145 (1989). Back To Text

[168] See id. Back To Text

[169] See Habscheid, supra note 3, at 387. Back To Text

[170] See Storme & Casman, Towards Justice with a Human Face 29 (1978). Back To Text

[171] See Regional Court Muenchen, WM 222 (1987); Arnold, supra note 118, § 122 Rn. 128, § 123 Rn. 20; Hanisch, supra note 142, at 1223. This argument is also supported by article 14 of UNCITRAL. which requires that foreign creditors receive actual notice instead of publication unless the court finds another method that is appropriate. Back To Text

[172] See Habscheid, supra note 3, at 388−89. Back To Text

[173] See id. Back To Text

[174] See supra section II (D)(3)(b). Back To Text

[175] According to section 17(2) InsO, the debtor shall be deemed illiquid if he is unable to meet his mature obligations to pay. As a rule, illiquidity shall be presumed if the debtor has stopped payments. See InsO § 17(2) (1999). Back To Text

[176] According to section 18(2) InsO, the debtor shall be deemed with imminent illiquidity if he is likely to be unable to meet his existing obligations to pay on the date of their maturity. See id. § 18(2). Back To Text

[177] According to section 19(2) InsO, over−indebtedness shall exist if the assets owned by the debtor no longer cover his existing obligations to pay. See id. § 19(2) Back To Text

[178] See Bork, supra note 62, at 473; see also Lynn LoPucki, The debtor in full control – System failure under Chapter 11 of the Code?, 57 Am. Bank. L.J. 100, 114 (1983); Robert L. Ordin, The Good Faith Principle in the Bankruptcy Code: A Case Study, 38 Bus. Law. 1795, 1808–11 (1983) (discussing situations where debtor files bankruptcy to delay creditors' collection efforts). Back To Text

[179] See Bork, supra note 62, at 473. Back To Text

[180] See Ordin, supra note 177, at 1795 (stating cases dealing with issue of good faith are commonplace under Bankruptcy Code); Lawrence Ponoroff & F. Stephen Knippenberg, The Implied Good Faith Filing Requirement: Sentinel of an Evolving Bankruptcy Policy, 85 Nw. U. L. Rev. 919, 921–22 (1991) (discussing courts have responded to "creative" chapter 11 filings by recognizing implied requirement that petition be filed in good faith). Back To Text

[181] See 11 U.S.C. § 1112(b) (1999) (providing "the court may convert a case [under chapter 11 of the Bankruptcy Code] to a case under chapter 7 [of the Bankruptcy Code] or may dismiss a case [under chapter 11], whichever is in the best interest of creditors and the estate, for cause."). Section 1112(b) sets forth examples of "cause," such as continuing loss to or diminution of the estate and absence of a reasonable likelihood of rehabilitation, inability to effectuate a plan, and unreasonable delay by the debtor that is prejudicial to creditors. Id. § 1112(b); see, e.g., Cedar Shore Resort, Inc., v. Mueller (In re Cedar Shore Resort, Inc.) 235 F.3d 375, 379 (8th Cir. 2000) (stating section 1112(b) of Bankruptcy Code permits court to dismiss chapter 11 petition for cause, such as bad faith filing); AMC

Mortgage Co., Inc. v. Tenn. Dep't of Revenue (In re AMC Mortgage Co., Inc.) 213 F.3d 917, 920 (6th Cir. 2000) (stating bankruptcy court has broad discretion to dismiss chapter 11 case for cause under section 1112(b)); In re SGL Carbon Corp. 200 F.3d 154, 160 (3d Cir. 1999) (explaining ten examples of "cause" enumerated in section 1112(b) are not exhaustive, and court may consider whether other factors qualify as cause). Back To Text

[182] See 11 U.S.C. § 1112(b)(3) (stating court may convert case under chapter 11 to chapter 7 of Bankruptcy Code for unreasonable delay by debtor that is prejudicial to creditors); see also Habscheid, supra note 3, at 390. Back To Text

[183] See Bankruptcy Rule 1008 (2001) (requiring all petitions "shall be verified or shall contain an unsworn declaration" of truthfulness subject to penalty of perjury); see also Taylor v. Freeland & Kronz, 503 U.S. 638, 644 (1992) (noting "[d]ebtors and their attorneys face penalties under various provisions [of the Bankruptcy Code and Rules] for engaging in improper conduct in bankruptcy proceedings."); Bell v. Bell (In re Bell), 225 F.3d 203, 220–221 (2d. Cir. 2000) (citing Bankruptcy Rule 1008). Back To Text

[184] The explicit requirement that the debtor must file its petition in good faith was embodied in section 141 of the Act, but was not implemented in the Code. It is nonetheless within the inherent jurisdiction of the bankruptcy courts to dismiss a case if there is sufficient evidence that the debtor did not act in good faith. See In re Northwest Recreational Activities, Inc., 4 B.R. 36, 39 (Bankr. N.D. Ga. 1980) (stating good faith "is merged into the power of the court to protect its jurisdictional integrity from schemes of improper petitioners seeking to circumvent jurisdictional restrictions and from petitioners with demonstrable frivolous purposes absent any economic reality"); see also United Savings Ass'n of Texas v. Timbers of Inwood Forest Ass'n, Ltd. (In re Timbers of Inwood Forest Ass'n, Ltd.), 808 F.2d 363, 383 n.11 (5th Cir. 1987) (Jones, J. dissenting) (stating cases may be vulnerable to dismissal or lifting automatic stay on ground that bankruptcy was filed in bad faith); Duggan v. Highland−First Ave. Corp., 25 B.R. 955, 962 (Bankr. C.D. Cal. 1982) (vacating automatic stay based on debtor's bad faith in filing of chapter 11 petition). Back To Text

[185] See Habscheid, supra note 3, at 391. Back To Text

[186] See supra note 60 (explaining reasons for commencing insolvency proceedings in Germany). Back To Text

[187] In re Johns−Manville Corp., 36 B.R. 727 (Bankr. S.D.N.Y. 1984). Back To Text

[188] See id. at 730 (stating no requirement exists that debtor be insolvent to obtain chapter 11 debtor status); see also Official Commission of Unsecured Creditors v. Nucor Corp. (In re SGL Carbon Corp.), 200 F.3d 154, 164 (3d Cir. 1999) (discussing same requirement); In re Mount Carbon Metropolitan District, 242 B.R. 18, 33 (Bankr. D. Colo. 1999) (discussing same requirement). Back To Text

[189] See supra note 60 (section 18(2) of InsO has, however, so far been rarely utilized by debtors as a reason to open an insolvency proceeding); Habscheid, supra note 3, at 393. Back To Text

[190] See id., supra note 3, Rn. 404. Back To Text

[191] See e.g., Restatement (Third) of Foreign Relations Law of US § 483 (1986); F.A. Mann, Öffentlich−rechtliche Ansprüche im internationalen Rechtsverkehr [Governmental Claims in International Proceedings], 7 (1956); Richard E. Smith, The Nonrecognition of Foreign Tax Judgments: International Tax Evasion, 1981 U. Ill. L. Rev. 241, 241 (discussing fact that United States courts do not generally enforce foreign tax liabilities). Back To Text

[192] See UNCITRAL art. 13 (permitting foreign creditors right to proceeding in State where insolvency took place); Wimmer, supra note 142, Rn. 220, 222. Back To Text

[193] See 11 U.S.C. § 523(a)(1) (1994); InsO §§ 38−39 (1999). Under the InsO only administrative expense claims and secured claims get a preferential treatment. Section 39 which mentions lower ranking creditors does not contradict this concept. Claims of lower ranking creditors where under the old law not entiteled to participate in the insolvency proceeding at all. Under the InsO such claims shall only be filed if the insolvency court requests so (sections 174 (3),

177 (2) InsO), are not entitled to vote in the creditors' assembly (section 77 (1) InsO and usually shall not receive anything under an insolvency plan (sections 225 (1), 246 InsO). See Kirchhof, supra note 50, Rn.161. Back To Text

[194] EGInsO Art. 102 (1999). Back To Text

[195] Georg Kuhn & Wilhelm Uhlenbruck, Kommentar zur Insolvenzordnung [Insolvency Law Commentary], § 61 Rz. 48a, 51a. Back To Text

[196] See Federal Court of Justice, BGHZ 118, 312 (holding punitive damage judgments pursue purpose of deterrence and punishment that are inconsistent with concept of compensation under German Civil Code); see also Peter Hay, The Recognition and Enforcement of American Money Judgements in Germany — The 1992 Decision of the German Supreme Court, 40 Am. J. Comp. L. 729, 745−46 (1992) (discussing how enforcement of punitive damages would violate German public policy); Hartwig Bungert, Vollstreckbarkeit US−amerikansischer Schadensersatzurteile in exorbitanter Hoehe [Enforcement of U.S. Monetary Damage Judgements of Extreme Amounts], ZIP, 1707 (1992). Back To Text

[197] See Habscheid, supra note 3, at 320, 406. Back To Text

[198] See Balz, supra note 3, at 515 (noting "[a] foreign main liquidator may not exercise her powers in a way which would be contrary to the general law of the Member State where she wants to act."); European Union: Convention on Insolvency Proceedings 35 I.L.M. 1223, 1230 (1996) [hereinafter] European Union] (discussing powers of liquidator: "the liquidator shall comply with the law of the Contracting State within the territory of which he intends to take action"). Back To Text

[199] See Balz, supra note 3, at 515 (emphasizing importance of liquidator selling assets in accordance with local law procedures); European Union, supra note 187, at 1230 (referring specifically to realization of assets). Back To Text

[200] See 11 U.S.C. § 541(a) (1994) (providing "[t[he commencement of the case under sections 301, 302, or 303 of the Code creates an estate [which] is compromised of all of the following property, wherever located and by whomever held."). See generally In re Chappel, 189 B.R. 489, 493 (9th Cir. 1995) (espousing broad interpretation of property of estate). Back To Text

[201] See 11 U.S.C. §§ 541−60 (1994) (concerning creation of bankruptcy estate); See Wimmer, supra note 149, art. 102, Rn. 320. Back To Text

[202] See Wimmer, supra note 149, Art. 102, Rn. 320. Back To Text

[203] See Habscheid, supra note 3, at 331. Back To Text

[204] Federal Court of Justice, BGHZ 88, 147, 155 ; Regional Court Düsseldorf, IPRspr 1990 Nr.254 b; Underwood v. Hillard, 98 F.3d 956, 961 (7th Cir. 1996) (holding use of stay to enjoin activity by foriegn receiver was consistent with statutory purpose of using stay to prevent uncontrolled race for debtor's assets in variety of chaotic proceedings in numerous courts). Back To Text

[205] See § 27 BGB. See generally Mathias Reimann, Conflict of Laws, Comparative Law and Civil Law: Codifying Torts Conflicts: The 1999 German Legislation in Comparative Perspective 60 La. L. Rev. 1297, 1297−99 (2000) (discussing background and purposes of Civil Code). Back To Text

[206] See Patricia Nacimiento, Grenzüberschreitende Gerichtsstandsvereinbarungen (Vertragsrecht) [Determination of Court of Competent Jurisdiction in Cross−Border Cases (Contract Law)], Frankfurter Allgemeine Zeitung, March 6, 2001. Back To Text

[207] See Klaus−Peter Berger, Internationale Wirtschaftsschiedsgerichtsbarkeit [International Commercial Arbitration Law] § 6I (1993) (concerning clauses of arbitration); Deutsche Institution für Schiedsgerichtsbarkeit (DIS), Das neue

Deutsche Schiedsverfahrensrecht in der Praxis [The New German Arbitration−Law in Practice], DIS−Mat VII (2001). Back To Text

[208] The recognition of foreign judgments requires besides compliance with the ordre public (section 328 No.4 ZPO) also reciprocity (section 328 No.5 ZPO) and is thus stricter than the standard under article 102 EGInsO. See Geimer & Schütze, Internationale Urteilsanerkennung, [Recognition of Foreign Judgments] Bd. I, Hb 2, 1385 (discussing requirements for recognition of judgments of foreign courts); Rolf A. Schütze, Deutsch− amerikansiche Urteilsanerkennung [German−American Recognition of Judgements] (1992); see also the Haager Convention on the Recognition on the Enforcement of Foreign Judgments, Karsten Otte, Scheitert das Haager Abkommen [Does the Haager Convention fail ?], DAJV Newsletter, 43 (Feb. 2000); Jeffrey D. Kovar, A Letter to the Hague Conference on Private International Law, DAJV Newsletter, 44 (Feb. 2000). Back To Text

[209] See Bungert, supra note 195. Back To Text

[210] Federal Court of Justice, BGHZ VIII 32/20. Back To Text

[211] Id. Back To Text

[212] Id. Back To Text

[213] Even if the DIP is technically in most cases the same entity, it is a different legal entity. See generally Klaus Kamlah, The New German Insolvency Act: Insolvenzordnung, 70 Am. Bankr. L.J. 417, 433 (1996) (stating German insolvency experts do not like debtor−in−possession concept). Back To Text

[214] See InsO § 80 (1999); see also 11 U.S.C. § 323 (1994) (explaining role of trustee). See generally Ziechmann, supra note 84, at 10 (describing German bankruptcy procedure and explaining how trustee administered and disposed of assets for debtor and only in unique circumstances did debtor continues to administer estate as debtor−in−possession). Back To Text

[215] The lex rei sitae is a fully acknowledged principle of Private International Law. See Kegel, supra note 114, at 572; Federal Court of Justice, BGHZ 52, 239, NJW 59 (1995); Higher Regional Court Düsseldorf, NJW 529 (1981); Higher Regional Court München, NJW RR, 664 (1989). Back To Text

[216] See generally Ulrich Drobnig, Secured Credit in International Insolvency Proceedings, 33 Tex. Int'l L.J. 53, 63 (1998) (explaining lex rei sitae governs creation, rank, disposition, termination, and effects of proprietary rights); Higher Regional Court Koeln, RIW 969 (1994) (A choice of law is not permissible). Back To Text

[217] See German Civil Code (Buergerliches Gesetzbuch, BGB) (hereinafter "BGB")§ 433 (describing basic duties of seller and buyer); BGB § 313 (explaining form of contract for alienation of piece of land). Back To Text

[218] See BGB § 873 (describing acquisition by way of agreement and registration); BGB § 925 (describing conveyance of title). German law strictly distinguishes between the obligation under the sales contract and the conveyance of ownership. The closing of the sales contract has no effect on the ownership. It only creates a right of the purchaser to the conveyance of the ownership. The actual conveyance of the ownership requires a separate agreement. Back To Text

[219] See BGB § 873 (noting entry in land register constitutes passing of title and has thus more than mere declaratory and evidentiary function). Back To Text

[220] This right follows from the recognition of the effects of the creation of a single estate. See EGInsO Art. 102 (1999). Back To Text

[221] See BGB § 929. German property law contains the principle of publicity that requires that every transfer of property must be identifiable by a third party. In the case of real property the entry in the land book and in the case of

personal property the handing over assures the publicity of the change of ownership. Back To Text

[222] See Habscheid, supra note 3, at 334. Back To Text

[223] Section 81 InsO incorporates section 892 BGB providing for the possibility of a good faith aquisition of title to real property. A good faith acquisition of title to personal property is however not possible. Section 81 InsO does not incorporate section 932 BGB which provides for good faith acquisitions of personal property. Back To Text

[224] Contrary to the American Deed Registry, a bona fide purchaser may rely on the accuracy of the land book, not only with regard to the absence of entries, (e.g. unrecorded interests, or the commencement of an insolvency proceeding) but also on the correctness of an existing entry. Title insurance is therefore unnecessary and does not exist in Germany. See Karl−Erbo Graf Kageneck, Deutsch−amerikanisches Begriffslexikon Direktinvestitionen [U.S.−German Dictionary of Direct Investment], 64 (1998). Back To Text

[225] See InsO §§ 49, 50; U.C.C. art. 9 (2001). Rights in rem include liens (judicial, statutory, and contractual), mortgages, pledges, and security interests within the meaning of Article 9 of the Uniform Commercial Code. Back To Text

[226] The situs of movable or immovable tangible assets is the place where the property is physically situated. For intangible property which requires registration in a public register, such as a patent, the situs is the location of the public register. For receivables, the situs is the place where the account debtor has the center of its main interest. See Balz, supra note 3, Rn. 510. Back To Text

[227] See Kirchhof, supra note 74, Rn. 22. and RegE § 390. But see Wimmer, supra note 149, Rn. 327, 328, who wants to allow interference with secured creditors' rights under the law of the foreign proceeding provided that the law of the situs of the collateral also provides for at least similar limitations. Back To Text

[228] See Jen Hausmann, The Value of Public−Notice Filing under Uniform Commercial Code Article 9: A Comparison with the German Legal System of Securities in Personal Property, 25 Ga. J. Int'l & Comp. L. 427, 439 (1996) (noting reservation of title by seller merely creates security interest in goods); see also U.C.C. §§ 1−201(37), 2−401 (2001). Back To Text

[229] See Balz, supra note 3, at 508−09. Back To Text

[230] See Kirchhof, supra note 76, Art. 102 Rn. 22. Back To Text

[231] 11 U.S.C. § 363(f) (1994). The reason for this rule is that throughout the world and even within the European Union laws on the rights of secured creditors in insolvency proceedings vary significantly. The treatment ranges from substantially interfering and inflicting considerable losses on secured creditors for the benefit of the debtor and its rehabilitation like the French redressement judiciaire, whereas other insolvency laws, such as those in the United Kingdom, leave secured creditors largely unaffected. Back To Text

[232] Balz, supra note 3, at 509; Collier International Business Insolvency Guide § 23.02[3] (2001), available at 2−23 INTBIG ¶ 23.02 (stating creditor must apply for foreclosure sale or sequestration of the property to enforce mortgage); Collier International Business Insolvency Guide § 23.03[1] (2001), available at 2−23 INTBIG ¶ 23.03 (declaring creditor must gain possession of collateral before being able to sell collateral). Back To Text

[233] See supra section III(2)(E)(VI). See generally Collier International Business Insolvency Guide § 23.07[6] (2001), available at 2−23 INTBIG ¶ 23.07 (stating separate domestic proceedings are governed by German Insolvency Code). Back To Text

[234] An executory contract under both German and U.S. law is a contract under which the obligation of both the bankrupt and the other party to the contract is so far unperformed that the failure of either to complete performance would constitute a material breach excusing the performance of the other. See Vern Countryman, Executory Contracts

in Bankruptcy (Part I), 57 Minn. L. Rev. 439 (1973) (defining executory contracts and trustee's right to assume or reject a contract); see also Vern Countryman, Executory Contracts in Bankruptcy (Part II), 58 Minn. L. Rev. 479 (1974) (continuing discussion on executory contracts); Eberhard Schollmeyer, Gegenseitige Verträge im internationalen Insolvenzrecht [Executory Contracts in International Insolvency Law] (1996). Back To Text

[235] See InsO § 103(1) (1999); see also 11 U.S.C. § 365 (describing trustee's rights to assume or reject any executory contract or un−expired lease of debtor). Back To Text

[236] See InsO § 103(2). Back To Text

[237] See Wimmer, supra note 149, art. 102, Rn. 340. Back To Text

[238] See supra section II(M). Back To Text

[239] In the absence of a choice of law clause, leases of real property are governed by the law of the situs of the real property. See § 380 RegE; EGBGB § 28(1)(3); see also Kirchhof, supra note 76, Rn.17; Wimmer, supra note 149, Rn.340,. Back To Text

[240] See EGInsO art. 33 Nr.16. Back To Text

[241] Dieter Martiny, Münchner Kommentar zum Buergerlichen Gesetzbuch [Munich Commentary on the Civil Code] Art. 30 EGBGB, Rn. 50. Back To Text

[242] See Wimmer, supra note 149, Rn. 345. Back To Text

[243] See European Court of Justice (Europaeischer Gerichtshof) [hereinafter EuGH] EuGH AP Nr.14; EWG−Directive 77/187 (defining business as organized body of persons and objects for purpose of permanent commercial operation); see also Federal Labor Court of Germany (Bundesarbeitsgericht) [hereinafter BAG] BAG AP Nr.196, 197 [regarding section 613a BGB] (defining business as organized body of persons and objects for purpose of permanent commercial operation). Back To Text

[244] See BAG AP Nr.189 [regarding section 613a BGB, ZInsO 483 (1999)] (defining conveyance of business as continued or resumed (in case of a temporary closedown) operation of the business by purchaser). Back To Text

[245] See Georg Annuss, Der Betriebsuebergang in der Insolvenz [Transfer of a Business in an Insolvency Proceeding], ZinsO 49, 50 (2001). The limitation of liability for claims that became due prior to the commencement of the proceeding applies, however, only to such claims that could be filed by the employees in the insolvency proceeding. Claims for holiday entitlement, for instance, cannot be filed in the insolvency proceeding so that a potential purchaser would have to grant these holidays even if the entitlement was earned entirely prior to the commencement of the proceeding and the sale of the business. Back To Text

[246] See InsO § 3:

(1) local is responsible excluding the insolvency court, in whose district of the debtors has its general area of jurisdiction. If the center of independent gainful occupation of the debtor is because of another place, then is responsible excluding the insolvency court, in whose district this place lies. (2) if several courts are responsible, then the court, with which first the opening of the insolvency procedure was requested, excludes the remaining.

Id. Back To Text

[247] See Wimmer, supra note 149, Rn. 295. Back To Text

[248] See supra section II (D). Back To Text

[249] See Habscheid, supra note 3, at 465. Back To Text

[250] See Wimmer, supra note 149, Rn. 295. Back To Text

[251] The secondary proceeding therefore reflects the territorial principle. Back To Text

[252] See Kirchhof, supra note 76, Rn. 37; Kuhn/Uhlenbruck, supra note 185, §§ 237, 238, Rn. 105. The universal approach of article 102(1) EGInsO leads therefore to a single uniform insolvency proceeding whereas the territorial approach of Article 102(3) EGInsO leads to a plurality of insolvency proceedings. Back To Text

[253] Habscheid, supra note 3, at 459. Since all creditors are allowed to file their claims in a secondary proceeding, a surplus will be generated only very rarely. This may occur when creditors with considerable claims abstain (perhaps prompted by the trustee in the main proceeding) from lodging their claims in the secondary proceeding. Back To Text

[254] This practice is different than the European Union Regulation on Cross Border Insolvency Law. Under the Regulation, the debtor must have an establishment in the state where he intends to file a parallel proceeding. The mere existence of property is explicitly not sufficient. See Klaus Wimmer, Die Verordnung (EG) Nr.13461/2000 ueber Insolvenzverfahren [The Regulation No.13461/2000 on Insolvency Proceedings], ZinsO, 101 (2001) and for its predecessor, the European Union Convention, Manfred Balz, Das neue europaeische Insolvenzuebereinkommen [The New European Insolvency Conventiont], ZIP 948, 953 (1996). Back To Text

[255] See Habscheid, supra note 3, at 425. Back To Text

[256] See InsO § 3:

(1) local is responsible excluding the insolvency court, in whose district of the debtors has its general area of jurisdiction. If the center of independent gainful occupation of the debtor is because of another place, then is responsible excluding the insolvency court, in whose district this place lies. (2) if several courts are responsible, then the court, with which first the opening of the insolvency procedure was requested, excludes the remaining.

Id. Back To Text

[257] Since sections 13 and 14 InsO regulate the eligibility to file an insolvency proceeding generally, both sections also apply to secondary proceedings under article 102(3) EGInsO. See InsO §§ 13, 14; Habscheid, supra note 3, at 428. Back To Text

[258] See id., 429, 461. Back To Text

[259] See id., 461. Back To Text

[260] See Leipold, supra note 123, at 533, 541. Back To Text

[261] See Kirchhof, supra note 76, Rn. 34. Back To Text

[262] See Habscheid, supra note 3, at 430. Back To Text

[263] See id. at 462. Back To Text

[264] With regard to the European Convention see Balz, supra note 236, at 948, 953. Back To Text

[265] See Habscheid, supra note 3, at 426. Back To Text

[266] See Leipold, supra note 123, at 540. Back To Text

[267] So specifically, art.3 (4) of the European Union Regulation On Cross Border Insolvencies. However, with the limitation that the debtor must be unable to commence a proceeding in the state where he has its center of main interest. Alternatively, the petition must be filed by a local creditor. Back To Text

[268] See Kirchhof, supra note 76, art. 102, Rn. 32. Back To Text

[269] Kirchhof, supra note 76, art.102 Rn. 35; Habscheid, supra note 3, at 462. Back To Text

[270] See Balz, supra note 3, at 490. Back To Text

[271] Id. Back To Text

[272] Such as real estate law, the law of secured credit, tax law, and labor law, all of which are relevant to bankruptcy cases. Back To Text

[273] Balz, supra note 3, at 486. Back To Text

[274] Such as the French redressement judiciaire [the French Insolvency Law]. Back To Text

[275] See Balz, supra note 3, at 509 and n.23. e.g, the secured creditors' right to satisfy their claims entirely outside any collective insolvency proceeding by appointing a private receiver who liquidates the assets. Back To Text

[276] See Westbrook, supra note 3, at 468−69. Back To Text

[277] See In re The Application of the Liquidating Committee of Papeleras Reunidas, S.A., 92 B.R. 584, 590, 595 (Bankr. E.D.N.Y. 1988) (holding since deferring to Spanish law did not afford American creditor of Spanish company in liquidation in Spain similar and fair treatment as creditor would be entitled to in United States, section 304 proceeding should be dismissed); Westbrook, supra note 3, at 468−69. Back To Text

[278] See In re Koreag, Controle et Revision S.A., 130 B.R. 705, 712−713 (Bankr. S.D.N.Y. 1991) (stating better rule is foreign law should simply comport with American Bankruptcy Code's notion of fair and equal treatment of all creditor's), vacated by 961 F.2d 341 (2d. Cir. 1992; See Westbrook, supra note 3, at 470. Back To Text

[279] For instance, with the accession of the common law countries of the United Kingdom and the Republic of Ireland the differences of law within the European Community were deepened significantly in 1973. The complexity of different legal cultures was also reflected by Denmark and Finland, members of the Scandinavian type of legal system. The Scandinavian system is generally viewed as a separate and distinct legal system, different from both the common law and the civil law. See Konrad Zweigert & Hein Kotz, Einführung in die Rechtsvergleichung (Introduction to Comparative Law) (1996). See also Richard B. Cappalli, At the Point of Decision: The Common Law's Advantage over the Civil Law, 12 Temple Int'l. & Comp. L.J. 87, 87−88 (1998) (noting that the problem of understanding foreign legal systems results not only from cultural and educational differences, but also from a lack of explanations of each legal system's underpinnings). Back To Text

[280] See Westbrook, supra note 3, at 470. Back To Text

[281] In the absence of the application of statutory provisions cross−border cases are commonly resolved on a comity basis. See Cunard S.S. CO. v. Salen Reefer Serv. AB, 773 F.2d. 452, 454−55 (noting that when a debtor is involved in a foreign bankruptcy proceeding section 304 of the Code is not the exclusive remedy to stay or enjoin creditor actions in the U.S.) See also Leist v. Simplot, 638 F,2d, 283, 313 (2d Cir.1980), aff"d sub nom. Merrill Lynch, Pierce, Fenner & Smith v. Curran, 456 U.S. 353, 102 S.Ct. 1825, 72 L.Ed.2d 182 (1982) (noting that section 304 was not considered by Congress to be exclusive. "When… Congress adds a new remedy…, where other remedies had been clearly recognized, it would be expected to say so if it meant the new remedy to be exclusive."). Comity will be granted to a decision or judgment of a foreign court if it is shown that the foreign court is a court of competent jurisdiction, and that the laws and public policy of the forum state and the rights of its residents will not be violated. See Hilton v.

Guyot, 159 U.S. 113, 16 S.Ct.139, 40 L.Ed. 95 (1985) 159 U.S. at 202−03., 16 S.Ct. at 158−59; Clarkson Co. v. Shaheen, 544 F.2d.624, 629 (2d Cir. 1976); Kenner Prod. Co. v. Societe Fonciere et Financiere Agache−Willot, 532, F.Supp. 478, 479 (S.D.N.Y.1982). Comity should be withheld only when its acceptance would be contrary or prejudicial to the interest of the nation called upon to give it effect. See Somportex Ltd. V. Philadelphia Chewing Gum Corp., 453 F.2d 435, 440 (3d Cir. 1971), cert. denied, 405 U.S. 1017, 92 S.Ct. 1294, 31 L.Ed.2d 479 (1972) (citing L.Orfield § E. R, International Law 736−37 (1965)). Back To Text

[282] The same arguments apply to the possibility of secondary proceedings under The European Union Regulation and UNCITRAL Model Rules on Cross Border Insolvencies. Back To Text

[283] See supra section III (2)(F). Back To Text

[284] See Wimmer, supra note 149, Art. 102 Rn. 383; Balz, supra note 3 at 520 (noting secondary proceedings serve to "mitigate or modify the principle of universality and mutual recognition of main proceedings for the sake of individual or public local interests"). Back To Text

[285] See supra section I. Back To Text

[286] See supra section II(L). Back To Text

[287] See supra section II(N). Back To Text

[288] See Westbrook, supra note 3, at 465; see also Thomas H. Jackson & Robert E. Scott, On the Nature of Bankruptcy: An Essay on Bankruptcy Sharing and the Creditors' Bargain, 75 Va. L. Rev. 155, 156−57 (1989) (generally outlining pros and cons of coordination and cooperation in bankruptcy proceedings). Back To Text

[289] See Westbrook, supra note 3, at 465. Back To Text