



Fall 9-1-1979

The Commencement Of A Case Under The New Bankruptcy Code

Frank R. Kennedy

Follow this and additional works at: <https://scholarlycommons.law.wlu.edu/wlulr>

Recommended Citation

Frank R. Kennedy, *The Commencement Of A Case Under The New Bankruptcy Code*, 36 Wash. & Lee L. Rev. 977 (1979).

Available at: <https://scholarlycommons.law.wlu.edu/wlulr/vol36/iss4/2>

This Article is brought to you for free and open access by the Washington and Lee Law Review at Washington and Lee University School of Law Scholarly Commons. It has been accepted for inclusion in Washington and Lee Law Review by an authorized editor of Washington and Lee University School of Law Scholarly Commons. For more information, please contact christensena@wlu.edu.

Washington and Lee Law Review

Member of the National Conference of Law Reviews

Volume XXXVI

Fall 1979

Number 4

THE COMMENCEMENT OF A CASE UNDER THE NEW BANKRUPTCY CODE

FRANK R. KENNEDY*

I.	THE RECOMMENDATIONS OF THE COMMISSION ON THE BANKRUPTCY LAWS	977
II.	THE FOUR KINDS OF CASES UNDER THE BANKRUPTCY CODE	981
A.	<i>Voluntary Cases—Section 301</i>	982
1.	The Petition	982
2.	Eligible Debtors	986
3.	Filing Fees	993
B.	<i>Joint Cases—Section 302</i>	995
C.	<i>Involuntary Cases—Section 303</i>	998
1.	Amenable Debtors	998
2.	Qualifications of Petitioning Creditors	1004
3.	Partnership Cases	1006
4.	Cases Against Debtors in Foreign Proceedings	1006
5.	Grounds for Involuntary Relief	1008
6.	Procedure	1014
a.	Joinder of Petitioners	1014
b.	Contest of a Petition	1014
c.	Jury Trial	1015
7.	The Interim Between the Filing of an Involuntary Petition and Entry of an Order for Relief	1015
8.	Conversion of a Case Under One Chapter to a Case Under Another Chapter	1018
D.	<i>Cases Ancillary to Foreign Proceedings—Section 304</i>	1019
III.	ABSTENTION	1022
IV.	CONCLUSION	1024

I. THE RECOMMENDATIONS OF THE COMMISSION ON THE BANKRUPTCY LAWS

The dramatic increase of petitions filed under the Bankruptcy Act by consumer debtors between 1946 and 1967 was perhaps the most significant

* Thomas M. Cooley Professor of Law, University of Michigan

factor that led to the establishment of the Commission on Bankruptcy Laws of the United States in 1970.¹ The Commission was charged with the responsibility of studying, analyzing, evaluating, and recommending changes in the bankruptcy laws.² The Commission found no reason to believe from its study, however, that the number of bankruptcy petitions being filed was excessive or that there was need for legislation to restrict access to the bankruptcy court by debtors seeking relief.³ The general thrust of the Commission's recommendations was to facilitate the filing of petitions under the bankruptcy laws by removing certain obstacles to effective relief. For this very reason, however, the recommendations were criticized by spokesmen for the consumer credit industry.⁴

Despite the increase in bankruptcies, the Commission was concerned that many consumer debtors filed without adequate information or understanding as to the nature of the relief available under the bankruptcy laws.⁵ One result of the lack of information regarding the possibilities under the Bankruptcy Act was the sporadic use of Chapter XIII by eligible wage-earner debtors.⁶ The Commission recommended that relief available under Chapter XIII be made more attractive in a number of ways,⁷ that its benefits be made available to any individual debtor with sufficiently regular and stable income to be able to make fixed payments of indebtedness pursuant to a plan,⁸ and that every individual eligible for such relief be counseled as to the options available under the bankruptcy laws before being required to select a form of relief.⁹

The Commission did not focus solely on the individual debtor. With

¹ REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, Part I, H.R. Doc. No. 137, Part I, 93d. Cong., 1st Sess. 1, 9, 33 (1973) [hereinafter cited as COMMISSION REPORT I]. The preamble to the Act of July 24, 1970 (amended 1973), Pub. L. No. 91-354, 84 Stat. 468, which created the Commission, referred first to the increase in the number of bankruptcies by more than 1000 percent in the preceding twenty years.

² Act of July 24, 1970 (amended 1973), Pub. L. No. 91-354, 84 Stat. 468.

³ COMMISSION REPORT I, *supra* note 1, at 9.

⁴ See Twinem, *Bankruptcy Report: Some Limitations on Creditors' Rights*, 29 BUS. LAW. 353, 354 (1974); Wiese, *The Position of the National Consumer Finance Association on the Report of the Commission on Bankruptcy Laws and the Proposed Bankruptcy Act of 1973*, 28 PERS. FIN. L.Q. REP. 47, 48 (1974).

⁵ COMMISSION REPORT I, *supra* note 1, at 9, 11, 159-60.

⁶ *Id.* at 9, 12, 157-58.

⁷ *Id.* at 13-14. The Commission suggested making relief by way of composition as well as extension available notwithstanding a debtor's having obtained a discharge or confirmation of a composition within the previous five-year period; eliminating confirmation of a composition as a limitation on future relief under the bankruptcy laws; eliminating the necessity of obtaining unsecured creditors' consent to a plan; enabling a debtor to obtain relief respecting indebtedness secured by real property; and enabling a debtor to obtain relief respecting indebtedness secured by personal property notwithstanding the secured creditor's objection.

⁸ See *id.* at 11.

⁹ *Id.* at 11, 159-60; REPORT OF THE COMMISSION ON BANKRUPTCY LAWS OF THE UNITED STATES, H.R. Doc. No. 137 Part II, 93d Cong., 1st Sess. § 4-203, 73-74 (1973) [hereinafter cited as COMMISSION REPORT II].

respect to business bankruptcies, the Commission's principal concerns related to the inadequacy of relief afforded creditors. The meagerness of distributions to creditors has been a frequent focus of critics of bankruptcy administration in this country.¹⁰ The Commission on Bankruptcy Laws of the United States found that factors delaying the commencement of proceedings under the Bankruptcy Act when liquidation was inevitable tended to reduce the estate available for distribution.¹¹ In order to make the bankruptcy laws "more effective as an instrumentality for relief at the instance of creditors," the Commission recommended eight changes in the laws:

(1) The concept of 'an act of bankruptcy' be abolished and the debtor be made amenable to involuntary proceedings when he has ceased to pay his debts or will be generally unable to pay his current liabilities.

(2) A debtor be protected against the risks of ill-founded petitions by requiring the court to hold a hearing immediately after the filing of an involuntary petition to determine whether the relief sought is in the best interests of the debtor and its creditors.

(3) A general assignment or general receivership continue to be a basis for involuntary proceedings without regard to whether the debtor was insolvent or unable to pay his debts at the time of the filing of the petition, on the premise that such a disposition or proceeding contemplates a liquidation and that creditors be able to require it to be conducted subject to the safeguards provided by the Bankruptcy Act.

(4) There be no jury trial of any issue raised on an involuntary petition.

(5) A creditor or creditors who have aggregate claims of \$2,500 be able to file an involuntary petition for liquidation of the debtor, and one or more creditors having claims of \$10,000 or more be able to file a petition seeking reorganization of the debtor.

(6) The estate be protected against the risk of depletion and deterioration of assets pending a determination of the issues on an involuntary petition by allowing the Bankruptcy Administration with court approval to take immediate possession to preserve the property during the interim before determination of the issues on the petition.

(7) During the interim between the filing of the petition and the determination of the issues thereon, persons dealing with the debtor in the ordinary course of his business be protected by being

¹⁰ See, e.g., S. ENZER, R. DE BRIGARD, & F. LANGAR, SOME CONSIDERATIONS CONCERNING BANKRUPTCY REFORM 218 (1973); D. STANLEY & M. GIRTH, BANKRUPTCY: PROBLEM, PROCESS, REFORM 92-93, 130 (1971); Lacy, *Land Sale Contracts in Bankruptcy*, 21 U.C.L.A. L. REV. 477, 502 (1973).

¹¹ COMMISSION REPORT I, *supra* note 1, at 14.

allowed to retain money or property acquired and to have claims against the estate for credit extended, and the Bankruptcy Administration be authorized to give express approval to specific transactions pending the resolution of the issues on the petition.

(8) The exclusion of corporations other than those that are moneyed, business, or commercial from amenability to involuntary proceedings be eliminated, along with the meaningless 'wage earner' exclusion.¹²

The problem of delay confronted not only creditors anxious to commence an involuntary proceeding to liquidate a debtor's estate. A debtor contemplating reorganization under Chapter XI frequently postponed the filing of the petition until losses and deterioration of his financial condition frustrated efforts to accomplish any realistic rehabilitation.¹³ An involuntary petition for a composition, extension, or reorganization was not available under the Bankruptcy Act except under Chapters VIII and X.¹⁴ These chapters, however, authorized petitions to be filed only by or against corporations,¹⁵ and the chapters were designed primarily for large, publicly-held corporations needing pervasive adjustments of their debt and capital structure.¹⁶ The use of Chapter X, which applied to corporations other than railroad corporations, was more restricted than the architects of the chapter intended.¹⁷ Consequently, most reorganizations of debtors under the Bankruptcy Act were effected in cases commenced and controlled by the debtors themselves.¹⁸ Chapter XII authorized a creditor or creditors under certain circumstances¹⁹ to propose a plan for reorganization. This option, however, was not exercised often because of the restrictions on its applicability and the benefits available under the chapter. The Commission recommended the consolidation of the reorganization chapters into a single chapter to eliminate the necessity of choosing the correct mode of relief and

¹² *Id.* at 15.

¹³ See *Hearings on H.R. 31 & H.R. 32 Before the Subcommittee on Civ. & Const'l Rts. of the House Comm. on the Judiciary*, 94th Cong., 1st Sess. 1867 (1976)(statement of Harvey L. Miller, William J. Rochelle, and J. Ronald Trost for the National Bankruptcy Conference) [hereinafter cited as *Hearings*].

¹⁴ An involuntary petition could be filed under § 77(a) of the Bankruptcy Act of 1898, R. BANKR. P. 8-103, and under § 126 of the Bankruptcy Act, and R. BANKR. P. 10-105 but not under any of the sections and rules applicable to Chapter IX, Chapter XI, and Chapter XII cases.

¹⁵ Bankruptcy Act §§ 88(a), 107, 126.

¹⁶ See COMMISSION REPORT I, *supra* note 1, at 23.

¹⁷ *Id.* at 246-48. The Commission Report described the increasing resort to Chapter XI rather than Chapter X for reorganization of large, publicly-held debtors. See also H.R. REP. No. 595, 95th Cong., 1st Sess. 222, reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5963, 6182 [hereinafter cited as HOUSE REPORT]. But see *Hearings*, *supra* note 13, at 2171-75 & 2208, containing rebuttal testimony by the Securities & Exchange Commission on the use of Chapters X and XI.

¹⁸ HOUSE REPORT, *supra* note 17, at 244-54, [1978] U.S. CODE CONG. & AD. NEWS at 6201-13.

¹⁹ Bankruptcy Act § 466, and R. BANKR. P. 12-36(b)(1976).

to eliminate the resulting litigation of the question whether the correct choice was made.²⁰ The result enlarged the kinds of relief obtainable in a reorganization case, and the Commission recommended that creditors should be enabled to commence an involuntary reorganization case as well as a case for liquidation.²¹

Finally, the Commission recognized that special problems arise in connection with estates that have assets in the United States and other countries. Therefore the Commission recommended a continuation of the option available to the debtor or a creditor to seek dismissal or suspension of a case commenced under the Bankruptcy Act when a liquidation or rehabilitation proceeding is pending in another country.²² The Commission proposed that the representative of a debtor undergoing liquidation or rehabilitation in a foreign country also should be afforded the option of filing a bankruptcy petition in this country against the debtor or a complaint seeking the dismissal or suspension of a petition previously filed by or against the debtor. The Commission also recommended that representatives be able to seek an injunction to stay any action against the debtor or enforcement of any lien against the debtor's property, or a complaint seeking turnover of property of the debtor.²³ These proposals looked to the enhanced possibilities of coordinated administration of estates involving other countries as well as the United States.²⁴

The reforms enacted by Congress on November 6, 1978, as the new Bankruptcy Code,²⁵ embody most of the recommendations of the Commission on Bankruptcy Laws set out in the preceding paragraphs. This article is an examination of the provisions of the Code that bear on the commencement of a case.

II. THE FOUR KINDS OF CASES UNDER THE BANKRUPTCY CODE

The commencement of a case under the new Bankruptcy Code is governed by sections 301-04 in Subchapter I of Chapter 3.²⁶ Four different kinds of cases are recognized in the new law, and a separate section of Title 11 deals with each. Section 301 covers voluntary cases, section 302 deals

²⁰ COMMISSION REPORT I, *supra* note 1, at 23, 28, 245-48.

²¹ *Id.* at 28; COMMISSION REPORT II, *supra* note 9, § 4-205(b), at 74.

²² COMMISSION REPORT II, *supra* note 9, § 4-103(a), at 69.

²³ *Id.* § 4-103(b)(2), at 69.

²⁴ The proposals for coordination between foreign and domestic bankruptcies were the target of extended criticism but were enacted substantially as proposed. *See* notes 158, 217, 221-23, & 225 *infra*.

²⁵ Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549 (1978). The new Bankruptcy Code is sometimes referred to as the Bankruptcy Reform Act or the Edwards Act. It will not be referred to as the Bankruptcy Act in this article, since that is the proper title of the bankruptcy law originally enacted in 1898. *See* Act of Dec. 20, 1959, Pub. L. No. 81-879, 64 Stat. 1113. The Bankruptcy Code will frequently be referred to in the text and notes simply as the 'Code'.

²⁶ Chapter 3 is entitled "Case Administration," 11 U.S.C.A. §§ 301-66 (1979) and Subchapter I is entitled "Commencement of a Case." 11 U.S.C.A. § 301-06 (1979).

with joint cases, section 303 governs involuntary cases, and section 304 is concerned with cases ancillary to foreign proceedings.

These four sections govern the commencement of all cases whether the petitioner is seeking liquidation, a composition, extension, reorganization, or any other variety of relief available under the Code. These sections should eliminate or minimize differences that have heretofore characterized the rules and forms applicable under different chapters of the Bankruptcy Act.

A. Voluntary Cases - Section 301

1. The Petition

Section 301 authorizes a voluntary case to be commenced by a debtor filing a petition²⁷ under Chapter 7, Chapter 9, Chapter 11, or Chapter 13.²⁸ Chapter 7 provides for liquidation of a debtor's estate; Chapter 9 for adjustment of the debts of a municipality; Chapter 11 for reorganization of a debtor; and Chapter 13 for adjustment of the estate by an extension or composition of the debts of an individual with regular income. A voluntary case is commenced by the filing of a petition with the bankruptcy court.²⁹ As under most of the sections of the Bankruptcy Act authorizing a voluntary petition, a voluntary petition under the Code cannot be contested.³⁰

²⁷ "[P]etition" is defined in § 101(31) of the Code as a "petition filed under Section 301, 302, 303, or 304 of this title, as the case may be, commencing a case under this title." 11 U.S.C.A. § 101(31) (1979). [In this article all citations to sections and references to this title are references to Title 11 of the United States Code unless otherwise indicated.] "Petition" was defined in § 1(24) of the Bankruptcy Act as "a document filed in a court of bankruptcy or with a clerk thereof initiating a proceeding under this title." This definition is also an appropriate one for the Bankruptcy Code, except that the petition initiates a "case" rather than a "proceeding." The shift in usage from "proceeding" to "case" occurred prior to enactment of the Code.

²⁸ Section 109 defines who may be a debtor. Subsection (b) states who may be a debtor under Chapter 7; subsection (c) states who may be a debtor under Chapter 9; subsection (d) states who may be a debtor under Chapter 11; and subsection (e) states who may be a debtor under Chapter 13. Chapters 1, 3, 5, and 15 apply generally to cases commenced under Chapters 7, 11, and 13. Chapter 1 and substantial portions of Chapters 3, 5, and 11 apply to cases under Chapter 9. §§ 103(e) and 901.

²⁹ H.R. 8200, the version of the Bankruptcy Code originally passed in the House, did not require a petition to be filed with the bankruptcy court. S. 2266, however, designated the place of filing as the bankruptcy court, and the House Managers acceded to the Senate on this point. 124 CONG. REC. H11091 (daily ed. Sept. 28, 1978)(statement by Rep. Edwards); 124 CONG. REC. S17497 (daily ed. Oct. 6, 1978)(statement by Sen. DeConcini). [Citations to Congressman Edwards' and Senator DeConcini's nearly identical statements in 124 CONG. REC. H11089-11115, S17406-17432, explaining the changes made in the bills originally passed by the House and Senate, are hereinafter cited as CONGRESSIONAL RECORD.] The National Conference of Bankruptcy Judges urged that all petitions be filed in the bankruptcy court to assure complete control by the court over all controversies and matters arising out of cases filed under the bankruptcy laws. See generally Lee, *A Critical Comparison of the Commission Bill and the Judges' Bill for the Amendment of the Bankruptcy Act*, 49 AM. BANKR. L.J. 1 (1975).

³⁰ No answer to a voluntary petition in straight bankruptcy (*i.e.*, for liquidation) or one

Filing the petition results in an automatic entry of an order for relief under the chapter invoked by the petition.³¹ The expression "order for relief"³² in the Code is equivalent to adjudication under the Bankruptcy Act³³ and is tantamount to an order approving the court's exercise of jurisdiction to grant relief pursuant to the provisions of the law. If the debtor is ineligible or the petition is insufficient, however, the language of the statute does not preclude the court from taking whatever action is appropriate to dispose of the document.³⁴

Neither insolvency nor inability to pay debts nor even the fact that the debtor is indebted in any amount is required to be alleged or proved under section 301. Section 109(c) requires a municipality seeking relief under Chapter 9, however, to show insolvency or inability to pay its debts, and section 109(e) apparently requires a petitioner who files under Chapter 13 to owe both unsecured and secured debts that are liquidated and noncontingent. The section, however, prescribes only the maximum and not the minimum amount of the debt.³⁵ The Bankruptcy Code requires no change

filed under Chapter IX, XI, XII, or XIII was authorized by the Bankruptcy Act or the Rules of Bankruptcy Procedure. There were two exceptions to the general rule: R. BANKR. P. 9-110(a)(2) authorized an answer to a voluntary petition under § 77 of the Bankruptcy Act to be filed by a creditor, stockholder, or indenture trustee, and § 137 of the Act, and R. BANKR. P. 10-112(a)(2) authorized a creditor or indenture trustee to controvert the allegations of a petition filed by a debtor in a Chapter X case. If the Chapter X debtor was not insolvent, any stockholder of the debtor could also file an answer.

³¹ Bankruptcy Code § 301 (2d sentence), 11 U.S.C.A. § 301(2d sentence) (1979).

³² Under Code § 102(6) the expression, "order for relief," means entry of an order for relief.

³³ See HOUSE REPORT, *supra* note 17, at 321, [1978] U.S. CODE CONG. & AD. NEWS at 6277. The effect of the second sentence of § 301 is essentially the same as provided by § 18f of the Bankruptcy Act. "Adjudication," as defined by § 1(2) of the Bankruptcy Act, meant "a determination whether by decree or by operation of law, that a person is a bankrupt." "The term adjudication is replaced by a less perjorative [sic] phrase in light of the clear power of Congress to permit voluntary bankruptcy without the necessity for an adjudication, as under the 1898 Act, which was adopted when voluntary bankruptcy was a concept not thoroughly tested." HOUSE REPORT, *supra* note 17, at 321, [1978] U.S. CODE CONG. & AD. NEWS at 6277. The "Bankruptcy Act of 1973," drafted by the Commission on the Bankruptcy Laws of the United States, had likewise substituted "order [or direction] for relief" for "adjudication." COMMISSION REPORT II, *supra* note 9, § 4-210, at 79-80.

Guidelines issued by the Co-reporters for the Advisory Committee on Bankruptcy Rules suggest, in a proposed Rule 1001(2) that "adjudication" be read to mean "order for relief" in all the Rules of Bankruptcy Procedure. The guidelines are further discussed in note 42 *infra*.

³⁴ The Rules of Bankruptcy Procedure do not specify the manner of attacking the jurisdiction of the bankruptcy court over a voluntary petition filed by an ineligible debtor, but Rule 121 does indicate that certain rules in Part 7 apply in proceedings to vacate an adjudication. With a substitution of "order for relief" for "adjudication," this rule still applies under the Code. See § 301. The Bankruptcy court would have no jurisdiction of a petition filed by an ineligible debtor, and the petition would be subject to dismissal by a bankruptcy court on the court's motion or on motion by a party in interest. See Seligon & King, *Jurisdiction and Venue in Bankruptcy*, 36 REF. J. 38-40 (1962). Lack of jurisdiction cannot be waived by a failure to object or delay in raising an objection to the court's jurisdiction.

³⁵ It is unlikely that the lack of "noncontingent, unliquidated" debts, secured or unsecured, will be held to render a petitioner ineligible for relief under Chapter 13, so long as the

in the allegations that a voluntary petitioner must make to obtain relief in a straight bankruptcy³⁶ or for adjustment of municipal indebtedness.³⁷ Inasmuch as voluntary petitions under Chapters VIII, IX, X, XI, XII, and XIII of the Bankruptcy Act had to allege insolvency or inability to pay debts,³⁸ however, there has been a liberalization of access by individuals, partnerships, and corporations to the bankruptcy court for reorganization and rehabilitation.

Rules of Bankruptcy Procedure will continue to govern the form of the petition and other aspects of practice and procedure not prescribed by the Code.³⁹ The Supreme Court's rule-making authority in the area of bankruptcy is circumscribed by the Code. However, the provision of the Enabling Act nullifying laws inconsistent with the rules and forms promulgated by the Court was repealed.⁴⁰ Section 405(d) of Public Law No. 95-598, nevertheless, provides that

[t]he rules prescribed under section 2075 of title 28 of the United States Code and in effect on September 30, 1979, shall apply to cases under title 11, to the extent not inconsistent with this Act, until such rules are repealed or superseded by rules prescribed and effective under such section, as amended by . . . this Act.

The Chief Justice has appointed an Advisory Committee on Bankruptcy Rules and two Co-reporters to prepare and propose Rules of Bankruptcy Procedure to apply in cases under the new Code.⁴¹ Since section 2075 of Title 28 requires rules promulgated pursuant to the section to be reported to Congress by May 1, the Committee did not deem it feasible to under-

debtor schedules or alleges some indebtedness and requests relief under the Code.

³⁶ The Bankruptcy Act did not require a voluntary petition for liquidation to contain any allegation regarding the petitioner's financial condition. Official Form No. 1, promulgated by the Supreme Court pursuant to § 30 of the Bankruptcy Act, required a voluntary petition in bankruptcy to allege that the petitioner owed debts, but that allegation was not required by Official Form No. 1 promulgated by the Court pursuant to 28 U.S.C. § 2075 (1976), which superseded § 30 of the Bankruptcy Act in 1964.

³⁷ Section 84 of the Bankruptcy Act, as amended by 90 Stat. 317, Act of Apr. 8, 1976, Pub. L. No. 94-260, like § 109(e) of the Code, required a petitioner under Chapter IX to allege insolvency or inability to pay debts as they mature.

³⁸ See §§ 77(a), 84, 130(1), 323, 423, 623.

³⁹ See 28 U.S.C. § 2075, as amended by Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, Title II, § 247, 92 Stat. 2672.

⁴⁰ This lamentable change requiring rules and forms hereafter promulgated pursuant to 28 U.S.C. § 2075 to be consistent with Congressionally enacted laws, is discussed in Kennedy, *The Bankruptcy Court Under the New Bankruptcy Law: Its Structure, Jurisdiction, Venue, and Procedure*, 11 ST. MARY'S L. J. 251, 304-09 (1979).

⁴¹ The Chairman of the Advisory Committee on Bankruptcy Rules is Circuit Judge Ruggero J. Aldisert of the Court of Appeals of the Third Circuit. The other members are Bankruptcy Judge Clive Bare, District Judge John T. Copenhaver, Jr., Professor Robert W. Foster, Charles Horsky, Esq., Bankruptcy Judge Beryl E. McGuire (retired), Bankruptcy Judge Asa Herzog (retired), Norman H. Nachman, Esq., Bankruptcy Judge Alexander L. Paskay, Joseph Patchen, Esq., District Judge Morey L. Sear, and District Judge Morell E. Sharp. The Co-reporters are Professors Lawrence P. King and Walter Taggart.

take to propose any new rules to take effect before October 1, 1979, the effective date of the Code. Guidelines have been prepared by the Committee and its Co-reporters, however, for the assistance of the bench and bar in developing interim procedures pending the promulgation of new Rules.

The consolidation of the requirements of a voluntary petition into a single section of the Code, along with the simplicity of those requirements, permits the use of a single form with alternative recitals to permit designation of the chapter under which the petitioner seeks relief. Accordingly, guidelines issued by the Co-reporters for the Advisory Committee on Bankruptcy Rules have suggested the use of a single, simple form.⁴² Schedules,

⁴² The guidelines issued by the Advisory Committee on Bankruptcy Rules suggested a Rule 1002 entitled "Debtor's Petition." This rule is suggested for use in lieu of Rules 103, 8-102, 9-3, 10-104, 11-6, 12-6, and 13-103, which have heretofore governed the filing of voluntary petitions under the several chapters of the Bankruptcy Act.

Subdivision (a) of suggested Rule 1002 requires a voluntary petition to conform substantially to Form No. 1, which is an adaptation of Official Forms No. 1, 11-F1, 12-F1, and 13-1. The result is a considerable simplification of the petition to be filed in a reorganization case by a debtor seeking relief of the kind formerly available only under Chapter VIII (§ 77) or Chapter X. An argument may be made that the more elaborate recitals prescribed by Rules 8-102 and 10-104 and Official Forms No. 8-1 and 10-1 are still effective because not inconsistent with the Bankruptcy Code, but the practical answer is that until a new set of Rules of Bankruptcy Procedure is promulgated in accordance with the enabling Act, practice and procedure under the Code will be largely governed by local rules.

Rule 927 contemplates that local bankruptcy rules may be promulgated and amended by a majority of the judges of each district court. Although the relationship between the United States district court and the bankruptcy court is considerably more attenuated under the Code than under the Bankruptcy Act, the grant of jurisdiction of cases and civil proceedings to the district court by 28 U.S.C. § 1471(a) and (b), as amended by the Bankruptcy Reform Act, Pub. L. No. 95-598, § 241, 92 Stat. 2668, should serve to sustain the power of the district court to prescribe local rules for practice and procedure under the Bankruptcy Code pending supersession of the existing rules by the Supreme Court pursuant to 28 U.S.C. § 2075 (1976).

A Comment accompanying Rule 927 of the 1979 Collier Pamphlet Edition of the Bankruptcy Rules declares that "[a]fter October 1, 1979 the power to make local rules will be vested in the bankruptcy court rather than the district court." The Comment then cites 28 U.S.C. §§ 156, 157, and 1471(c), added by §§ 201 and 241 of the Bankruptcy Reform Act of 1978. The first cited section, however, goes no further than to authorize rules of the bankruptcy court to provide for division of the business of a bankruptcy court having more than one judge, and the second cited section goes no further than to authorize each bankruptcy court to establish by local rule or order schedules of court sessions at designated places of holding court other than at the headquarters office of the court. Section 1471(c) provides that the bankruptcy court "shall exercise all of the jurisdiction conferred by this section on the district courts," but this jurisdictional grant can hardly be said to be inconsistent with Rule 927. In the existing state of uncertainty as to the locus of the power to prescribe local rules, it is advisable for the bankruptcy judges and the district judges to act cooperatively and jointly in promulgating such rules.

Although Rule 106 arguably remains effective and applicable because not inconsistent with the Bankruptcy Code, a suggested new Rule 1005 has been drafted to prescribe a uniform caption for a petition for a case filed under any chapter of Title 11.

Rule 109 and corresponding rules for cases filed under Chapters VIII-XIII of the Bankruptcy Act, which require verification of the petition, accompanying documents, and amendments appear to remain applicable under the principle of noninconsistency, but the guide-

lists of creditors, and statements of affairs are required to be filed by statutory provisions that are generally consistent with the Rules of Bankruptcy Procedure.⁴³ The guidelines issued by the Co-reporters suggest, however, a new Rule 1007 to accommodate particular needs for information regarding creditors and equity security holders in a Chapter 11 case.

2. Eligible Debtors

Section 109 defines who may be a debtor under new Title 11. Subsection (a) makes it clear that only a person who resides in the United States, or has a domicile, place of business, or property in the United States, may be a debtor under Chapter 7, 11, or 13.⁴⁴ Any person may be a debtor under Chapter 7 unless excluded by one of the three paragraphs of section 109(b). A "person" is defined in section 101(30) to include an individual partnership, and a corporation.⁴⁵ A governmental unit is not included,⁴⁶ but if it

lines of the Co-reporters have suggested an unsworn declaration be added at the end of each of these papers pursuant to 28 U.S.C. § 1746 (1976). A signed certification "under the penalty of perjury" is given the same effect under the statute as a verification.

Rule 1002 suggested as a guideline by the Co-reporters includes new requirements regarding the number and routing of copies of petitions, and a new Rule X-1002 prescribes that the United States trustee shall get a copy of a petition and of all related documents in a pilot district. A pilot district is one of eighteen such districts designated for an experiment to be conducted under the supervision of the Attorney General between October 1, 1979, and April 1, 1984. See 11 U.S.C.A. § 1501 (1979). The experiment is designed to discover the feasibility and desirability of a system of bankruptcy administration employing an official trustee with responsibility for supervising administration of cases and trustees in cases under Chapters 7, 11, and 13 and acting as trustee in certain cases under Chapters 7 and 13.

⁴³ Compare § 521(1) with R. BANKR. P. 108.

⁴⁴ This limitation of eligibility is consistent with the result that would be reached under § 2a(1) of the Bankruptcy Act. See Comment, 35 N.C. L. REV. 476, 477-78 (1957).

⁴⁵ The chauvinistic inclusion of "women" in the definition of "persons" in § 1(23) of the Bankruptcy Act is omitted from 11 U.S.C.A. § 101(30) (1979). The word "partnership" remains undefined in the Code. Therefore, what constitutes a partnership is left to nonbankruptcy law. See 1A W. COLLIER, BANKRUPTCY ¶ 5.02 (14th ed. 1974) [hereinafter cited as COLLIER]. The word "corporation" is defined in § 101(8) of the Code in much the same way as it is defined in § 1(8) of the Bankruptcy Act. The word is defined in both places to include unincorporated organizations. Since the corporateness of the debtor is not material in determining eligibility or amenability of a debtor for relief under the new law, the definition has less significance under the new law than it had under the old.

The HOUSE REPORT, *supra* note 17, at 309, [1978] U.S. CODE CONG. & AD. NEWS at 626, noted that the new definition of a debtor "is intended specifically to include a labor union" and overrules *In re Freight Drivers Local No. 600*, 432 F. Supp. 1326, 1328 (E.D. Mo. 1977). That decision, which was an erroneous construction of the Bankruptcy Act, already has been reversed in *Gordon Transports, Inc. v. Highway & City Frt. Drivers, Local No. 600*, 576 F.2d 1285 (8th Cir.), *cert. denied*, 99 S. Ct. 612 (1978).

A municipality may not be a debtor under Chapter 7 because it is not a person. See § 101(14), (29), (30).

⁴⁶ A "governmental unit" means "United States; State; Commonwealth; District; Territory; municipality; foreign state; department; agency, or instrumentality of the United States, a State, a Commonwealth, a District, a Territory, a municipality, or a foreign state, or other foreign or domestic government." § 101(21). A "governmental unit," along with a "person, estate, [or] trust," is included in the term "entity." § 101(14).

is a municipality, defined as a "political subdivision or public agency or instrumentality of a State,"⁴⁷ it may be a debtor under Chapter 9 but not any other chapter.⁴⁸ Three groups of persons are excluded from eligibility from relief under Chapter 7: (1) a railroad;⁴⁹ (2) a domestic insurance company,⁵⁰ bank,⁵¹ savings bank,⁵² cooperative bank,⁵³ savings and loan association,⁵⁴ building and loan association,⁵⁵ homestead association,⁵⁶ or

⁴⁷ Section 101(29).

⁴⁸ Section 109(c).

⁴⁹ Section 109(b)(1). A railroad is defined in § 101(33) as a "common carrier by railroad engaged in the transportation of individuals or property or owner of trackage facilities leased by such common carrier." The definition is a modification of the term "railroad corporation" as used in § 77(m) of the Bankruptcy Act, which had required that such a corporation be engaged in interstate commerce. The most plausible explanation for including the limitation in § 77 is that Congress had doubts in 1933 when § 77 was enacted that its power to provide for reorganization of railroads extended to an intrastate carrier. See HOUSE REPORT *supra* note 17, at 313, [1978] U.S. CODE CONG. & AD. NEWS at 6270.

⁵⁰ Section 109(b)(2). Section 4 of the Bankruptcy Act, in subsections (a) and (b), excluded insurance corporations from eligibility and amenability as bankrupts. Although "corporation" was defined in § 1(8) of the Bankruptcy Act, to include an unincorporated association, the term is not as broad as "company," which may include a partnership or conceivably an individual entrepreneur. A foreign insurance corporation engaged in the insurance business in the United States, as well as a domestic insurance corporation, was no doubt excluded from the eligibility as a bankrupt or debtor under the Bankruptcy Act.

⁵¹ Section 109(b)(2). Section 4 of the Bankruptcy Act excluded a banking corporation from eligibility and amenability as a bankrupt. Several cases have held that partnerships and individuals engaged in banking were eligible for relief under the Bankruptcy Act. See, e.g., *In re Faour*, 72 F.2d 719, 720(2d Cir.), cert. denied, 293 U.S. 613 (1934)(individual); *Fahey v. Sapio*, 30 F.2d 330, 331-32 (5th Cir.), cert. denied, 279 U.S. 871 (1929)(partnership); *Missouri v. Angle*, 236 F. 644, 650 (8th Cir. 1916)(individual); *Dickas v. Barnes*, 140 F. 849, 851-52 (6th Cir. 1905)(partnership). The exclusion by § 109(b) of a bank without regard to the form of its organization overrules these cases. A foreign banking corporation doing business in the United States as well as a domestic banking corporation was probably excluded from eligibility as a bankrupt or debtor under the Bankruptcy Act. Cf. text accompanying notes 61, 62, 69 & 70 *infra*.

⁵² Section 109(b)(2). A savings bank is a new category of excluded persons, but a savings bank constituting a corporation within the broad definition of § 1(8) of the Bankruptcy Act was undoubtedly excluded by § 4 of that Act.

⁵³ Section 109(b)(2). A cooperative bank is a new category of excluded persons but was undoubtedly excluded under the Bankruptcy Act as a banking corporation. See note 52 *supra*.

⁵⁴ Section 109(b)(2). A savings and loan association is generally regarded as another name for a building and loan association. *Sovern, Section 4 of the Bankruptcy Act: The Excluded Corporations*, 42 MINN. L. REV. 171, 198 (1957)[hereinafter cited as *Sovern*]. But see *Clemons v. Liberty Sav. & Real Estate Corp.*, 61 F.2d 448, 450 (5th Cir. 1932)(corporation "organized to do a general savings and loan business" held to be neither a bank nor a building and loan association). Both a building and loan association and a savings and loan association receive funds from small investors primarily for use in financing home purchases. See *Sovern, supra*, at 199.

⁵⁵ Section 109(b)(2). A building and loan association was excluded by an amendment of § 4 of the Bankruptcy Act, made by Act of Feb. 11, 1932, Pub. L. No. 72-27, Ch. 38, 47 Stat. 47. Such an association had theretofore been held amenable to an involuntary petition under the Bankruptcy Act. *In re Bay Cities Guaranty Building-Loan Ass'n*, 48 F.2d 623, 624-25 (S.D. Cal. 1931). An objection was raised to the 1932 amendment of § 4 because two states

credit union;⁵⁷ and (3) a foreign entity like any of those listed in the second group but engaged in business in the United States.⁵⁸ The exclusion of a railroad continues a limitation on the court's jurisdiction in a liquidation case under the Bankruptcy Act,⁵⁹ but the assumption underlying the limitation that a railroad should not be liquidated is no longer valid. Thus a railroad may be liquidated in a case under Chapter 11.⁶⁰ The exclusions of the second and third groups of persons, most of whom also were excluded by the Bankruptcy Act,⁶¹ are premised on a Congressional reluctance to displace established modes of administration of the estates of excepted

had no laws controlling building and loan associations. The report of the House Committee on the Judiciary accompanying the amendment, however, explained that state equity and insolvency laws may be invoked to obtain administration of the affairs of such an association. H.R. REP. NO. 98, 82d Cong., 1st Sess. 1 (1952).

⁵⁵ Section 109(b)(2). A homestead association is a new category of excluded persons. The exclusion overrules *Missco Homestead Ass'n, Inc. v. United States*, 185 F.2d 280, 282 (8th Cir. 1950) (corporation formed to borrow money from the United States to obtain real estate for sublease to tenant farmers held subject to bankruptcy under § 4 of the Bankruptcy Act).

⁵⁷ Section 109(b)(2). A credit union was not excluded under the Bankruptcy Act.

⁵⁸ Section 109(b)(3).

⁵⁹ Bankruptcy Act § 4a & b.

⁶⁰ Section 1174.

⁶¹ The Commission on Bankruptcy Laws considered whether the exclusions of building and loan associations and insurance and banking corporations should be retained in the Code. The Commission acknowledged that a number of prevalent problems concerning these organizations might be solved by appropriately drafted bankruptcy legislation but recognized that other difficulties would be engendered by such legislation. The availability of federal insurance was thought to mitigate, if it did not eliminate, most of the problems arising out of insolvencies of banking corporations and building and loan associations. The argument for bankruptcy jurisdiction of insurance corporations was stronger, but the Commission was persuaded by considerations set out in a memorandum prepared by Professor Spencer Kimball not to propose the extension of bankruptcy laws to insurance corporations. COMMISSION REPORT I, *supra* note 1, at 72, 183-84, 223 n. 12.

The National Conference of Bankruptcy Judges proposed in a bill, introduced as H.R. 32 in the 94th Congress, 1st Session, that insurance corporations no longer be excluded from the Bankruptcy Act. Not surprisingly, the American Life Insurance Association strongly opposed the proposal of the Bankruptcy Judges. *Hearings, supra* note 13, at 1582-84, 1620-22 (statement and testimony of John J. Creeden for the American Life Ins. Ass'n).

The National Bankruptcy Conference appointed a special committee to study the desirability and feasibility of bankruptcy legislation applicable to insurance companies and foreign banks. The committee recommended an extension of the bankruptcy laws to foreign banks not doing business in the United States. NATIONAL BANKRUPTCY CONFERENCE, REVISED REPORT ON FOREIGN BANKS OF THE SPECIAL COMM. ON INSURANCE COMPANIES AND FOREIGN BANKS 30-31 (1976). The National Bankruptcy Conference approved this recommendation and submitted it as part of its proposed "Bankruptcy Act of 1975" to the House Judiciary Committee. *Hearings, supra* note 13, Appendix, Ser. No. 27, at 349-51. With respect to insurance companies, the special committee prepared a careful report, at the end of which it concluded that the ultimate answer to the question whether insurance companies should be brought within the scope of the bankruptcy laws required extended study and recommended continuation of the exclusion pending the completion of such a study. REPORT ON INSURANCE COMPANIES OF THE SPECIAL COMMITTEE ON INSURANCE COMPANIES AND FOREIGN BANKS 28 (1975) [hereinafter cited as REPORT ON INSURANCE COMPANIES]. The recommendation respecting foreign banks eventuated in the enactment of § 303(k).

organizations.⁶² Like the Bankruptcy Act, the Code leaves undefined the terms used in identifying the kinds of persons excluded from eligibility and amenability, and neither the Code nor the legislative history undertakes to resolve the question whether the terms should be given a uniform meaning or whether they should depend on the state or other nonbankruptcy law. If state law provides the systems of administration for the categories of persons specified in the second and third groups of excluded persons it is appropriate for the courts to look to that law in determining whether a particular debtor fits into one of the excluded classes. The case law that developed under the Bankruptcy Act, however, tended to rely on state classification when the question was whether a particular debtor was excluded, as an insurance corporation,⁶³ and applied a uniform or federal test when the question was whether an excluded banking corporation was involved.⁶⁴ The cases also were split on the question whether the powers granted a corporation should be determinative, or whether its activities should be more significant.⁶⁵ The Code and its legislative history do not clearly opt for giving a federal or state-oriented content to the exclusionary words, but the fact that none of the excluded persons need be a corpo-

⁶² See HOUSE REPORT, *supra* note 17, at 318, [1978] U.S. CODE CONG. & AD. NEWS at 6265; SEN. REP. No. 989, 95th Cong., 2d Sess. 31 (1978), reprinted in [1978] U.S. CODE CONG. & AD. NEWS 5787, 5817 [hereinafter cited as SENATE REPORT]. Dean Sovern has shown that the reluctance to make domestic and foreign insurance companies, banks, savings banks, etc., eligible for relief under Chapter 7 rests on quite insubstantial evidence of legislative intent. Sovern, *supra* note 54, at 172-82. See Samuels, *Unregulated Foreign Banks in Bankruptcy: Section 4 of the Bankruptcy Act*, 23 N.Y.L.S. L. REV. 47, 73-76 (1977) [hereinafter cited as Samuels]. Dean Sovern acknowledged that there are sufficient differences between insurance and state banking corporations and state building and loan associations, on the one hand, and most other corporate debtors, on the other, to warrant excluding the former category from eligibility and amenability under the general bankruptcy laws, but suggested enactment of special chapters of the bankruptcy laws designed to deal with their particular problems. Sovern, *supra* note 54, at 243. The draftsmen of section 109(b)(2) and (3) have ignored Dean Sovern's analysis of the legislative history and suggestions for reform and have instead enlarged the exclusions of financial institutions from eligibility and amenability of debtors under the bankruptcy laws. See SENATE REPORT, *supra*, at 31, [1978] U.S. CODE CONG. & AD. NEWS at 5817. The only explanation given in the legislative history is a cryptic reference to "the change in various banking laws since the current law was last amended on this point." HOUSE REPORT, *supra* note 17, at 318, [1978] U.S. CODE CONG. & AD. NEWS at 6275; SENATE REPORT, *supra*, at 31, [1978] U.S. CODE CONG. & AD. NEWS at 5817.

⁶³ *Sims v. Fidelity Assur. Ass'n*, 129 F.2d 442, 451 (4th Cir. 1942), *aff'd*, 318 U.S. 608 (1943); Sovern, *supra* note 54, at 182-91, 194-98, 205.

⁶⁴ *In re Prudence Co.*, 79 F.2d 77, 79 (2d Cir.), *cert. denied*, 296 U.S. 646 (1935); Sovern, *supra* note 54, at 191-94, 205.

⁶⁵ Compare *In re Union Guarantee & Mtge. Co.*, 75 F.2d 984, 985 (2d Cir.), *cert. denied*, 296 U.S. 594 (1935) (company empowered to issue insurance policies held to be excluded as an insurance corporation), and *Gamble v. Daniel*, 39 F.2d 447, 450 (8th Cir.), *appeal dismissed*, 281 U.S. 705, *cert. denied*, 282 U.S. 848 (1930) (lack of power to accept deposits held conclusive that debtor was not bank), with *In re Supreme Lodge of the Masons Annuity*, 286 F. 180, 188 (N.D. Ga. 1923) (company issuing several forms of insurance held to be insurance corporation) and *Clemons v. Liberty Sav. & Real Estate Corp.*, 61 F.2d 448, 450 (5th Cir. 1932) (corporation held not a bank although empowered to receive deposits).

ration means that more deference should be given to activities of the debtor than to its powers.

When a petition by or against a debtor was challenged under the Bankruptcy Act on the ground that the debtor was a bank, the crucial question was whether the debtor received deposits.⁶⁶ A negative answer was usually dispositive,⁶⁷ but an affirmative answer might lead to a consideration of other factors.⁶⁸ Whether or not a debtor receives deposits is likely to continue to be significant in determining whether a debtor is one of the three varieties of excluded banks under the Bankruptcy Code.

Foreign insurance and financial institutions engaged in business in the United States are excluded from eligibility and amenability under the Bankruptcy Code on the same premise as that underlying the immunity of domestic institutions of the same kind. The corollary of this last exclusion is that a foreign insurance company, a foreign bank, or other foreign financial institution may be a debtor under the new bankruptcy law if it is not engaged in business in the United States but does have property here. The law thus adopts the approach taken in *Israel-British Bank (London) Ltd. v. FDIC*,⁶⁹ which held that a foreign bank not engaged in the banking business in this country was not a banking corporation within the meaning of section 4 of the Bankruptcy Act. The rationale for permitting relief under Title 11 concerning a foreign financial company not doing business here is based on the absence of any nonbankruptcy law of this country governing liquidation and rehabilitation of such an organization.⁷⁰ Conditioning bankruptcy jurisdiction over a foreign financial institution on the fact that it does not do business in the United States may be questioned on the ground that nonbankruptcy relief in this country for such a debtor is not inferior in availability or effectiveness to that provided a foreign financial institution doing business here.⁷¹ Such an argument,

⁶⁶ See, e.g., *In re Prudence Co.*, 79 F.2d 77, 79 (2d Cir. 1935)(debtor held not to be a banking corporation); *Woolsey v. Security Trust Co.*, 74 F.2d 334, 336-37 (5th Cir. 1934)(debtor held to be a banking corporation).

⁶⁷ See, e.g., *In re Prudence Co.*, 79 F.2d 77, 79-80 (2d Cir. 1935); *Gamble v. Daniel*, 39 F.2d 447, 450 (8th Cir. 1930).

⁶⁸ See, e.g., *Clemons v. Liberty Sav. & Real Estate Corp.*, 61 F.2d 448, 450 (5th Cir. 1932)(corporation's many powers to engage in transactions involving real estate, choses in action, and construction, without power to permit depositors to withdraw funds by check, considered); *In re Bay Cities Guaranty Bldg.-Loan Ass'n*, 48 F.2d 623 (S.D. Cal. 1931)(inability of depositors to draw checks on their deposits negated classification as bank).

⁶⁹ 536 F.2d 509 (2d Cir. 1976), cert. denied, 429 U.S. 978 (1976). The decision is subjected to extended criticism in *Samuels*, *supra* note 62, at 48, 68-76.

⁷⁰ After referring to the explicit coverage of foreign banks and insurance companies in § 109(b)(3), the legislative reports explained that banking institutions and insurance companies are excluded because "alternative provision is made for their liquidation under various regulatory laws." HOUSE REPORT, *supra* note 17, at 318, [1978] U.S. CODE CONG. & AD. NEWS at 6275; SENATE REPORT, *supra* note 62, at 31, [1978] U.S. CODE CONG. & AD. NEWS at 5817.

⁷¹ Cf. *Samuels*, *supra* note 62, at 72-92. Only ten American states and the District of Columbia permit foreign banks to do business within their jurisdictions. *Hablutzel & Lutz, Foreign Banks in the United States After the International Banking Act of 1978: The New*

however, goes more to raise doubts about the wisdom of excluding any financial institution from eligibility and amenability under the bankruptcy laws than about the propriety of differentiating between foreign companies that engage in business in this country and those that do not.⁷²

Access to relief under Chapter 9 is restricted to a municipality.⁷³ While there is no requirement that the municipality be located in the United States, the municipality must be "generally authorized to be a debtor under such chapter by State law or by a governmental officer or organization empowered by State law to authorize such entity to be a debtor under such chapter."⁷⁴ Since there is no counterpart in the new law to the definition of "States" in section 1(29) of the Bankruptcy Act, it appears that neither Washington, D.C., nor San Juan, Puerto Rico, nor any other city or political unit located in a territory or a possession of the United States can be a debtor under Chapter 9.⁷⁵ There are other limitations on the

Dual System, 96 BANKING L.J. 133, 141-42 (1979). Section 4 of the International Banking Act of 1978, 12 U.S.C.A. § 3102(a)(1979 cum. supp.), authorizes the Comptroller of the Currency to issue a federal charter to a foreign bank to establish an agency or branch in any of 32 states that neither permit nor prohibit foreign bank operations.

⁷² A principal advantage of bankruptcy relief is the availability of the avoiding powers of the trustee. Samuels, *supra* note 62, at 81. Another is the nationwide scope of the court's jurisdiction and the feasibility of a unitary administration. *Id.*; Sovern, *supra* note 64, at 215. Professor Samuels has pointed out that a domestic bank with assets in one state but subject to regulation only by another state is in much the same position as a foreign bank with property but not doing business in the United States. Samuels, *supra* note 62, at 98. It is not easily explicable why the advantages of bankruptcy relief should be available in a case involving a financial institution or insurance company only if it is not doing business in this country.

⁷³ Section 109(c)(1). A "municipality" is defined in section 101(29) as a "political subdivision or public agency or instrumentality of a State."

⁷⁴ Section 109(c)(2).

⁷⁵ While there may be special reasons why Washington, D.C., should not be eligible for relief under Chapter 9, it is not self-evident why all political subdivisions, public agencies, and instrumentalities in Puerto Rico, Guam, and other territories and possessions of the United States should be precluded from relief under the chapter. S. 658, which passed the Senate on September 7, 1979, included a new 11 U.S.C. § 101(37A), defining "State" to include "the Commonwealth of Puerto Rico, the Panama Canal Zone, the District of Columbia, and any territory or possession of the United States." It was explained in SEN. REP. No. 96-305, 96th Cong., 1st Sess. 2 (1979), that "[t]hese governmental units were inadvertently left out of the definition of 'state' during the passage of the Reform Act." There was actually no definition of "state" in the Bankruptcy Reform Act. S. 658 also included a new 11 U.S.C. § 102(9), defining "United States" to include the governmental units listed in the proposed definition of "State". It was explained in SEN. REP. No. 96-305, *supra* at 3, that the amendment was necessary to make clear that the law applied to debtors residing, having their domiciles, or having property in the areas mentioned. A Committee Print offered by Congressman Edwards in the House on October 22, 1979, as a substitute for S. 658 made no relevant change in § 101 but added the following two new paragraphs to § 102:

(9) 'United States', when used in a geographical sense, includes all locations where the judicial jurisdiction of the United States extends, including territories in possession of the United States; and

(10) except for the purposes of who may be a debtor in Chapter 9 of this title, "State" includes the District of Columbia and Puerto Rico.

availability of relief under section 109(c). The municipality must be insolvent or unable to meet its debts as they mature, must desire to effect a debt adjustment plan, or, unless excused, must have obtained an agreement of a majority of the creditors intended to be affected through the proposed plan.⁷⁶ The requirement of agreement of a majority of the creditors to the debtor's proposed plan is excused if the debtor has unsuccessfully negotiated in good faith, is unable to negotiate because such negotiation is impracticable, or reasonably believes a creditor may attempt to obtain a preference.⁷⁷

Only a person who may be a debtor under Chapter 7 may be a debtor under Chapter 11, except that a railroad may be a debtor under Chapter 11.⁷⁸ Two classes of persons eligible for relief under Chapter 7, but not Chapter 11, are stockbrokers and commodity brokers.⁷⁹

Finally, Chapter 13 affords relief to an individual with regular income who owes at the time of the filing of the petition unsecured debts of less than \$100,000 and secured debts of less than \$350,000.⁸⁰ The individual's spouse may be a joint petitioner under Chapter 13.⁸¹ No stockbroker or

⁷⁶ Section 109(c)(3), (4), &(5). The majority of creditors required to agree to a Chapter 9 plan is a number of creditors holding at least a majority in amount of the claims of each class that the debtor intends to impair under the plan it is proposing. Section 901 makes applicable in a Chapter 9 case the definition of impairment set out in § 1124.

⁷⁷ The requirements of § 109(c) of the Code are substantially a restatement of § 84 of the Bankruptcy Act.

⁷⁸ Section 109(d).

⁷⁹ A "stockbroker" is defined in § 101(39) as a person engaged in the business of effecting transactions and securities for the account of others or with members of the general public, from or for his own account. A "commodity broker" is defined in § 101(5) as a "futures commission merchant, foreign futures commission merchant, clearing organization, leverage transaction merchant, or commodity options dealer . . ." Bankruptcy relief concerning stockbrokers and commodity brokers is governed exclusively by Subchapters III and IV of Chapter 7.

⁸⁰ Section 109(e). An "individual with regular income" is defined in § 101(24) as an "individual whose income is sufficiently stable and regular to enable such individual to make payments under a plan under chapter 13 of this title, other than a stockbroker or commodity broker." The purpose and effect of §§ 101(24) and 109(e) are to enable sole proprietors of small businesses, as well as wage earners, to obtain relief under Chapter 13. A husband and wife engaged in operating a "mom & pop grocery store" may thus seek relief under Chapter 13 or under Chapter 11. If the spouses are a partnership, however, the partnership is eligible for relief only under Chapter 7 or Chapter 11, but that does not appear to preclude or prejudice the availability of relief of the spouses as individuals under Chapter 13. *See* HOUSE REPORT, *supra* note 17, at 320, [1978] U.S. CODE CONG. & AD. NEWS at 6277.

⁸¹ Section 109(e) authorizes an individual with regular income, or an individual with regular income and his or her spouse, to file a petition under Chapter 13. Thus an individual without regular income may not be a sole petitioner under Chapter 13, even though married to an individual with regular income. When spouses file under Chapter 13, their debts are combined, and the ceilings are applied to them as if they were a single petitioner. In discussing the eligibility of a husband and wife engaged in the grocery business as joint petitioners under Chapter 13, the HOUSE REPORT, *supra* note 17, at 320, [1978] U.S. CODE CONG. & AD. NEWS at 6277, stated that the crucial issue is "whether the assets of the grocery store are for the benefit of all creditors of the debtor or only for business creditors . . ." This explanation

commodity broker is eligible for relief under Chapter 13.⁸² In computing the indebtedness which must not exceed the ceiling, only noncontingent, liquidated indebtedness is considered.⁸³

3. Filing Fees

Filing fees are prescribed by section 1930 of Title 28 of the United States Code.⁸⁴ Until a very late date in the legislative process, the bankruptcy bills contemplated that, as recommended by the Commission on Bankruptcy Laws,⁸⁵ an *in forma pauperis* petition would be as available

is hardly illuminating, and the scope of Chapter 13 is further beclouded by a statement that "[t]he intent of the section is to follow current law that a partnership by estoppel may be adjudicated in bankruptcy and therefore would not prevent a Chapter 13 debtor from subjecting assets in such a partnership to the reach of all creditors in a Chapter 13 case." *Id.* The law has generally been understood not to authorize an adjudication of a partnership by estoppel under the Bankruptcy Act. *See In re Hudson Clothing Co.*, 148 F. 305, 307 (D. Me. 1906), *aff'd sub nom.* *Manson v. Williams*, 153 F. 525 (1st Cir. 1907), *aff'd*, 213 U.S. 453 (1909); *In re Kenney*, 97 F. 554, 559 (S.D.N.Y. 1899), *aff'd*, 105 F. 897 (2d Cir. 1900), *aff'd sub nom.* *Clarke v. Larremore*, 188 U.S. 486 (1903); *Tatum v. Acadian Production Corp. of La.*, 35 F. Supp. 40, 45 (E.D. La. 1940); *cf. In re Evans*, 161 F. 590, 591 (N.D. Ga. 1908). Moreover, if the estate of a partnership by estoppel were subject to administration as a separate entity in bankruptcy, the rights of the creditors of the individual members of the partnership in the partnership property would be subject to the right of the creditors of the partnership, who could first satisfy their claims out of that property. The individual partners' creditors would be entitled to reach the partnership property only if there was a surplus. *See HOUSE REPORT*, *supra* note 17, at 199. It is thus likely that the authors of the Report meant to say that if the husband and wife were members of a partnership by estoppel, that fact would not prevent either debtor or both debtors from filing a Chapter 13 petition. If one spouse should file, his or her creditors would be entitled to insist that a confirmed plan distribute property of value equal to their share of the property of the debtor without any priority for partnership creditors. Likewise, if both spouses should file, their creditors and the creditors of each would be entitled to distribution without subordination to the rights of any partnership creditors.

The rewriting of the discussion of § 109(e) in the HOUSE REPORT, *supra* note 17, at 320, [1978] U.S. CODE CONG. & AD. NEWS at 6277, as suggested above, is supported by this additional sentence in the REPORT: "However, if the partnership is found to be a partnership by agreement, even informal agreement, then a separate entity exists and the assets of that entity would be exempt from a case under Chapter 13." That statement is also confusing, however, insofar as it purports to confer an exemption on assets of a consensual partnership from the claims of creditors under Chapter 13. All the property of a Chapter 13 debtor, including his or her interest in a partnership or a corporation, should enter into the calculation of whether a plan proposed for confirmation under § 1325(a)(4) will yield a distribution equal to that of a liquidation under Chapter 7.

⁸² See note 79 *supra*.

⁸³ Section 109(e).

⁸⁴ See § 246 of Title II, Act of November 6, 1978, Pub. L. 95-598, 92 Stat. 2671.

⁸⁵ COMMISSION REPORT I, *supra* note 1, at 9; COMMISSION REPORT II, *supra* note 9, at 58-59. The Supreme Court ruled, by a five-to-four vote, that the bankruptcy Act precluded the filing of an *in forma pauperis* petition in bankruptcy and that it was constitutional for Congress to limit relief to petitioners who can pay filing fees. *United States v. Kras*, 409 U.S. 434, 436 (1973). The Commission had concluded from a study of the experience in states where the prevailing law permitted the filing of *in forma pauperis* petitions in bankruptcy that no significant increase in filings would result. COMMISSION REPORT I, *supra* note 1, at 9,

in the bankruptcy court as it is in other federal courts pursuant to section 1915 of title 28.⁸⁶ As finally enacted, however, section 1930 requires a payment to the clerk of the bankruptcy court of a filing fee for any case commenced under the Act, "[n]otwithstanding section 1915 of this title." At the same time, filing fees are substantially increased:

- (1) for a case commenced under Chapter 7 or Chapter 13, \$60;
- (2) for a case commenced under Chapter 9, \$300;
- (3) for a case commenced under Chapter 11 by or against a debtor other than a railroad, \$200; and
- (4) for a case commenced under Chapter 11 by or against a railroad, \$500.

An individual commencing a voluntary case under section 301 is authorized to pay filing fees in installments. The permissible payment period and the number of installments will be governed by Rules of Bankruptcy Procedure.⁸⁷ In explaining the increase in filing fees, the House and Senate managers of the bill pointed out that the new legislation abolishes the referees' salary and expense fund, "which was established long ago in an era when the bankruptcy courts were supposed to be self-supporting."⁸⁸ The explanation concluded that "[t]he referee salary and expense fund has been running a deficit for several years and deleting it serves to bring the bankruptcy court into line with all other Federal courts."⁸⁹ In a curious and confusing observation by the managers, the increase of filing fees was said to treat "bankruptcy cases identical with other Federal court cases and comports with dollar values appropriate in 1978 for gaining access to a Federal court."⁹⁰

11, see Shuchman, *Theory and Reality in Bankruptcy: The Spherical Chicken*, 41 LAW & CONTEMP. PROB. 66, 86-88 (1977).

⁸⁶ HOUSE REPORT, *supra* note 17, at 449, [1978] U.S. CODE CONG. & AD NEWS at 6404.

⁸⁷ Rule 107(b) of the Rules of Bankruptcy Procedure permitted four monthly installments and an extension of up to six months after the date of the filing of the petition. The Co-reporter's guidelines have suggested a new Rule 1006 that tracks Rule 107(b) with minor modifications: (1) In conformity with 28 U.S.C. § 1930(a), only an individual may apply for permission to pay fees in installments; (2) the application is to be accepted by, and payments of the fees are to be made to, the clerk of the bankruptcy court rather than of the district court; and (3) the requirement of Rule 107(b)(3) that filing fees must be paid in full before the bankrupt may pay his attorney for his services is omitted. Since suggested Interim Rule 1006(b)(2) is almost a verbatim copy of Bankruptcy Rule 107(b)(2), the omission of Bankruptcy Rule 107(b)(3) presumably represents a judgment by the new Advisory Committee on Bankruptcy Rules that the requirement that a debtor pay his filing fees before he pays his attorney is inconsistent with the new Bankruptcy Reform Act. If so, the conflict is not incontrovertibly clear.

⁸⁸ *Congressional Record*, *supra* note 29, at H11108 and S17425.

⁸⁹ *Id.*

⁹⁰ *Id.* The statement regarding identity of treatment of bankruptcy cases and other federal court cases presumably has reference to the fact that 28 U.S.C. § 1914(a) was amended by § 244 of the Bankruptcy Reform Act of 1978 to increase the fee for filing a civil action in a United States district court from \$15 to \$60. Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 244, 92 Stat. 2671. This change undoubtedly surprised many lawyers for plaintiffs who commenced actions in federal courts on and after October 1, 1979.

B. Joint Cases-Section 302

Section 302 authorizes the initiation of a joint case by an individual and his or her spouse. A joint case is commenced only by the filing with the bankruptcy court of a single petition. The result of the filing of the petition is an automatic entry of an order for relief. Such a petition may be filed under Chapter 7, Chapter 11, or Chapter 13.⁹¹ As in a voluntary case commenced under section 301, a petition in a joint case need not allege insolvency or inability to pay debts as they mature. Since a joint case is really a single case, although there are two petitioners and two debtors, only one filing fee is payable under section 1930(a). Moreover, the fee in a joint case may be paid in installments.⁹²

Prior to the promulgation of the Rules of Bankruptcy Procedure, a joint petition could be filed concerning only a partnership and one or more partners, but that authorization was withdrawn by the Rules of Bankruptcy Procedure.⁹³ The reason for the abolition of the joint petition in cases involving partnerships was that such petitions created more problems and difficulties than they solved. Section 302 does not preclude the possibility of the filing of a petition by a husband and wife who are partners, but if the partnership is to be a debtor in the case, the petition for the partnership must be filed pursuant to section 301. Moreover, a petition for relief under Chapter 13 cannot be filed for the partnership since only individuals are eligible for relief under that chapter.⁹⁴

Section 302(b) requires the court to determine, after the commencement of a joint case, "the extent, if any, to which the debtor's estate shall be consolidated." In such a case it is inferable that a single trustee will be appointed for the consolidated estates.⁹⁵ The consolidation of estates under

⁹¹ Section 109(b), (d), & (e). Section 109(a) also requires that both spouses must satisfy the jurisdictional requirement that the debtor reside or have a domicile, place of business, or property in the United States.

⁹² 28 U.S.C. § 1930(a)(last sentence).

⁹³ See the Advisory Committee's Notes to Rule 105 and 117(b) of the Rules of Bankruptcy Procedures. The Rules of Bankruptcy Procedure were promulgated by the Supreme Court in 1973-76 pursuant to 28 U.S.C. § 2075 (1976) and are published in the United States Code immediately following Title 11. The Rules remain effective under the Bankruptcy Code to the extent not inconsistent with the Code until repealed or superseded by rules promulgated pursuant to the congressional enabling act as amended by § 247 of the Bankruptcy Reform Act of 1978. The amendment eliminated a provision nullifying laws in conflict with rules promulgated under the enabling act. See text accompanying notes 39-40 *supra*.

⁹⁴ See note 81 *supra*.

⁹⁵ According to the legislative reports, § 302(b) "is designed mainly for ease of administration." HOUSE REPORT, *supra* note 17, at 321, [1978] U.S. CODE CONG. & AD. NEWS at 6277; SENATE REPORT, *supra* note 62, at 32, [1978] U.S. CODE CONG. & AD. NEWS at 5818. Administration of consolidated estates by more than one trustee is unlikely to make for ease of administration.

Section 701(a) requires the court in a liquidation case to appoint a disinterested person to serve as interim trustee in a case promptly after an order for relief is entered under Chapter 7, which means promptly after the petition is filed in a voluntary case. Section 15701, which applies in the 18 pilot project districts, requires the United States trustee to make the

section 302(b) involves more than the appointment or election of a single trustee, however, as the legislative reports indicated⁹⁶ that consolidation means the combination of the spouses' assets and liabilities "in a single pool" to pay creditors. The Reports indicated that the relevant factors in the court's determination whether to order consolidation "include the extent of jointly held property and the amount of jointly-owned debts."⁹⁷ Inferably, the key to the question of whether to order consolidation is "ease of administration."⁹⁸ Neither the statute nor the courts are free, however, to disregard constitutional limitations in ordering consolidation. If *H*, who has \$10,000 worth of nonexempt property and \$20,000 in liabilities, marries *W*, who has \$20,000 in assets and \$10,000 in liabilities, the creditors of *W* may object on constitutional grounds to the consolidation of *H*'s and *W*'s estates and distribution pro rata to the creditors of each.⁹⁹ Without acknowledging constitutional difficulties, the legislative reports conceded that the section is not a "license to consolidate in order to avoid other provisions of the title to the detriment of either the debtors or their creditors."¹⁰⁰ In any event, it appears that section 302 contemplates joint administration of the estates of the joint petitioners as a matter of procedure in all cases, and that Rule 117 of the Rules of Bankruptcy Procedure, which leaves joint administration of estates to the discretion of the court, is modified by the Code insofar as the estates of a husband and wife as joint petitioners are concerned.¹⁰¹

appointment. Since the filing of a petition by spouses commences a "joint case," these sections evidently contemplate the appointment of a single trustee. Query, however, whether, after the court has determined on consolidation of spouses' estates, the creditors of either spouse may not insist on a right to elect their own trustee? Cf. Rule 210(b) of the Rules of Bankruptcy Procedure. The court should in any event order the appointment, or authorize the election, of separate trustees for the two spouses' estates whenever warranted by an apparent conflict of interest.

⁹⁶ HOUSE REPORT, *supra* note 17, at 321, [1978] U.S. CODE CONG. & AD. NEWS at 6277; SENATE REPORT, *supra* note 62, at 32, [1978] U.S. CODE CONG. & AD. NEWS at 5818.

⁹⁷ *Id.*

⁹⁸ *Id.*

⁹⁹ See Seligson & Mandell, *Multi-Debtor Petition — Consolidation of Debtors and Due Process of Law*, 73 COM. L.J. 341 (1968). See also Berry, *Consolidation in Bankruptcy*, 50 AM. BANKR. L.J. 343, 357-62 (1976); Kennedy, *Insolvency and the Corporate Veil in the United States*, in PROCEEDINGS OF THE 8TH INTERNATIONAL SYMPOSIUM ON COMPARATIVE LAW 233, 248-55 (1971).

Professor Landers does not believe that the hypothetical case supposed in the text will arise very often. See Landers, *The Bankrupt's Spouse: The Forgotten Character in The Bankruptcy Drama*, 1974 UTAH L. REV. 709, 753 [hereinafter cited as Landers]. Professors Landers and Richard Posner have engaged in debate as to the appropriateness of consolidation of assets and liabilities of affiliated corporations. Landers, *A Unified Approach to Parent, Subsidiary, and Affiliate Questions in Bankruptcy*, 42 U. CHI. L. REV. 589, 628-51 (1975); Posner, *The Rights of Creditors of Affiliated Corporations*, 43 U. CHI. L. REV. 499, 518-26 (1976); Landers, *Another Word on Parents, Subsidiaries and Affiliates in Bankruptcy*, 43 U. CHI. L. REV. 527, 531, 538 (1976).

¹⁰⁰ See HOUSE REPORT, *supra* note 17, at 321, [1978] U.S. CODE CONG. & AD. NEWS at 6277, SENATE REPORT, *supra* note 62, at 32, [1978] U.S. CODE CONG. & AD. NEWS at 5818.

¹⁰¹ Only Rule 117(b)(1) appears to be inconsistent with the Code and then only when a

Section 302 appears to be a response to Professor Jonathan Landers' call for specific provisions in the bankruptcy law addressed to "the unique problems present in the husband-wife situation."¹⁰² Professor Landers argued that consolidation is desirable in nearly all husband-wife bankruptcies.¹⁰³ He noted that a husband and wife are a single entity for joint purchases and many other purposes and that purchases are made and debts are incurred by either or both without regard to whether the intended or actual beneficiary is the actual purchaser or both spouses. Commingling of assets and joint record-keeping are commonplace and facilitated by prevailing commercial practice, and creditors' expectations are predicated on an assumption of joint activity and joint liability.¹⁰⁴ Therefore, to resist consolidation Professor Landers would require creditors to show that the husband and wife kept their activities separate. Creditors would have to identify separately the assets each spouse brought to the marriage, the earnings or other income of each, and to trace these funds to personal expenditures by each, including those for support and investment. Professor Landers cited a number of cases approving consolidation in husband-wife bankruptcies.¹⁰⁵ He acknowledged that most of the cases arose out of efforts by the trustee to reach entireties property, particularly in the Fourth Circuit, where the courts are notoriously zealous to prevent spouses from exploiting the immunity of entireties property from levy by creditors of either spouse.¹⁰⁶ The Code takes a long step toward reducing the necessity for the trustee to rely on consolidation as a technique for reaching entireties property, by enabling the trustee to sell the debtor's interest in a tenancy by the entirety to the extent it is not exempt.¹⁰⁷ This reform, recommended by the Commission on the Bankruptcy Laws,¹⁰⁸ was truncated by a provision included in the exemption section of the Code permitting a debtor to invoke by election the immunity given his interest in an estate by the entirety by the nonbankruptcy law of his domicile.¹⁰⁹ The

husband and wife are joint petitioners under § 302. There is no indication that a husband and wife are required to file jointly.

¹⁰² See Landers, *supra* note 99, at 759.

¹⁰³ *Id.* at 754.

¹⁰⁴ *Id.* at 753.

¹⁰⁵ See *Roberts v. Henry V. Dick & Co.*, 275 F.2d 943 (4th Cir. 1960); *In re Pennell*, 15 F. Supp. 743 (W.D. Pa. 1935).

¹⁰⁶ See *In re Seats*, 538 F.2d 1176 (4th Cir. 1976); *Phillips v. Krakower*, 46 F.2d 764 (4th Cir. 1931).

¹⁰⁷ See §§ 363(h) & 522(b)(1).

¹⁰⁸ COMMISSION REPORT II, *supra* note 9, at 192.

¹⁰⁹ Section 522(b)(2)(B). The option to elect the law of one's domicile is available to any debtor who has had a domicile in a state affording such as immunity for the 180 days preceding the filing of the petition or for a longer portion of the 180-day period than in any other place. If the debtor opts for a federal package of exemption provided by § 522(d), the immunity of the interest in property held by the entirety under nonbankruptcy law is unavailable to the debtor. A state may, however, bar its domiciliaries from electing the federal exemption, by virtue of a curious provision added to § 522(b)(1) at a late stage in the congressional proceedings at the instance of Senator Wallop and others. 124 Cong. Rec.

cases that have allowed a trustee of both spouses' estates to sell their interests in nonexempt property held by the entirety¹¹⁰ are still viable under the Code, however, and constitute a shoal for counsel considering the possibility of filing a joint petition on behalf of debtors who are tenants by the entirety.¹¹¹

C. *Involuntary Cases-Section 303*

1. Amenable Debtors

An involuntary case may be commenced only under Chapter 7, where liquidation is the objective,¹¹² or Chapter 11, where reorganization is the objective.¹¹³ To be a debtor in an involuntary case under either of these chapters, a person must be eligible to be a voluntary petitioner under the chapter chosen. This requirement excludes a railroad under Chapter 7 but not under Chapter 11¹¹⁴ and also excludes under either chapter an insurance company or a financial institution of any of the kinds catalogued in subsections 109(b)(2) and (3) of Title 11.¹¹⁵ There are three further exclusions from amenability to an involuntary case, namely, a farmer, a corporation that is not a moneyed, business, or commercial corporation,¹¹⁶ and a foreign bank not engaged in the banking business in the United States. A foreign bank can be a debtor in an involuntary petition filed only under Chapter 7, and then only if a foreign proceeding by or against the debtor

S17406 (daily ed. Oct. 6, 1978)(remarks of Sen. Wallop). Four states have enacted such discriminatory legislation. Chapter 79-363, 1979 Fla. Laws (to be codified as FLA. STAT. § 222.20); Act No. 597, 1979 La. Sess. Law Serv. 1168 (West)(to be codified as LA. REV. STAT. § 3881 in (B)); Amended Substitute House Bill No. 674, 1979 Ohio Laws (to be codified as OHIO REV. CODE § 2329.662); House Bill 1940, 1979 Va. Acts (to be codified as VA. CODE § 34-3.1). The enactment of such legislation by the state of South Carolina was favored by Lacy, *South Carolina's Statutory Exemptions in Consumer Bankruptcy*, 30 S.C. L. REV. 643, 689-90, 701 (1979).

¹¹⁰ *In re Wetteroff*, 453 F.2d 544 (8th Cir.), cert. denied, 409 U.S. 934 (1972); *Reid v. Richardson*, 304 F.2d 351 (4th Cir. 1962), aff'g 198 F. Supp. 689 (W.D. Va. 1961); *In re Utz*, 7 F. Supp. 612 (D. Md. 1934); 4A COLLIER, *supra* note 45, ¶ 70.17[8], at 185-86.1 (1975); Craig, *An Analysis of Estates by the Entirety in Bankruptcy*, 48 AM. BANKR. L.J. 255, 267-72 (1974); Note, *The Effect of Bankruptcy on Estates by Entireties*, 89 U. PA. L. REV. 1073 (1941); 61 MICH. L. REV. 1351 (1963).

¹¹¹ After a tenant by the entirety has filed a voluntary petition, the other tenant may become an involuntary debtor under § 303. The fact that one spouse's bankruptcy case was closed before the other's case was commenced was no obstacle to consolidation and administration of the entireties property in *Reid v. Richardson*, 304 F.2d 351 (4th Cir. 1962). See Plumb, *The Recommendations of the Commission on the Bankruptcy Laws—Exempt and Immune Property*, 61 VA. L. REV. 1, 128-29 (1975). But cf. *Shipman v. Fitzpatrick*, 350 Mo. 118, 164 S.W.2d 912 (1942); *Dickey v. Thompson*, 323 Mo. 107, 18 S.W.2d 388 (1929) (criticized in 43 HARV. L. REV. 312 (1929)).

¹¹² See §§ 109(b), 303(a), & 704.

¹¹³ See §§ 109(d), 303(a), 1123, & 1172.

¹¹⁴ Sections 109(b)(1) & (d).

¹¹⁵ See notes 50-58 *supra*.

¹¹⁶ Section 303(a).

is already pending.¹¹⁷

The exclusion respecting a farmer is in one respect narrower and in another respect broader under the Code than under the Bankruptcy Act. Since a farmer had generally been held to qualify under the Bankruptcy Act if the major part of his income was derived from farming operations,¹¹⁸ the Code's requirement that more than 80% of a farmer's gross income be derived from a farming operation is a new limitation on the scope of the exclusion.¹¹⁹ Since a farmer may now be a partnership or corporation,¹²⁰ the immunity afforded this class of persons under section 303 is broader than under the Bankruptcy Act, which defined a 'farmer' as an individual¹²¹ and further excepted a farmer only if the farmer was a 'natural person'.¹²² Notwithstanding the interpretive difficulties presented, the courts protected farming partnerships as well as the farmer members thereof from involuntary proceedings under the Bankruptcy Act.¹²³ To this extent the new law codifies a result generally reached under the Bankruptcy Act. The immunizing of farming corporations from involuntary bankruptcy is, however, new law, since no case afforded any immunity to a corporate farmer under the Bankruptcy Act.¹²⁴

¹¹⁷ Section 303(k).

¹¹⁸ The courts have generally required a farmer who has two sources of income to derive more than half of his gross income from the farming operations. *See, e.g., In re Hinrichs*, 314 F.2d 384, 386 (7th Cir. 1963) (part-time farmer whose principal income came from commissions on sales held not a farmer); 1 COLLIER, *supra* note 45, ¶ 4.14[2]-[4] (1974). The definition of "farmer" in § 1(17) of the Bankruptcy Act specified that the "farmer" is "an individual personally engaged in farming or tillage of the soil." The definition further explained, however, that the term "shall include an individual personally engaged in dairy farming or in the production of poultry, livestock, or poultry or livestock products in their unmanufactured state, if the principal part of his income is derived from any one or more of such operations." It was not clear whether the clause regarding the "principal part of his income" applied to every farmer or only to one engaged in dairy farming or production of poultry or livestock or their products.

¹¹⁹ Section 101(17). The Code defines "farming operation" to include "farming, tillage of the soil, dairy farming, ranching, production or raising of crops, poultry, or livestock, and production of poultry or livestock products in an unmanufactured state." § 101(18). This definition is a paraphrase of the definition of "farmer" in § 1(17) of the Bankruptcy Act. The only new word appearing in the new definition is "ranching." That addition can hardly be thought to expand the term beyond its ordinary meaning.

¹²⁰ Section 101(30).

¹²¹ Section 1(17) of the Bankruptcy Act.

¹²² Section 4b of the Bankruptcy Act.

¹²³ *H.D. Still's Sons v. American Nat'l Bank*, 209 F. 749 (4th Cir. 1913), *cert. denied*, 232 U.S. 723 (1914). *See also In re Palma Bros.*, 8 F. Supp. 920, 922 (D. Nev. 1934).

¹²⁴ The enlargement of the immunity afforded farmers from involuntary bankruptcy to include corporations is not justified or explained in the legislative history. As H.R. 8200 first passed the House, it excluded from the definition of "farmer" any person receiving in excess of \$275,000 gross income from farming operations in the year before the filing of the petition. The HOUSE REPORT, *supra* note 17, at 322, [1978] U.S. CODE CONG. & AD. NEWS at 6278, explained that the definition of farmer, derived from the Small Business Act, was intended to encompass small farmers, not agribusinesses. The expansive approach taken in the enacted definition is to be contrasted with that animating the Review Committee for Article 9 of the

Another exclusion from amenability to an involuntary petition is "a corporation that is not a moneyed, business, or commercial corporation." This exclusion continues an immunity provided by section 4b of the Bankruptcy Act.¹²⁵ The Commission on Bankruptcy Laws had been persuaded

Uniform Commercial Code when it recommended deletion of the special exemption from notice-filing for purchase-money security interests in farm equipment:

While family farms still exist in this country, farms operating on a subsistence basis rather than operating as businesses must now be a small part of the total occupation of farming. Accordingly, the Committee proposes to adopt the theory expressed in Leavitt, 'A Bank Examiner Looks at Agricultural Lending,' 49 Fed. Res. Bull. 922, 926 (1963), namely, 'Farming has changed from "way of life" to a "way of business" and farm credit must be treated like business credit.'

Permanent Editorial Board for the Uniform Commercial Code, Preliminary Draft No. 2, p. 15 (1970).

The legislative reports explained that "[f]armers are excepted because of cyclical nature of their business. One drought year or one year of low prices, as a result of which a farmer is temporarily unable to pay his creditors, should not subject him to involuntary bankruptcy." HOUSE REPORT, *supra* note 17, at 322, [1978] U.S. CODE CONG. & AD. NEWS at 6278; SENATE REPORT, *supra* note 62, at 32, [1978] U.S. CODE CONG. & AD. NEWS at 5818. Many kinds of entrepreneurs that are equally subject to vicissitudes of nature and price fluctuations are not granted protection from their creditors seeking relief under the Bankruptcy Code.

¹²⁵ The expression "moneyed, business, or commercial corporations" made its first appearance in the Bankruptcy Act of 1867, Pub. L. No. 176, § 37, 14 Stat. 517, 535. The applicability of the law to corporations was limited to those that were "moneyed, business, or commercial corporations" in order to prevent its use "against religious and educational and eleemosynary corporations." Cong. Globe, 39th Cong., 2d Sess. 989 (1867). Many interpretations of the expression made it clear that the definition included railroads, banks, and insurance companies. Samuels, *supra* note 62, at 50. National banks were not included because the National Bank Act was held paramount. *In re Manufacturers' Nat'l Bank*, 16 F. Cas. 665 (N.D. Ill. 1873) (No. 9,051).

All corporations were excluded from voluntary bankruptcy by the Bankruptcy Act of 1898, but only national banks and banks incorporated under state and territorial laws were explicitly excluded from involuntary bankruptcy. Bankruptcy Act of 1898, Pub. L. No. 591, § 4(b), 30 Stat. 544, 547 (1898). Other corporations were made generally amenable to involuntary bankruptcy by language in § 4b of the Act subjecting to involuntary adjudication "any corporation engaged principally in manufacturing, trading, printing, publishing, or mercantile pursuits, owing debts to the amount of one thousand dollars or over." *Id.* After "mining" was added to the list of pursuits in 1903 by Act of Feb. 5, 1903, Pub. L. No. 62, § 3, section 4b of the Act was amended in 1910 to repeal the references to various kinds of pursuits and to subject "any moneyed, business, or commercial corporation, except a municipal, railroad, insurance, or banking corporation, owing . . . one thousand dollars or over" to involuntary bankruptcy. Act of June 25, 1910, Pub. L. No. 294, § 4, 36 Stat. 838, 839. Although the result was thought to be more formal than substantive, see H.R. REP. No. 511, 61st Cong., 2d Sess. 205-06 (1910), it is clear that a number of new enterprises were brought within the scope of involuntary proceedings, including, for example, public utilities other than railroads. *But see* H. BLACK, BANKRUPTCY 107 (2d ed. 1930) [hereinafter cited as BLACK]. Black doubted that public service corporations should be held amenable to involuntary bankruptcy because of "their close connection with the convenience of the public interest in their uninterrupted and efficient operation." *Id.* at 107.

Section 4b of the Bankruptcy Act contained two additional limitations on amenability to involuntary bankruptcy which disappear from the Code. A wage-earner was excluded, but the definition practically eliminated any beneficiary of this immunity by placing a ceiling of \$1,500 on his annual compensation. Bankruptcy Act § 1(32). The subdivision also included

to delete the exclusion on an assessment of the considerations set out in a careful study of this immunity in an article by Dean Sovern.¹²⁶ The legislative reports, by noting that the exclusion protects eleemosynary institutions, including churches, schools, charitable organizations, and foundations,¹²⁷ impliedly accept the rationale that it is better for these institutions' creditors to be left to the hazards of grab law than for the institutions to be subjected to liquidation or reorganization under the bankruptcy laws, unless and until the institutions' managers opt for relief under Title 11. The protection of such a corporation from an involuntary reorganization under Chapter 11 is perhaps more easily justified, or at least more easily understood, than immunity from involuntary liquidation. However, if a reorganization plan could be formulated that meets all the standards required for confirmation by section 1129,¹²⁸ no readily apparent public policy or interest would be trammelled.¹²⁹

Since the classification of a corporation as "moneyed, business, or commercial" for the purposes of section 303(a) implements or vindicates no state policy,¹³⁰ there is no reason to consult state law in determining whether a particular corporation is amenable to involuntary administration under the bankruptcy laws. Whatever policy considerations underlie the limitation imposed by the phrase,¹³¹ the phrase should be given a

an ambiguous limitation applicable to a debtor owing debts in the amount of \$1,000 or more. It was not clear from the statutory language whether the limitation required every person against whom an involuntary petition was filed to owe \$1,000, or whether it applied only to a moneyed, business, or commercial corporation. Conceivably, the limitation operated to restrict the number of corporations immunized from involuntary bankruptcy. The Commission recommended deletion of the immunity for a wage-earner as meaningless and elimination of any differentiation of corporations based on the amount of their indebtedness or their character as moneyed, business, or commercial. COMMISSION REPORT I, *supra* note 1, at 15. Section 303(a) of the Bankruptcy Code preserves the latter distinction, but the other two recommendations of the Commission were followed.

¹²⁶ Sovern, *supra* note 54, at 231-43 (1957).

¹²⁷ HOUSE REPORT, *supra* note 17, at 322, [1978] U.S. CODE CONG. & AD. NEWS at 6228; SENATE REPORT, *supra* note 62, at 32, [1978] U.S. CODE CONG. & AD. NEWS at 5818.

¹²⁸ The owners and managers of a corporation that is not moneyed, business, or commercial cannot be compelled to continue the activities of the corporation against their will. This potential problem, however, is presented by any involuntary petition seeking relief under Chapter 11. Unwilling management should be displaced by a disinterested trustee if an involuntary case under Chapter 11 is commenced by a petition that is sufficient in all respects under section 303 and the interests of creditors and the debtor, as distinguished from the owners and the managers, are better served by a continuation rather than a dismissal of the case.

¹²⁹ Cf. Sovern, *supra* note 54, at 239.

¹³⁰ As Dean Sovern noted, states do not usually have any classification of a corporation as moneyed, business, or commercial. *Id.* at 231.

¹³¹ Dean Sovern surmised that:

Congress adopted this involuntary bankruptcy exclusion in 1910 . . . because it thought that corporations which were unconcerned with money, business or commerce should not have their laudable activities disrupted by liquidation at the instance of pestiferous creditors. Perhaps, too, the members of Congress felt that a remedy once thought of as the special province of blackguards, and occasionally

uniform construction across the country. Although "moneyed" originally had reference to banking and other financial corporations,¹³² the three words, "moneyed," "business," and "commercial" have generally not been distinguished in the construction of the language of section 4b of the Bankruptcy Act.¹³³ The words generally have been held not to afford immunity to all "nonprofit" corporations,¹³⁴ particularly cooperatives organized to market produce.¹³⁵

There has been no doubt about the Congressional purpose in the Bankruptcy Act to exclude religious, educational, and charitable or eleemosynary corporations from involuntary bankruptcy,¹³⁶ and the Bankruptcy Code plainly extends the immunity of these organizations. There is less certainty about fraternal and social organizations,¹³⁷ and there have been divergent rulings in cases involving organizations that have engaged in money-making activities for the purpose of financing their noncommercial purposes.¹³⁸ Congress did not manifest any intent in the Bankruptcy Code to extend or to expand the scope of the immunity covering corporations that are not moneyed, business, or commercial.

As noted above,¹³⁹ a foreign bank that is eligible for relief as a voluntary debtor under Title 11 is nevertheless afforded a double immunity by section 303(k): (1) Such a bank cannot be subjected to an involuntary reorg-

still so regarded, ought not to be inflicted on such highminded enterprises. In short, Congress' purpose was . . . to give those corporations a dispensation from an unpleasant law designed for the self-seeking world of commerce and business.

Id. at 232.

¹³² See generally BLACK, *supra* note 125.

¹³³ *Id.*

¹³⁴ See, e.g., *Missco Homestead Ass'n v. United States*, 185 F.2d 280 (8th Cir. 1950) (cooperative society formed under state statutes governing "benevolent corporations" for rehabilitation and relief of needy farm families nevertheless held to be subject to involuntary bankruptcy). *But cf.* *Hoile v. Unity Life Ins. Co.*, 136 F.2d 133 (4th Cir. 1943) (mutual benefit society held not a moneyed, business or commercial corporation because not organized for profit). The *Missco* case appears not to be overruled by §§ 109(b)(2) and 303(a). See text accompanying notes 56 & 115 *supra*.

¹³⁵ See, e.g., *In re Wisconsin Coop. Milk Pool*, 119 F.2d 999 (7th Cir.), *cert. denied*, 314 U.S. 655 (1941); *Schuster v. Ohio Farmers' Coop. Milk Ass'n*, 61 F.2d 337 (6th Cir. 1932); *In re South Shore Coop. Ass'n*, 4 F. Supp. 772 (W.D.N.Y. 1933).

¹³⁶ See *Govern*, *supra* note 54, at 233.

¹³⁷ Compare *In re William McKinley Lodge*, 4 F. Supp. 280, 283 (S.D.N.Y. 1933) (Masonic lodge held subject to involuntary bankruptcy because of income received from renting lodge rooms to the general public) with *In re Elmsford Country Club*, 50 F.2d 238, 241 (S.D. N.Y. 1931) (corporation formed to operate a golf course for the pleasure of its members held not to be subject to voluntary bankruptcy). Such corporations are not within the categories of "churches, schools, and charitable organizations," to which the legislative history refers. HOUSE REPORT, *supra* note 17, at 332, [1978] U.S. CODE CONG. & AD. NEWS at 6278.

¹³⁸ Compare *In re William McKinley Lodge*, 4 F. Supp. 280 (S.D.N.Y. 1933) with *In re Michigan Sanitarium & Benevolent Ass'n*, 20 F. Supp. 979 (E.D. Mich. 1937), *appeal dismissed*, 96 F.2d 1019 (6th Cir. 1938) (payments to hospital for services rendered to patients able to pay held not to subject the hospital to involuntary bankruptcy, since such payments simply enabled the hospital to carry out charitable activities).

¹³⁹ See text accompanying note 117 *supra*.

anization petition and (2) an involuntary petition for liquidation can be filed only if a foreign proceeding concerning the debtor is pending. The latter immunity was recommended by the National Bankruptcy Conference in recognition of the potentially dire consequences for the foreign bank in its own country that may be triggered by an involuntary petition in this country.¹⁴⁰ With respect to the first immunity, no objection is likely to be raised against a bar imposed on an involuntary petition for reorganization of a foreign bank. A legitimate inquiry, however, is why either of these immunities should be restricted to an involuntary case against a foreign bank. Since section 109(b) quite pointedly and probably unnecessarily excludes from the benefits and burdens of the Bankruptcy Code both domestic and foreign savings and cooperative banks when they are doing business in the United States, the reference in section 303(k) to only a foreign bank must mean that no special immunity against any variety of involuntary petition under Title 11 attaches to any of the eligible foreign financial institutions other than a "plain and ordinary" foreign bank or to any foreign insurance company. The narrowness of section 303(k) has been criticized,¹⁴¹ but the burden of justifying additional or broader immunities is on the proponent. The risk of a run on any foreign financial institution other than a conventional bank or on an insurance company, with the irreversible consequences that attend a bank run, are not likely to be triggered by an involuntary petition in this country. In any event, the Code contains ample authority for the bankruptcy court to dismiss or suspend a case filed against a foreign debtor of any kind when the interests of the debtor and the creditors would be better served.¹⁴²

¹⁴⁰ See *Hearings, supra* note 13, Appendix, Ser. No. 27, at 350-51. See also HOUSE REPORT, *supra* note 17, at 324, [1978] U.S. CODE CONG. & AD. NEWS at 6280; SENATE REPORT, *supra* note 62, at 35, [1978] U.S. CODE CONG. & AD. NEWS at 5818. The REPORT ON INSURANCE COMPANIES, *supra* note 61, at 27-29, pointed out that the dependence of banks upon liabilities withdrawable on demand or on short notice makes it imperative to avoid situations which undermine banks' ability to attract funds. The hazard pointed out by the Committee was aggravated under the version of the Bankruptcy Act proposed by the Commission on Bankruptcy Laws by the fact that a single petitioner could file an involuntary petition. COMMISSION REPORT II, *supra* note 9, § 4-205(a), at 74.

A confusing statement in the House and Senate Reports declared that "[a]n involuntary case commenced under this subsection [k] gives the foreign representative an alternative to commencing a case ancillary to a foreign proceeding under section 304." HOUSE REPORT, *supra* note 17, at 324, [1978] U.S. CODE CONG. & AD. NEWS at 6280; SENATE REPORT, *supra* note 62, at 35, [1978] U.S. CODE CONG. & AD. NEWS at 5818. Sections 301 and 303 give the foreign representative several alternatives to proceeding under section 304, but subsection 303(k) creates no alternative; it limits what would otherwise be available under other subsections of section 303.

¹⁴¹ Samuels, *supra* note 62, at 92; cf. Howard, *United States Bankruptcy Jurisdiction Over Unregulated Foreign Banks*, 17 HAW. INT'L L. REV. 359, 394 (1976) (criticizing the section for disabling creditors of a foreign bank to obtain bankruptcy relief when it would be equitable to grant it).

¹⁴² Section 305; see text accompanying notes 227-34 *infra*. Although § 305 requires notice and hearing, it is unlikely that the limitation imposed by § 303(k) on the filing of a petition against a foreign bank will be deemed self-enforcing. It may be easier to establish a right to

2. Qualifications of Petitioning Creditors

Section 303(b) prescribes the qualifications for petitioners in most involuntary cases. Paragraph (1), requiring three or more petitioners¹⁴³ holding unsecured claims of \$5,000 or more, is the usually applicable provision.¹⁴⁴ The claims must not be contingent, but there is no requirement in the statute that they be liquidated.¹⁴⁵ The petitioning creditors¹⁴⁶ may be

recover damages for bad faith in filing a petition in violation of § 303(k) than one dismissible under § 305, but that seems an insufficient reason for broadening § 303(k).

¹⁴³ The Commission on Bankruptcy Laws recommended that one petitioner with a claim of at least \$10,000 in a reorganization case be permitted to file an involuntary petition. COMMISSION REPORT II, *supra* note 9, § 4-205. The Commission's recommendation was consistent with its purpose to facilitate involuntary proceedings against a debtor destined for relief under the bankruptcy laws and generally consistent with bankruptcy laws in other countries in according the right to file a petition in bankruptcy to a single petitioner. See COMMISSION REPORT I, *supra* note 1, at 225 n. 44; *Hearings, supra* note 13, at 1445 (statement of Professor Kurt H. Nadelmann); EUROPEAN BANKRUPTCY LAWS at 57, 70, 77, 92, 123, 142 (I. Ross ed. 1974) (discussing the laws of Austria, Belgium, England, France, Germany, and Sweden).

The notion that a single petitioner should have the option to precipitate involuntary proceedings under the bankruptcy laws was generally opposed by critics in hearings on the Commission's and Bankruptcy Judges' bills. These critics thought it would tend to jeopardize a privately negotiated settlement outside bankruptcy, encourage a demand for a preference as a price for not filing an involuntary petition, and facilitate the design of a competitor to acquire a business rival by filing an involuntary petition against him. See *Hearings, supra* note 13, at 325 (testimony of Daniel Cowans, former bankruptcy judge from California); 976 (testimony of Bernard Shapiro for the National Bankruptcy Conference); 1604-05, and 1631 (statement and testimony of John J. Creedon for the American Life Insurance Ass'n); 1657, 1663 (statement and testimony of L.E. Creel III for the Dallas Bar Ass'n); 1670, 1672, 1678 (statement of K. Richard Kaufman for Credit Managers Ass'n of Southern California); 1748, 1757 (statement and testimony of Robert J. Grimmig for American Bankers Ass'n); 1870 (statement of American Ass'n of Equipment Lessors); Appendix, Ser. No. 27, at 351 (draft of proposed amendments by National Bankruptcy Conference).

¹⁴⁴ The minimum amount required to be held by petitioning creditors has been increased from \$500 in straight bankruptcy under the Bankruptcy Act (§ 59b) to the amount heretofore required of petitioning creditors in corporate reorganization under Chapter X (§ 126). See § 303(b)(1). The minimum amount is made uniform "in order that there not be an artificial difference between the two chapters [*i.e.*, Chapters 7 and 11]." HOUSE REPORT, *supra* note 17, at 322, [1978] U.S. CODE CONG. & AD. NEWS at 6278. Petitioners in railroad reorganization cases have been required by § 77(a) of the Bankruptcy Act to have claims aggregating not less than 5% of all the indebtedness of the railroad corporation. As under Chapter X (§ 126), but not in straight bankruptcy or railroad reorganization under the Bankruptcy Act, an indenture trustee representing the holder of a qualified claim may be a petitioner on an involuntary petition. § 303(b)(1).

¹⁴⁵ Query, whether Rules of Bankruptcy Procedure may require, as does § 59b of the Bankruptcy Act, that the claims of petitioners be amenable to liquidation without unreasonably delaying the administration of the estate? Rules 104 and 10-105 of the Rules of Bankruptcy Procedure, which have governed involuntary petitions, include no reference to the nature of the claims of petitioning creditors.

The disqualification of a petitioning creditor for participation in the act of bankruptcy alleged, imposed by Rule 104(b), is no longer applicable by virtue of the abolition of acts of bankruptcy. See text accompanying notes 165-85 *infra*.

¹⁴⁶ While § 303(b) does not identify "creditors" as qualified petitioners, the reference in the text to "petitioning creditors" is accurate and appropriate. Paragraphs (1) and (2) of

partially secured, so long as the petitioners' aggregated unsecured claims amount to at least \$5,000.

Paragraph (2) of section 303(b) preserves the rule of the Bankruptcy Act requiring only one petitioner if there are fewer than twelve creditors of the debtor.¹⁴⁷ In computing the number of creditors, employees, insiders, and transferees of voidable transfers are excluded.¹⁴⁸ An insider is defined in section 101(25) and includes any of 18 categories of persons. The exclusions are comparable to those provided by section 59e of the Bankruptcy Act.¹⁴⁹

Rules 104(d) and 10-105(b) disqualify any person from acting as petitioner who transferred or acquired a claim for the purpose of commencing a case. Whether this disqualification remains effective depends on the answer to a question that must be frequently considered and answered by the draftsmen of the rules under section 2075: Is the Code's omission of a procedural limitation embodied in the Rules inconsistent with its continuing applicability?¹⁵⁰ The guidelines distributed by the Co-reporters for the Advisory Committee on Bankruptcy Rules assumes that such a limitation may still be imposed and applied.¹⁵¹ While the Code's silence may imply a negation of particular Rules of Procedure, the drawing of a general and automatic implication of negation from silence would tend to restrict unduly the ability of the Supreme Court to enforce procedural safeguards found necessary or desirable in the light of experience.

section 303(b) actually authorize only an entity that is a holder of a claim against the debtor to file or join in filing an involuntary case. A "claim" is defined in § 101(4) to include a right to payment or a right to an equitable remedy for breach of performance even though the breach does not give rise to a right of payment. A "creditor" is defined in § 101(9) as an entity having a claim against the debtor or the estate.

¹⁴⁷ Section 303(b)(2). The sole petitioner under the Code, however, must have an unsecured, noncontingent claim of at least \$5000, ten times the minimum required by § 59b of the Bankruptcy Act.

¹⁴⁸ Transfers such as statutory liens, preferences, fraudulent transfers, postpetition transfers, and liens securing fines, penalties, and multiple, exemplary, or punitive damages are those voidable by the trustee as a hypothetical creditor or purchaser or as a successor to an actual creditor of the estate. It is conceivable but unlikely that a petitioning creditor may be disqualified on account of having received a postpetition transfer.

¹⁴⁹ One ground of exclusion no longer recognized is that involving creditors who have participated in the act of bankruptcy charged in the petition. *But see* R. BANKR. P. 104(b). Since there is no longer any act of bankruptcy, this ground of exclusion is no longer appropriate.

¹⁵⁰ The question whether the Code's failure to mention a procedural limitation of the Rules nullifies such a limitation assumes that Rules 104(d) and 10-105(b) are procedural and thus fall within the ambit of the rule-making power granted by Congress. As pointed out in the Advisory Committee's Note to Rule 104(d), the latter provision was derived from General Order 5(2), which had originally been promulgated by the Supreme Court pursuant to its narrow authority to prescribe interstitial rules and forms of procedure. Neither General Order 5(2) nor the Rule of Procedure disqualifying transferors and transferees of claims from acting as petitioners have been challenged as in excess of the Court's rule-making power.

¹⁵¹ See Interim Rule 1003(b), derived from R. BANKR. P. 104(d) and 10-104(d).

3. Partnership Cases

Paragraph (3) of section 303(b)(3) contains additional options for the commencement of an involuntary case against a partnership. These provisions are in no way a limitation on the availability of voluntary relief on a petition against the partnership by creditors under paragraphs (1) and (2) of section 303(b). Furthermore, the additional options provided by section 303(b)(3) are derived from prior bankruptcy law.¹⁵²

The first option provided by section 303(b)(3) has sometimes been referred to as the hybrid petition in that it authorizes a petition to be filed against a partnership by one or more but fewer than all of the general partners. This option has been called hybrid because it is voluntary so far as the petitioning partner is concerned but involuntary with respect to the other partners. Unlike a creditors' petition, the hybrid petition under the Bankruptcy Act did not need to allege the commission of an act of bankruptcy and thus sufficed if it alleged the insolvency of the partnership.¹⁵³ An act of bankruptcy is not required to be alleged in any involuntary petition under the Code, but the allegations and proof required for a hybrid petition under the new law are the same as required for a creditors' petition.¹⁵⁴

A second option for a partnership debtor is available when relief has been ordered with respect to all of the general partners in a partnership. In such a case a general partner, the trustee of a general partner, or a creditor of the partnership may file a petition to seek relief.¹⁵⁵ While this provision is comparable to an option provided in section 5i of the Bankruptcy Act, supplemented and implemented by Rule 105(d) of the Rules of Bankruptcy Procedure, the new law differs in that it requires a petitioner to allege and prove the same grounds for requesting relief as are imposed on any other petitioner. When all the general partners have been adjudged bankrupt, the Bankruptcy Act and the Rules of Bankruptcy Procedure have required no allegation and no showing other than the partners' adjudications in order to obtain an adjudication of the partnership.

4. Cases Against Debtors in Foreign Proceedings

A fourth kind of involuntary case is one that may be commenced by a foreign representative of an estate that is undergoing administration in a

¹⁵² Section 303(b)(A) is derived from the first sentence and the proviso of § 5b of the Bankruptcy Act. Section 303(b)(3)(B) is derived from the first sentence of § 5i of the Act.

¹⁵³ Bankruptcy Act § 5b (proviso). Since a partnership cannot be insolvent if any partner is solvent, this provision did not enable a solvent member of a failing firm to put the partnership into bankruptcy. 1A COLLIER, *supra* note 45, at 704 (1978).

¹⁵⁴ Since insolvency need not be alleged or established under § 303 of the new law, a solvent partner of such a firm may precipitate any involuntary case concerning the partnership under the new law. The partner must nevertheless allege and, if the petition is contested, show the elements specified in 303(h).

¹⁵⁵ Section 303(b)(3)(B).

foreign proceeding.¹⁵⁶ The standing accorded a foreign representative by section 303(b)(4) in no way diminishes the eligibility of a debtor in a foreign proceeding to file a voluntary petition under section 301, or the debtor's amenability to an involuntary petition filed by creditors or other parties in interest under paragraph (1), (2), or (3) of section 303(b).¹⁵⁷ The availability of relief to other petitioners under the Bankruptcy Code is no reason for withholding relief from the foreign representative, who is the logical party in interest to seek such relief if it is needed or appropriate.¹⁵⁸ As previously noted,¹⁵⁹ there is a special limitation on the availability of an involuntary petition against a foreign bank not engaged in doing busi-

¹⁵⁶ Section 303(b)(4). A "foreign proceeding" is defined as a proceeding, whether judicial or administrative and whether or not under bankruptcy law, in a foreign country in which the debtor's domicile, residence, principal place of business, or principal assets were located at the commencement of such proceeding, for the purpose of liquidating an estate, adjusting debts by composition, extension, or discharge, or effecting a reorganization. § 101(19).

A "foreign representative" is defined in § 101(20) as a "duly selected trustee, administrator, or other representative of an estate in a foreign proceeding."

¹⁵⁷ The debtor in a foreign proceeding is eligible to file a voluntary petition if he can satisfy the requisites of § 109(a) by having a domicile, place of business, or property in the United States. These requisites also apply to a petition filed against such a debtor under § 303, including one filed by a foreign representative under § 303(b)(4). A petition filed concerning a debtor in a foreign proceeding under § 301, 302, or 303, including 303(b)(4), contemplates administration of the debtor's estate in the same manner as any other estate that is administered under Title 11, but there are special provisions that may apply to such a case. Thus § 305(a)(2) recognizes that suspension or dismissal may be particularly appropriate in such a case. Section 508(a) provides a special rule for effecting equality of distribution when a debtor's estate is being administered in a foreign proceeding as well as under Title 11.

Section 304, discussed in the text accompanying notes 214-26 *infra*, provides for certain ancillary relief on a petition filed by a foreign representative, but such relief is less than or at least different from that obtainable under §§ 301-303.

¹⁵⁸ See *Hearings, supra* note 13, at 1510, 1516 (statement of Professor Stefan A. Riesenfeld); Stevens, *The Interpenetration of Foreign Bankruptcy Laws in Domestic Proceedings Under H.R. 8200*, 52 AM. BANKR. L.J. 61, 66-67, 75 (1978) [hereinafter cited as Stevens]. But see *Hearings, supra* note 13, at 1443, 1449, 1451, 1508 (statement and testimony of Professor Kurt H. Nadelmann).

If § 303(b)(4) had been in effect, the German liquidator of the Herstatt Bank could have filed a timely petition to obtain an avoidance of liens of attaching creditors against funds of the bank held in New York. See Stevens, *supra*, at 64. See also note 221 *infra*. While that option might have been available to the liquidator under the Bankruptcy Act, there was no explicit recognition of his standing in the Act. Moreover, there was doubt as to the amenability to bankruptcy of the bank, a *Kommanditgesellschaft auf Aktien*, which in some respects is like a partnership and in some respects like a corporation. Finally the liquidator was uncertain as to his vulnerability to litigation and binding adverse judgments in American courts. See note 225 *infra*; see also Nadelmann, *Rehabilitating International Bankruptcy Law: Lessons Taught by Herstatt and Company*, 52 N.Y.U. L. Rev. 1, 13 (1977) [hereinafter cited as Nadelmann]. Under the circumstances the attaching creditors were able to obtain an advantageous settlement and dismissal of an involuntary bankruptcy petition filed against the Bank. Becker, *International Insolvency: The Case of Herstatt*, 62 A.B.A.J. 1290, 1294-95 (1976); Samuels, *supra* note 62, at 91 n. 180; cf. Nadelmann, *supra* at 9-10.

¹⁵⁹ See text accompanying notes 139-42 *supra*.

ness in the United States, because such a case may be commenced only if a foreign proceeding concerning the bank is pending in another country.¹⁶⁰

5. Grounds for Involuntary Relief

The most noteworthy change accomplished by the Bankruptcy Code within the scope of this article is the abolition of the acts of bankruptcy. This is a reform called for over forty years ago¹⁶¹ and vigorously supported by Professor James MacLachlan in his hornbook on bankruptcy published over twenty years ago.¹⁶² The National Bankruptcy Conference was persuaded by Professor MacLachlan's argument of the soundness of this reform,¹⁶³ but the Conference did not concur in his belief that the reform should be coupled with a substantial stiffening of other requirements prescribed for the filing of an involuntary petition.¹⁶⁴ Consistently with its view that involuntary petitions ought to be easier to file and to sustain against contesting debtors, the Commission on Bankruptcy Laws recommended elimination of the concept of acts of bankruptcy along with reduction of the required number of petitioners to one.¹⁶⁵ Although Congress rejected the latter recommendation, it adopted the former.¹⁶⁶

The Code does not particularize what shall be contained in an involuntary petition. Subsection (h) of section 303 provides that if the petition is not controverted timely, the court shall order relief against the debtor in an involuntary case. While the statute does not particularize the elements

¹⁶⁰ Section 303(k).

¹⁶¹ Treiman, *Acts of Bankruptcy: A Medieval Concept in Modern Bankruptcy Law*, 52 HARV. L. REV. 189 (1938) [hereinafter cited as Treiman].

¹⁶² J. MACLACHLAN, BANKRUPTCY 56-64 (1956) [hereinafter cited as MACLACHLAN]. See also Herzog, *Bankruptcy Tomorrow*, 45 AM. BANKR. L. J. 57, 59 (1971); Seligson, *Major Problems for Consideration by the Commission on the Bankruptcy Laws of the United States*, 45 AM. BANKR. L. J. 73, 98-100 (1971); Note, "Acts of Bankruptcy" in Perspective, 67 HARV. L. REV. 503 (1954).

¹⁶³ National Bankruptcy Conference, Summary of Proceedings of the 1957 Annual Meeting, Res. No. 46, and Summary of Proceedings of the 1958 Annual Meeting, Res. No. 30.

¹⁶⁴ The Conference disagreed with Professor MacLachlan's insistence on requiring a substantial percentage of the debtor's creditors to join in an involuntary petition. See MACLACHLAN, *supra* note 162, § 71. The result of the Conference debate on the appropriate number of petitioning creditors was withdrawal by the Conference in favor of its previously adopted resolutions favoring abolition of acts of bankruptcy. Summary of Proceedings of the 1958 Ann. Meeting, Res. No. 30.

¹⁶⁵ See text accompanying note 12 *supra*.

¹⁶⁶ Section 303(h). It has been argued that acts of bankruptcy were not abolished by the Code, since the second statutory ground for involuntary petition, *see* text accompanying notes 175-77 *infra*, includes an event that would have constituted the fourth act of bankruptcy and an event that comes close to the fifth act of bankruptcy. The term "act of bankruptcy" has nevertheless disappeared from the Bankruptcy Code, and the objectionable features of the concept have been eliminated. See HOUSE REPORT, *supra* note 17, at 323, [1978] U.S. CODE CONG. & AD. NEWS at 6280 ("The second test . . . is not a partial reenactment of acts of bankruptcy"); SENATE REPORT, *supra* note 62, at 34, [1978] U.S. CODE CONG. & AD. NEWS at 5820.

of a prima facie case, subsection (h) requires the court to order relief against the debtor in an involuntary case only after trial if the petition is contested. The entry of an order for relief against the debtor in an involuntary case is authorized only if (1) the debtor is generally not paying its debts as they become due, or (2) within 120 days before the filing of the petition, a custodian has been appointed or authorized to take charge of substantially all of the property of the debtor.

The first alternative of subsection (h) is derived from the Commission's recommendation that a general failure to pay debts as they become due should be a ground for relief on an involuntary petition.¹⁶⁷ As an alternative ground for relief the Commission had also recommended that "the debtor will be generally unable to pay his current liabilities as they become due."¹⁶⁸ Originally this alternative was favored by the House Judiciary Committee and included in the version of H.R. 8200 first passed by the House.¹⁶⁹ The Senate bill, S. 2266, had prescribed as the first ground for involuntary relief that "the debtor is generally unable to pay or *has failed* to pay a major portion of his debts as such debts *became* due." In opting for general nonpayment of debts as they become due rather than on inability to pay them, Congress seems to have rejected the traditional formulation of the equity definition of insolvency as a ground for involuntary administration.¹⁷⁰ Inability to pay is thus no defense to a petition under

¹⁶⁷ COMMISSION REPORT II, *supra* note 9, § 4-205(c)(2).

¹⁶⁸ *Id.* § 4-205(c)(1).

¹⁶⁹ The House Report accompanying H.R. 8200 pointed out that the first ground in § 303(h) adopted the equity insolvency test which "has been in equity jurisprudence for hundreds of years, and though it is new in the bankruptcy context (except in Chapter X), the bankruptcy courts should have no difficulty in applying it." HOUSE REPORT, *supra* note 17, at 323, [1978] U.S. CODE CONG. & AD. NEWS at 6280. The Report understated the extent to which the equity insolvency test has been relevant in bankruptcy. The insolvency test has been an alternative requirement when the fifth act of bankruptcy has been relied on by petitioning creditors seeking involuntary adjudication. Bankruptcy Act § 3a(5). A voluntary petition filed under §§ 77(a), 84, 130(1), 323, 423, or 623 had to allege that the debtor was insolvent or unable to pay his debts as they mature. Likewise an involuntary petition under § 77a or 130(1) was required to allege insolvency or inability to pay debts as they mature.

Professor James MacLachlan recommended that any debtor otherwise amenable to bankruptcy should be subject to an adjudication as bankrupt if he is in fact unable to pay his debts as they mature. MACLACHLAN, *supra* note 162, at 63-64, 436. Professor MacLachlan suggested that the ultimate fact of such inability should be conclusively evidenced by proof that "the debtor has failed to pay or secure the payment of a final judgment rendered against him at least one month and not exceeding five months before the petition." Prima facie evidence of such inability would be that within four months before the petition, the debtor has stopped making payments in the due course of business. *Id.* at 436.

¹⁷⁰ See note 169 *supra*. The managers of the final version of H.R. 8200 that reconciled the differences with S.2266 simply observed that § 303(h)(1) was a compromise of the standards found in the House and Senate versions. Congressional Record, *supra* note 29, at H11091 and S17407. It was suggested in the SENATE REPORT, *supra* note 62, at 34, [1978] U.S. CODE CONG. & AD. NEWS at 5820, that the test of failure to pay a major portion of his debts as they become due was a variation of the equity insolvency test.

U.C.C. § 1-201(23) defines an "insolvent" person as one "who either has ceased to pay his debts in the ordinary course of business or cannot pay his debts as they become due or is

section 303(h)(1) if the debtor is avoiding or generally neglecting payment of his debts. The Code focuses on the debtor's behavior in respect to his debts rather than his financial condition and has thereby eliminated the need for and the relevance of an inquiry into the latter when an involuntary petition is contested.¹⁷¹

The Commission acknowledged that the scope and meaning of "generally failed" must be left to the courts. The Commission felt that the courts must find "more than a past failure to pay only a few of his debts," and that the court must "consider both number and amount" of debts in determining whether a failure is general.¹⁷² The legislative reports accompanying S. 2266 and the Code as enacted do not elaborate on what may constitute proof of the existence of this first ground, but Congress did not require a showing that the debtor has failed to pay a major portion of his debts.¹⁷³ With respect to the second ground for an involuntary petition,

insolvent within the meaning of the federal bankruptcy law." The Official Comment adds nothing by way of explanation of this definition except to say that the three tests of insolvency are alternatives "and must be approached from a commercial standpoint." The definition is not discussed in any of the literature generated by the Code.

It was held in *In re Creative Buildings, Inc.*, 498 F.2d 1, 2-3 (7th Cir. 1974), that return of two checks, one for \$47,859.23 and another for \$9,900.76, for insufficient funds did not require a finding that the drawer was insolvent within the meaning of U.C.C. § 1-201(23). The first check was paid when re-presented. The court acknowledged that "[t]he issuance of the NSF checks may indicate an impecunious status and be notice that the drawer may be insolvent." The question of insolvency arose in the case when the payee of the check, invoking U.C.C. § 2-702, sought to reclaim goods shipped to the drawer.

¹⁷¹ The concept of the acts of bankruptcy was criticized because the concept ignored the debtor's financial condition at the date of filing the petition. The statutory focus of § 303(h)(1) is on what the debtor is doing in respect to his debts at the very moment of the filing of the petition. If, as Professor MacLachlan suggested, MACLACHLAN, *supra* note 162, at 436, nonpayment of indebtedness is evidence of inability to pay debts, the Code's reliance on general nonpayment of debts as they mature is a way of establishing the debtor's current financial condition without requiring the creditors to engage in discovery of evidence to prove insolvency. Whatever the difficulties posed by the vagueness of "generally not paying" debts as they become due, the scope and nature of the factual inquiry entailed by the new test should be less burdensome on both the petitioners and the debtor. Rule 114 authorizing examination of the bankrupt in respect to insolvency or inability to pay debts as they mature, is no longer applicable, but discovery procedures available under Rule 205 should remain available to petitioning creditors. In addition, the Co-reporters for the Advisory Committee on Bankruptcy Rules have suggested an adaptation of Rule 114 as a new Rule 1008. The suggested rule requires the debtor to appear with his books, papers, and accounts to submit to an examination if he denies an allegation of an involuntary petition that he is generally not paying his debts as they become due.

¹⁷² COMMISSION REPORT II, *supra* note 9, at 75.

¹⁷³ Pointing out that "[f]rom the creditor's standpoint, the word 'generally' could be troublesome," John J. Creedon for the American Life Insurance Association recommended that either a general failure or a failure to pay a major portion of his debts be a ground for an involuntary petition. *Hearings, supra* note 13, at 1605. Mr. Creedon suggested that although the debtor might be in default to two or three creditors holding 90% of a debtor's indebtedness, the debtor's nondelinquency in respect to a thousand other small creditors holding small claims might insulate him from involuntary proceedings. Inferably Congress concluded that a debtor in such a situation would be unlikely to prevail on a contest of an

namely, that a custodian has been appointed to take charge of the property of the debtor, the word "custodian" is defined in section 101(10) to mean a trustee, receiver, or agent appointed or authorized to take charge of the debtor's property, or an assignee under general assignment for the benefit of creditors. The receiver or trustee must be one that is either appointed in a case or proceedings instituted under some law other than Title 11¹⁷⁴ or one that has been appointed or authorized to take charge of the property for the purpose of enforcing a lien or for the purpose of effecting general

involuntary petition and that the statutory language already covered a situation such as that suggested by Mr. Creedon.

Experience under the Canadian Bankruptcy Act may be instructive. Since 1922 when it was introduced into the Canadian law, 12-13 Geo. V, c.8, § 3, the act of bankruptcy most frequently used by petitioning creditors is that the debtor "ceases to meet his liabilities generally as they become due". A few cases have ordered administration on the basis of a showing of aggravated failure to pay a single indebtedness. *In re Raynor*, [1935] 2 D.L.R. 542 (P.E.I.); *cf. In re Canadian Cap Co.*, 53 Ont. L. Rep. 506 (App. Div. 1922) (default in payment of series of notes due one creditor held sufficient when statute did not require general cessation of payments). Generally, however, proof of nonpayment of a single debt has been held insufficient support for a petition grounded upon an allegation of general cessation of payments. *See, e.g., In re Holmes and Sinclair*, 20 Can. Bankr. Ann. (n.s.) 111 (Ont. Sup. Ct. 1975); *In re Tetrault & Freres Limitee*, 28 Can. Bankr. Ann. 28 (Quebec 1946). Proof of nonpayment of several debts of substantial size in disregard of creditors' demands and debtor's promises to pay on the eve of the filing of the petition has frequently been upheld as a sufficient basis for an order of administration. *In re Shirley*, [1928] 1 D.L.R. 969 (nonpayment of 16 accounts totaling \$3733.30 held to be an act of bankruptcy notwithstanding payment in full of 40 accounts and partial payments on 21 accounts); *In re Glenn*, 23 Can. Bankr. Ann. 81 (Ont. Sup. Ct. 1941); *In re Shellbrook Store*, 13 Can. Bankr. Ann. 24 (Sask. 1931); *In re Campbell*, [1947] Ont. Wkly. Notes 675 (High Ct. of Justice in Bankruptcy 1947).

Since the Canadian law requires an act of bankruptcy to have been committed within six months of the filing of the petition, the question arises whether a continuing failure to pay debts that commenced before the six-month period may suffice as a basis for an involuntary petition. "Stale defaults" antedating the six-month period have not been treated as a cessation occurring within the period. *In re England & Son*, [1923] 2 D.L.R. 738 (C.A.); *In re Vipond and Ewing*, 70 Que. K.B. 41 (1941). Failure to respond to demands made for payment of old indebtedness within the six-month period has, on the other hand, been held a sufficient act of bankruptcy. *In re Raitblat*, [1925] 2 D.L.R. 219 (Ont. Sup. Ct.), *aff'd*, [1925] 3 D.L.R. 446 (C.A.).

I am indebted to John D. Honsberger, Q.C., of the Toronto Bar for the references to the Canadian cases cited in this note.

¹⁷⁴ If a receiver or trustee is appointed in any nonbankruptcy litigation ("a case or proceeding not under this title"), the purpose of the appointment is relevant only in a custodianship involving less than substantially all of the debtor's property. If the purpose in such a case is lien enforcement, the custodianship is not ground for an involuntary petition. A receivership obtained in a proceeding supplementary to execution on a judgment or a receivership to conserve assets during the pendency of a statutory proceeding is, on the other hand, a ground for involuntary relief under § 303(h)(2), irrespective of the amount or proportion of the property taken in charge by the receiver. Possibilities for harsh application of § 303(h)(2) are intended to be kept within bounds by § 305(a), which authorizes dismissal if "the interest of creditors and the debtor would be better served" thereby, and by § 303(i), which imposes liability on petitioners in the event of a dismissal. See the discussion of these safeguards in the text accompanying notes 199-204 & 227-34 *infra*.

administration for the benefit of creditors. An agent is also a custodian if appointed to enforce a lien or to effect general administration. If the purpose of the custodianship is the enforcement of a lien, however, the custodian must have been appointed or authorized to take charge of substantially all of the debtor's property in order to furnish a ground for involuntary relief under Title 11. A custodian need not be appointed by a court and need not be vested with title or subject to any fiduciary obligations respecting the property in his custody.

The alternative of a custodianship dating from a time within 120 days of the filing of the petition comes close to continuing the fourth and fifth acts of bankruptcy. Thus the case law applying section 3a(4) and, to a lesser extent, section 3a(5) of the Bankruptcy Act will be relevant in construing the definition of "custodian" and applying section 303(h)(2).¹⁷⁵ When a custodian of the kind referred to in section 303(h)(2) is appointed or authorized to take charge, however, neither insolvency nor inability to pay debts as they mature need be shown, as has been necessary under section 3a(5) of the Bankruptcy Act. Under the Bankruptcy Act the appointment of a receiver in a lien foreclosure proceeding has not been regarded as an act of bankruptcy.¹⁷⁶ Thus, predicating an involuntary liquidation on a custodianship of substantially all of the property in a mortgage and lien foreclosure proceeding is a departure from old law. On the other hand, such a custodianship did constitute a ground for the filing of an involuntary petition for reorganization under Chapter X of the Bankruptcy Act, but there was no 120-day limit for such a petition.¹⁷⁷

The significance of the time limitation on the utility of the second ground of an involuntary petition under section 303(h) is considerably diminished by the continuing availability as a ground, without time limitation, of the general nonpayment of debts as they become due.¹⁷⁸ The duty of a custodian to turn over and account to the trustee for property of the estate is not subject to any limitation pegged to the time when the petition is filed.¹⁷⁹ Thus, a custodianship is treated in both liquidation and reorgan-

¹⁷⁵ See 1 COLLIER, *supra* note 45, at ¶¶ 3.402-3.406, & 3.502-3.505 (1974).

¹⁷⁶ MACLACHLAN, *supra* note 162, at 48.

¹⁷⁷ Bankruptcy Act § 131(2), & (3). In some respects the Bankruptcy Code provisions permitting an involuntary petition to be filed on the ground of the appointment or authorization of a custodian to take charge of the property of the debtor are broader than § 131 of the Bankruptcy Act. A custodianship in other than a lien enforcement proceeding need not involve substantially all of the debtor's property under §§ 101(10) and § 303(h)(2) of the Code as was required under § 131(2) of the Bankruptcy Act. Moreover, an agent who is neither a trustee nor a receiver may qualify as a custodian under the Code provisions if appointed or authorized by contract or other applicable law, but § 131 of the Bankruptcy Act does not recognize such a person. On the other hand, possession of a debtor's property by an indenture trustee or mortgagee was a ground for filing an involuntary petition under Chapter X (§ 131(3)) but is not a ground under § 303(h) of the Code.

¹⁷⁸ Cf. HOUSE REPORT, *supra* note 17, at 324, [1978] U.S. CODE CONG. & AD. NEWS at 6280; SENATE REPORT, *supra* note 62, at 34, [1978] U.S. CODE CONG. & AD. NEWS at 5820.

¹⁷⁹ Section 543. An assignee for the benefit of creditors appointed or taking possession

izations under the Code in much the same way as it was in Chapter X reorganization cases.

One of the criticisms of the concept of acts of bankruptcy was that it focused on an event that might have predated the filing of a petition by several months and that might be unrelated to the condition of the debtor at the filing of the petition seeking relief.¹⁸⁰ On the other hand, the four-month period was so short that it sometimes led to the filing of a petition before an adequate investigation could be made to determine whether all the elements of an act of bankruptcy had been committed, lest the allowable period expire.¹⁸¹ A more serious objection to the acts of bankruptcy, however, was the heavy burden of proving their commission.¹⁸² Most acts of bankruptcy required proof of insolvency, in the bankruptcy or equity sense, at some point in the last four months preceding a filing of the petition.¹⁸³ The Commission noted several problems in proving acts of bankruptcy.¹⁸⁴ The difficulties of proving the commission of an act of bankruptcy and the risk of damages for failure of proof deterred or delayed the filing of petitions that ought to have been filed earlier in order to prevent the deterioration of the financial condition of the debtor and the loss or disappearance of assets which further reduced the value of the estate.¹⁸⁵

more than 120 days before the filing of the petition may not, however, be surcharged for any improper or excessive disbursement under § 543(c)(3).

¹⁸⁰ See generally Treiman, *supra* note 161.

¹⁸¹ See *e.g.*, Dworsky v. Alanjay Bias Binding Corp., 182 F.2d 803 (2d Cir. 1950) (dismissing involuntary petition predicated on commission of second act of bankruptcy without sufficient allegations of facts); Rawlins v. Hall-Epps Clothing Co., 217 F. 884 (5th Cir. 1914) (denying application for examination to develop information regarding insolvency and commission of action of bankruptcy by alleged bankrupt).

¹⁸² COMMISSION REPORT I, *supra* note 1, at 188. "The commercial world has little time or inclination to argue about valuations shown on a balance sheets and, in most instances, the sort of evidence that is adduced upon the trial of an issue of insolvency when the debtor resists adjudication in bankruptcy is not available." MACLACHLAN, *supra* note 162, at 55.

¹⁸³ Insolvency at the time of the commission of the act was required in connection with the second and third acts and was a usual accompaniment of the first act, although a person may make a fraudulent transfer without being insolvent. Proof of the fifth act of bankruptcy required a showing of insolvency or inability to pay debts as they matured, *i.e.*, insolvency in the equity sense, at the time the act was committed. The sixth act of bankruptcy required the debtor to admit substantially that he was insolvent in an equity sense.

The first sentence of section 3c of the Bankruptcy Act made an allegation and proof by the bankrupt that he was solvent at the date of the filing of the petition a complete defense to an involuntary petition grounded on the first act of bankruptcy. Curiously this was the only provision of the Bankruptcy Act which recognized that the actual financial condition of the debtor at the time of the filing of the petition should affect his amenability to an involuntary bankruptcy.

¹⁸⁴ Commission Report I, *supra* note 1, at 188. Several but not all witnesses at the legislative hearings on the Commission's and Bankruptcy Judges' bill approved the recommendation to abolish acts of bankruptcy. *Hearings, supra* note 13, at 1546 (testimony of Lewis W. Levit for Commercial Law League of America), 1657, 1663 (statement and testimony of L.E. Creel III for the Dallas Bar Ass'n). *But see id.* at 1670, 1678 (statement and testimony of Richard Kaufman for National Ass'n of Credit Management).

¹⁸⁵ "A frequent practical consequence [of the operation of the law requiring proof of an

Congress manifestly accepted this rationale when it enacted section 303(h) of Title 11.

6. Procedure

a. Joinder of Petitioners

Subsection (c) of section 303 authorizes joinder of a qualified petitioner after the filing of the petition and before the case is dismissed or relief is ordered. Such joinder would be appropriate in a case where only one or two petitioners joined in the petition or when the claim of one of three original petitioners is disallowed and at least three are required by section 303(b)(1). Such joinder would also be appropriate where an additional petitioner is required to satisfy the requirement of an aggregate of \$5,000 to be held by petitioning creditors under either paragraph (1) or (2) of section 303(b). The statute does not include a procedure to enable the original petitioner to obtain information about other creditors which would facilitate the addition of other petitioners, but the procedure for this purpose provided by Bankruptcy Rule 104(e) is consistent with the statute and thus should remain available until superseded by a new rule dealing with the subject matter.¹⁸⁶

b. Contest of a Petition

An involuntary petition may be contested only by the debtor or, if the debtor is a partnership, by a general partner that did not join in the petition.¹⁸⁷ The service of the petition on the debtor or the nonjoining partner, and the time within which the answer must be filed or served are presumably governed by Rules 111 and 112 of the Rules of Bankruptcy Procedure¹⁸⁸ until a new procedure is prescribed pursuant to the amended rule-making statute.¹⁸⁹

act of bankruptcy] is to postpone a liquidation until the debtor has become further involved, so that the creditors receive less, with no compensating benefit to the debtor." MACLACHLAN, *supra* note 162, at 57.

¹⁸⁶ See Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 405(d), 92 Stat. 2549. The Co-reporters for the Advisory Committee on Bankruptcy Rules have indicated, however, that they regard Rule 104(e) as superseded by § 303(c) of the Code.

¹⁸⁷ Section 303(d). Rule 112 of the Rules of Bankruptcy Procedure, providing for the filing of responsive pleadings and motions, appears to be entirely consistent with the statute and therefore applicable under the Code. In accordance with the recommendation of the Commission on the Bankruptcy Laws, the provision in § 136 of the Bankruptcy Act for contest by an indenture trustee or stockholder of an involuntary petition filed under Chapter X is not continued in the Code. COMMISSION REPORT II, *supra* note 9, at 79.

¹⁸⁸ Rule 111 authorizes service of a summons and petition anywhere in accordance with Rule 704, and Rule 112 generally allows 20 days after the issuance of a summons for the serving and filing of an answer to a petition. These rules remain effective under the Code. See the note accompanying Interim Rule 1003 suggested by the Co-reporters for the Advisory Committee on Bankruptcy Rules.

¹⁸⁹ 28 U.S.C. § 2075.

c. Jury Trial

Section 1480(b) of Title 28 of the United States Code¹⁰⁰ explicitly provides that the bankruptcy court may order the issues arising under section 303 to be tried without a jury. The abolition of the right to a jury trial in contested proceedings on an involuntary petition, heretofore assured by section 19 of the Bankruptcy Act,¹⁰¹ involves no constitutional issue, since there was no right to a jury trial in bankruptcy proceedings under the common law of England in 1789.¹⁰² The bankruptcy court may nevertheless appropriately empanel a jury and submit to it any issues that arise in a contest of an involuntary petition under section 303.

7. The Interim Between the Filing of an Involuntary Petition and Entry of an Order for Relief

Title 11 recognizes that facilitating the filing of an involuntary petition may increase the risk of an improvident petition. The new law contains safeguards of the right of a business debtor to continue in business pending a determination of the issues in a contested petition. Thus, section 303(f) provides that unless and until the court provides otherwise, and pending the entry of an order for relief, "any business of the debtor may continue to operate, and the debtor may continue to use, acquire, or dispose of property as if an involuntary case concerning the debtor had not been commenced."¹⁰³ Restrictions on the use, sale, and lease of property of the

¹⁰⁰ See Bankruptcy Reform Act of 1978, of Pub. L. No. 95-598, § 241(a), 92 Stat. 2549.

¹⁰¹ The Commission had recommended the abolition of the right to a jury trial of issues raised in the contest of an involuntary petition because of its belief that the statutory provision therefore had been exploited by debtors to delay adjudication. *Commission Report II, supra* note 9, at 45 (citing Rochelle & King, *A Proposal to Raise Bankruptcy Courts to District Court Level*, 13 U. KAN. L. REV. 391, 395-96 (1965)). The resulting delay has permitted estates to deteriorate in value and assets to disappear. The Commission's recommendation met with general favor. See Cook, *Involuntary Bankruptcy and the Proposed Bankruptcy Act of 1973: Reform at Last*, 20 N.Y.L. FORUM 97, 119-21 (1974).

¹⁰² See *Barton v. Barbour*, 104 U.S. 126, 133-34 (1881); *In re Christensen*, 101 F. 243, 244 (N.D. Iowa 1900); 2 COLLIER *supra* note 45, at ¶ 19.02 (1974).

¹⁰³ The authorization for the continuing conduct of the business of the debtor under this provision does not, however, protect all persons who deal with the debtor during the interim. Section 549(a) authorizes the trustee to avoid any postpetition transfer of property of the estate, even though authorized under § 303(f), unless the transfer is saved by subsection (b) or (c) of section 549.

Section 549(b) validates against the trustee any transfer during the interim to the extent it is for value other than the satisfaction or security of a prepetition debt, irrespective of knowledge by the transferee of the pendency of the case. This subsection represents a change of the law of § 70d(3) of the Bankruptcy Act by neutralizing the effect of actual knowledge by the transferee of the pendency of the case. The Commission had recommended similar protection for persons dealing with the debtor during the interim before the order for relief. COMMISSION REPORT II, *supra* note 9, § 4-208(c).

Section 549(c) makes unavoidable any transfer of real property during the interim to a bona fide purchaser for a present fair equivalent value or to a purchaser at a judicial sale without constructive knowledge of the pendency of the case. If the real property of the debtor

estate prescribed by section 363 do not limit the debtor during the interim before the order for relief unless a court order imposes one or more of these restrictions.¹⁹⁴ Those who extend credit or acquire claims in the ordinary course of the debtor's business or financial affairs¹⁹⁵ during the interim between the filing of an involuntary petition and the order for relief or the appointment of a trustee¹⁹⁶ if that occurs earlier, have claims allowable against the estate.¹⁹⁷ These claims are accorded priority just below that given administrative expenses.¹⁹⁸

is located in the county where the case is commenced, the filing of the petition is deemed to give all subsequent purchasers constructive knowledge of the pendency of the case; if the property is located in another county, a copy of the petition must be filed in the records of real estate conveyances in such county to constitute constructive knowledge to subsequent purchasers. A purchaser of real property at a judicial sale is apparently protected by the statute without regard to his actual knowledge of the case or the value of the consideration given for the property, but the purchaser who gives present value is protected only to the extent of the value given without actual knowledge of the case. These results are generally consistent with those required by § 21g of the Bankruptcy Act. For a discussion of the law under § 21g, see 2 COLLIER, *supra* note 6, at ¶ 21.30 (1974); MACLACHLAN, *supra* note 162, § 197.

¹⁹⁴ Section 363 actually refers only to the trustee in restricting the use, sale, or lease of property of the estate, but a debtor in possession in a Chapter 11 case is subject to these restrictions under section 1107. HOUSE REPORT, *supra* note 17, at 404, [1978] U.S. CODE CONG. & AD. NEWS at 6360. Moreover, § 541(a) converts the property of the debtor into property of the estate on the commencement of a case under § 303. Although inadequately expressed, the Congressional intent is apparently to permit the debtor to use, sell, and lease his property before the entry of the order for relief without any constraint, direct or indirect, imposed by § 363. If the estate or secured creditors need protection against spoliation by the debtor or others, section 303(f) recognizes the authority of the bankruptcy court to enter appropriate orders. HOUSE REPORT, *supra* note 17, at 323, [1978] U.S. CODE CONG. & AD. NEWS at 6279; SENATE REPORT, *supra* note 62, at 33, [1978] U.S. CODE CONG. & AD. NEWS at 5819. Such an order may include the appointment of an interim trustee pursuant to subsection (g). See note 206 *infra*.

¹⁹⁵ The reference to financial affairs in § 502(f) is apparently intended to protect a creditor acquiring a claim against a debtor who is not engaged in business but who incurs the debt in a routine or ordinary transaction. Cf. HOUSE REPORT, *supra* note 17, at 373, [1978] U.S. CODE CONG. & AD. NEWS at 6329; SENATE REPORT, *supra* note 62, at 88, [1978] U.S. CODE CONG. & AD. NEWS at 5874.

¹⁹⁶ See text accompanying notes 205-07 *infra*.

¹⁹⁷ Section 502(f); HOUSE REPORT, *supra* note 17, at 354, [1978] U.S. CODE CONG. & AD. NEWS at 6310; SENATE REPORT, *supra* note 62, at 65, [1978] U.S. CODE CONG. & AD. NEWS at 5851.

¹⁹⁸ Section 507(a)(2). Such a priority had been recommended by the Commission. COMMISSION REPORT II, *supra* note 9, § 4-405(a)(2). The legislative reports indicated that "involuntary gap" creditors were granted first priority under the Bankruptcy Act. HOUSE REPORT, *supra* note 17, at 357, [1978] U.S. CODE CONG. & AD. NEWS at 6313; SENATE REPORT, *supra* note 62, at 69, [1978] U.S. CODE CONG. & AD. NEWS at 5855. The law was far from clear on this point. Section 63b of the Bankruptcy Act simply declared that a gap creditor had a provable claim for property transferred or services rendered "for the benefit of the estate" to the extent of the value received by the estate. See MACLACHLAN, *supra* note 162, §§ 140,294. This provision was held not to cover claims for taxes. *In re Berkshire Hardware Co., Inc.*, 39 F. Supp. 663,666 (D. Mass. 1941). The Senate Report accompanying S.2266, *supra* note 62, at 69, [1978] U.S. CODE CONG. & AD. NEWS at 5855, declared, however, that

Under section 303(e) the court may require the petitioners, after notice and hearing for cause, to file a bond to indemnify the debtor.¹⁹⁹ This requirement is intended to discourage frivolous and spiteful petitions.²⁰⁰ Indemnification of the debtor may be required under section 303(i) if the petition is dismissed without the consent of the petitioners and the debtor. Under that subsection the court may grant judgment for the debtor against the petitioners for costs, a reasonable attorney's fee, or any damages proximately caused by the installation of a trustee under Title 11.²⁰¹ If the debtor can establish "bad faith," the petitioner may also be held liable for any damages proximately caused by the filing of the petition or for punitive damages.²⁰² As the legislative reports recognized, an involuntary petition that is dismissed because none of the grounds specified in subsection (h) is established may nonetheless result in putting the debtor out of business.²⁰³ The statute does not impose liability in such a case, however, unless the petition was filed in bad faith or damages proximately resulted from the displacement of the debtor from possession of its property by the appointment of a trustee.²⁰⁴

The new law does not provide for the appointment of a receiver, and indeed the court is prohibited by section 108(b) from making such an appointment. Although section 701(a) authorizes the appointment of an interim trustee in a liquidation case only after an order for relief has been entered,²⁰⁵ section 303(g) provides for the appointment of an interim trustee before entry of an order for relief in an involuntary case if necessary to preserve the property of the estate or to prevent loss to the estate.²⁰⁶ The

the priority granted gap creditors by § 507(a)(2) would include taxes incurred during the conduct of the ordinary course of the debtor's business or financial affairs.

¹⁹⁹ Section 303(e) goes further than Rules 201(d) and 10-201 and § 69a of the Bankruptcy Act, from which it was derived. These provisions of prior law authorized the imposition of a bond requirement only when there was an application for the appointment of a receiver in a straight bankruptcy case.

²⁰⁰ HOUSE REPORT, *supra* note 17, at 323, [1978] U.S. CODE CONG. & AD. NEWS at 6279; SENATE REPORT, *supra* note 62, at 33, [1978] U.S. CODE CONG. & AD. NEWS at 5819.

²⁰¹ The legislative intent is to permit all three kinds of awards to be made against the petitioners in an appropriate case. See HOUSE REPORT, *supra* note 17, at 324, [1978] U.S. CODE CONG. & AD. NEWS at 6280; and SENATE REPORT, *supra* note 62, at 34, [1978] U.S. CODE CONG. & AD. NEWS at 5820, where § 203(i) is paraphrased. The use of "or" here is explained by a reference to § 102(5), which provides that as used in Title 11 is "not exclusive." The legislative reports explained as follows: "Thus, if a party 'may do (a) or (b)', then the party may do either or both. The party is not limited to a mutually exclusive choice between the two alternatives." HOUSE REPORT, *supra* note 17, at 315, [1978] U.S. CODE CONG. & AD. NEWS at 6272; SENATE REPORT, *supra* note 62, at 28, [1978] U.S. CODE CONG. & AD. NEWS at 5813.

²⁰² Section 303(i)(2).

²⁰³ HOUSE REPORT, *supra* note 17, at 323, [1978] U.S. CODE CONG. & AD. NEWS at 6279; SENATE REPORT, *supra* note 62, at 33, [1978] U.S. CODE CONG. & AD. NEWS at 5819.

²⁰⁴ Section 303(i)(1)(C).

²⁰⁵ The court makes the appointment of the interim trustee under § 701(a), but in the 18 pilot districts, § 15701(a) authorizes the United States trustee to make the appointment.

²⁰⁶ The trustee is appointed by the United States trustee in any of the 18 pilot districts, § 15303, and by the court in any of the other districts. § 303(g). In both kinds of districts,

appointment may be made only on request of a party in interest and after notice to the debtor and a hearing.²⁰⁷ The trustee may take possession of the property and operate any business of the debtor. As under Rule 201(d), the debtor may regain possession on filing a bond in an amount fixed by the court, conditioned on the debtor's accounting for and delivering to the trustee the property of the estate or its value.

8. Conversion of a Case Under One Chapter to a Case Under Another Chapter

The question arises whether, if an involuntary case is commenced against an amenable debtor, the case may be interrupted by the filing of a petition under another chapter by the debtor. This question involves a construction of the sections dealing with conversion. Under section 706, a debtor may convert a case under Chapter 7 to a case under Chapter 11 or Chapter 13 at any time, unless the debtor is not eligible for relief under

however, the court determines after notice and hearing whether an interim trustee shall be appointed.

The Code provisions relative to the appointment of an interim trustee under § 303(g) are cryptic. The latter subsection authorizes the court to appoint an interim trustee before an order for relief but then refers to § 701, which authorizes an appointment of an interim trustee only "after the order for relief under this chapter." A person selected under § 701 to serve as trustee qualifies under § 322 by filing a bond with the court. Inferably the interim trustee appointed under § 303(g) qualifies in the same way, but the statute and legislative history are silent about the matter. In a nonpilot district the court determines the amount of the bond and the sufficiency of the surety on the bond. *See* § 322(b). In a pilot district the amount of a bond and the sufficiency of the surety on the bond filed by a trustee under § 322(a)(2) are determined by the United States trustee, according to § 15322(b)(1), but there is no § 322(a)(2). S.658, passed by the Senate on September 7, 1979, would delete the "(2)" from § 15322(b)(1) but would not clarify the obscurities concerning the appointment and qualification of an interim trustee.

²⁰⁷ The import of "on request of a party in interest" is considered in legislative history that discusses § 102(1), where the expression "after notice and a hearing" appears:

The phrase 'on request of a party in interest' . . . is intended to restrict the court from acting *sua sponte*. Rules of bankruptcy procedure or court decisions will determine who is a party in interest for the particular purposes of the provisions in question. . . .

The phrase 'after notice and a hearing' . . . is intended . . . to mean after such notice as is appropriate in the particular circumstances, and such opportunity, if any, for a hearing as is appropriate in the particular circumstances. If a provision of title II [sic] authorizes an act to be taken 'after notice and a hearing' this means that if appropriate notice is given and no party to whom such notice is sent timely requests a hearing, then the act sought to be taken may be taken without an actual hearing.

In very limited emergency circumstances, there will be insufficient time for a hearing to be commenced before an action must be taken. The action sought to be taken may be taken if authorized by the court at an *ex parte* hearing of which a record is made in open court. A full hearing after the fact will be available in such an instance.

Congressional Record, *supra* note 29, at H11090 and S1707.

the chapter to which conversion is sought²⁰⁸ or the case had previously been converted from one under either of those chapters.²⁰⁹ A liquidation case can also be converted on request of a creditor or other party in interest and after notice and hearing²¹⁰ to a Chapter 11 case but not to a Chapter 13 case.²¹¹ Likewise a Chapter 11 or Chapter 13 case may be converted on the request of a creditor or other party in interest to a liquidation case, but only if the debtor is subject to an involuntary petition under section 303.²¹² The right of a creditor to seek conversion can be exercised without regard to whether the original petition commenced a voluntary or an involuntary case. A single party in interest may seek conversion, even though such a party could not have qualified as a petitioning creditor for an involuntary case under section 303.²¹³

D. Cases Ancillary to Foreign Proceedings—Section 304

Section 304, authorizing the commencement of a case ancillary to a foreign proceeding, is a new provision and is derived from a recommendation of the Commission on Bankruptcy Laws.²¹⁴ If a case concerning a debtor is pending in another country, a “case ancillary to the foreign proceeding” may be commenced by the filing of a petition in this country by a foreign representative of the debtor.²¹⁵

As earlier indicated,²¹⁶ section 303(b)(4) authorizes a foreign representative to initiate an involuntary case against a debtor concerning whom a foreign proceeding is pending. The option provided by section 303(b)(4) manifestly contemplates an independent case, although a provision in section 508(a) requires an equalization of distribution when a creditor has

²⁰⁸ A stockbroker or commodity broker may not convert a case under Chapter 7 to a case under either Chapter 11 or Chapter 13, see §§ 706(a) & 109(d), and any debtor who is not an individual with regular income and indebtedness within the limitations prescribed by § 109(e) may not seek conversion of a case to one under Chapter 13. A spouse of an individual eligible to convert to a case under Chapter 13 may convert only if the spouse is independently eligible or is joining with his or her spouse who is likewise converting.

²⁰⁹ It appears that a case started as a Chapter 13 case and converted to a Chapter 7 case pursuant to § 1307 on request of the debtor may not thereafter be converted under § 706 at the behest of the debtor or any other party in interest to a Chapter 11 case. It likewise seems that a case started under Chapter 11 cannot be converted to a liquidation case under Chapter 7 by the debtor or on request of a creditor or other party in interest pursuant to § 1112. The legislative intent in these situations, however, is not unmistakably clear.

²¹⁰ Section 706(b).

²¹¹ Section 706(c).

²¹² Sections 1112(b) & (c) and 1307(b) & (e). A farmer or corporation protected from an involuntary petition under § 303(a) and from an involuntary conversion of a Chapter 11 or 13 case into a case under any other chapter concerning such a debtor is not protected from an involuntary conversion of a liquidation case into a Chapter 11 case.

²¹³ The term “party in interest” is not defined. See note 207 *supra*.

²¹⁴ COMMISSION REPORT II, *supra* note 9, at 69-71.

²¹⁵ A “foreign proceeding” is defined in § 101(19), and a “foreign representative” is defined in § 101(20). See note 156 *supra*.

²¹⁶ See text accompanying note 156 *supra*.

received a distribution in a foreign proceeding on a claim that is allowed in a case instituted under Title 11. Section 304, however, contemplates a proceeding that is merely ancillary to the main proceeding. The House Report explained that such a petition "does not commence a full bankruptcy case."²¹⁷

If the petitioner proceeds under section 303,²¹⁸ the debtor may file an answer and contest the petition, whereas if the petition is filed under section 304, any "party in interest" may controvert the petition.²¹⁹ If the petition is filed under section 303, the petitioner must allege and, if the petition is contested, must prove the general nonpayment of debts or that a custodianship arose within 120 days before the filing of the petition.²²⁰ While any party in interest may controvert a petition filed under section 304, there is no requirement of a showing of nonpayment of debts or of custodianship.

When an order for relief is entered against a foreign debtor under section 303, the debtor is treated like any domestic debtor. This means that the debtor's estate is collected by a trustee, claims are allowed, and the proceeds of the estate are distributed in accordance with the rules prescribed in Chapter 5. The modes of relief available under section 304(b) include: (1) an injunction against the commencement or continuation of an action against the debtor or its property, the enforcement of any judgment against the debtor's property, or the creation or enforcement of a lien against its property; (2) an order to turn over the property of the debtor's estate or its proceeds; or (3) an order for other appropriate relief.²²¹

²¹⁷ HOUSE REPORT, *supra* note 17, at 324, [1978] U.S. CODE CONG. & AD. NEWS at 6280. Professor Kurt H. Nadelmann raised the question whether § 304 is constitutional, suggesting that the Tenth Amendment precludes federal intervention in the absence of a domestic bankruptcy interest. *Hearings, supra* note 13, at 1447, 1450. The constitutionality of § 304 cannot be seriously doubted. *See Hearings, supra* note 13, at 1515-16 (statement of Professor Stefan A. Riesenfeld); Howard, *United States Bankruptcy Jurisdiction Over Unregulated Foreign Banks*, 17 HARV. INT'L L.J. 359, 388-93 (1976) [hereinafter cited as Howard].

²¹⁸ The foreign representative of an estate in a foreign proceeding may file an involuntary petition against the debtor in a domestic proceeding under § 303(b)(4). While a single creditor may qualify as a sole petitioner under § 303(b)(2), *see* text accompanying note 147 *supra*, generally three or more petitioners are required for an involuntary petition by creditors. One partner may file an involuntary petition against the partnership under § 303(b)(3).

²¹⁹ Section 304(b) provides that "if a party in interest does not timely controvert the petition, or after trial," the court may take one of three kinds of action. A "party in interest" is not defined in the Act. *See* note 207 *supra*.

²²⁰ *See* text accompanying notes 161-85 *supra*.

²²¹ As pointed out in Stevens, *supra* note 158, at 64-65, § 304 would have significantly strengthened the position of the German liquidator of the Herstatt Bank in dealing with creditors who attached funds of the bank in the Chase Manhattan Bank in New York. Query, whether turnover ordered pursuant to § 304(b)(2) would subject the property to the laws of the foreign jurisdiction and deprive creditors of liens obtained under the laws of this country? The Commission assumed that its proposed § 4-103(b)(4) would not have this effect, stating that "[t]his does not override the general American rule of conflict of laws that foreign trustees may not defeat rights acquired by local creditors through levy on local assets. . . ." *But see* Stevens, *supra* note 158, at 64:

While as previously noted, section 304 contemplates that a petition under the section may be controverted and that relief may be granted only after trial, the section does not specify what the issues may be at trial. Subsection (c), however, specifies six factors to guide the court in determining what relief will best assure "an economical and expeditious administration" of the debtor's estate. These considerations are: (1) just treatment of all holders of claims against or interests in the estate; (2) protection of claim holders in the United States against prejudice and inconvenience in a foreign proceeding; (3) prevention of preferential or fraudulent dispositions of the property of the estate; (4) distribution of proceeds of the estate substantially in accordance with the order prescribed by Title 11; (5) comity; and (6) the appropriate provision of an opportunity for a fresh start for the individual concerned in the foreign proceeding.²²² The House and Senate Reports emphasized that these guidelines are designed to give the court the maximum flexibility in handling ancillary cases.²²³ "Principles of international comity and respect for the judgments and laws of other nations suggest" that the court be accorded the utmost flexibility in entering appropriate orders.²²⁴

In order to assure a foreign representative that the access to the bankruptcy court afforded him under sections 303, 304, and 305 are not a trap, section 306 provides that an appearance in the bankruptcy court under any

Attaching creditors whose liens survived the preference period under Section 547 . . . solely because of the delay and confusion involving the insolvent multinational might have found their liens under attack from German preference laws applied to implement the fundamental bankruptcy goal of preference avoidance as articulated in Section 304 and 305.

The American conflict of law rules dealing with domestic property subject to a judicial lien when the debtor's estate is under foreign administration are discussed in *Hearings, supra* note 13, at 1486-87, 1505 (statement of Professor Kurt Nadelmann); Nadelmann, *Solomons v. Ross and International Bankruptcy Law*, 9 *Mod. L. Rev.* 154, 163-68 (1946); Riesenfeld, *The Status of Foreign Administrators of Insolvent Estates: A Comparative Survey*, 24 *Am. J. Comp. L.* 288, 306 (1976).

²²² Section 304(c) paraphrases the last sentence of the Commission's proposed § 4-103(c) but adds the factor of "comity." COMMISSION REPORT II, *supra* note 9, at 69-70. The role of comity is discussed in Stevens, *supra* note 158, at 70-72.

The references in § 304(c) to just treatment of holders of claims and interests, protection of creditors in the United States from prejudice and inconvenience, and distribution according to the priority system of the Code enable the court to apply a policy of reciprocity. COMMISSION REPORT I, *supra* note 1, at 70; Stevens, *supra* note 158, at 72-75. The provisions of the Commission's proposed § 4-103(c), on which § 304(c) is based, were nevertheless criticized for failure to limit the foreign representative's rights under the Code by more explicit incorporation of the principle of reciprocity. See Howard, *supra* note 217, at 385-96.

²²³ HOUSE REPORT, *supra* note 17, at 325, [1978] U.S. CODE CONG. & AD. NEWS at 6281; SENATE REPORT, *supra* note 62, at 35, [1978] U.S. CODE CONG. & AD. NEWS at 5821. The Reports disagreed with critics of the Commission's proposal from which § 304 was derived as to whether such a provision enhances or impairs flexibility. See *Hearings, supra* note 13, at 1447, 1448, 1451 (statements of Professor Kurt H. Nadelmann); Howard, *supra* note 217, at 398-99.

²²⁴ HOUSE REPORT, *supra* note 17, at 325, [1978] U.S. CODE CONG. & AD. NEWS at 6281; SENATE REPORT, *supra* note 62, at 35, [1978] U.S. CODE CONG. & AD. NEWS at 5821.

of these three sections does not submit the foreign representative to the jurisdiction of any court of the United States for any other purpose.²²⁵ The bankruptcy court may nevertheless condition any grant of relief under any of these sections on compliance by the foreign representative with the orders of the bankruptcy court.²²⁶

III. ABSTENTION

Section 305(a) empowers the court, after notice and hearing, to dismiss a case under Title 11 or to suspend proceedings in such a case at any time if "(1) the interests of creditors and the debtor would be better served by such dismissal or suspension; or (2)(A) there is pending a foreign proceeding; and (B) the factors specified in section 304(c) of this title warrant such dismissal or suspension."²²⁷ The House Report accompanying H.R. 8200

²²⁵ The German liquidator of the Herstatt Bank is reported to have been advised not to appear in the United States to attack preferences obtained in this country by creditors through attachments of its funds in the Chase Manhattan Bank, N.A., because of the risk of being subjected to the jurisdiction of American courts and adverse judgments that might be res judicata in Germany and of being exposed to discovery procedures. Becker, *International Insolvency: The Case of Herstatt*, 63 A.B.A.J. 1290, 1292 (1976). See also note 158 *supra*.

Although the legislative reports indicated that § 306 was needed to protect the foreign representative from creditors who might file an involuntary petition in this country for the purpose of inducing the representative to come to this country and thereby to subject the estate to American jurisdiction, the statute protects the foreign representative from subjecting himself to jurisdiction of any state court as well as of any federal court. HOUSE REPORT, *supra* note 17, at 352, [1978] U.S. CODE CONG. & AD. NEWS at 6281; SENATE REPORT, *supra* note 62, at 36, [1978] U.S. CODE CONG. & AD. NEWS at 5821.

²²⁶ Section 306 suggests that the relief sought by the foreign representative may be denied unless he submits to in personam jurisdiction of the court. Stevens, *supra* note 158, at 69. The size of the estate subject to the in rem jurisdiction of the domestic bankruptcy court will of course have a direct bearing on the effectiveness of any effort to obtain the consent of the foreign representative to the exercise of in personam jurisdiction. On the other hand, submission by a foreign representative to in personam jurisdiction does not deprive the foreign court of its jurisdiction, either in personam or in rem, in respect to the foreign representative and the estate of the debtor.

Thus, although coordination among bankruptcy courts of the world may require an increasing reliance on *in personam* jurisdiction, practically speaking, *in rem* jurisdiction, which provides a more ready means for enforcing orders, will continue to be a touchstone of bankruptcy proceedings and to limit the degree of international cooperation among courts.

Id. at 70. The legislative reports disavow any Congressional intent to give the bankruptcy court "carte blanche . . . to require the foreign representative to submit to jurisdiction in other courts contrary to the general policy of the section." The purpose of § 306 is to enable the bankruptcy court to enforce its own orders necessary to the grant of appropriate relief under § 303, 304, or 305. HOUSE REPORT, *supra* note 17, at 326, [1978] U.S. CODE CONG. & AD. NEWS at 6282; SENATE REPORT, *supra* note 62, at 36, [1978] U.S. CODE CONG. & AD. NEWS at 5822.

²²⁷ A foreign representative is explicitly authorized to seek dismissal or suspension of a case under Title 11 if a foreign proceeding is pending. § 305(a)(2)(A). Since there can be no foreign representative without the pendency of a foreign proceeding (§ 101(20)), subparagraph (2)(A) is simply a statutory grant of standing to such a representative. Professor Kurt H. Nadelmann vigorously opposed the recommendations of the Commission on Bankruptcy

suggested that a court might properly exercise its power under section 305(a) when an out-of-court workout affords adequate assurance of a satisfactory adjustment with less expense than full administration under Title 11.²²⁸ The provision for abstention when there is no pending proceeding concerning the debtor in any other jurisdiction,²²⁹ is new in the bankruptcy statutes, though there is authority for recognizing an inherent power in the bankruptcy court to decline to exercise its jurisdiction.²³⁰ There is considerable overlap between the two paragraphs of section 305(a) since all the factors specified in section 304(c), with the possible exception of "comity," involve the interest of creditors and the debtor. The fact that a similar proceeding is pending should obviously influence the court when a discretionary dismissal or suspension is sought, but the absence of such a competing proceeding does not preclude the court from weighing many of the same factors in acting on an abstention request.

The authority of the court to abstain under section 305 extends to a case filed under section 301, 302, 303, or 304. While the Code speaks only of dismissal or suspension of a case, the statutory language should not pre-

Laws to accord standing to foreign representatives. See *Hearings, supra* note 13, at 1448, 1449, & 1451.

²²⁸ HOUSE REPORT, *supra* note 17, at 325, [1978] U.S. CODE CONG. & AD. NEWS at 6281; SENATE REPORT, *supra* note 62, at 36, [1978] U.S. CODE CONG. & AD. NEWS at 5822.

²²⁹ The legislative reports noted that "[a] principle of the common law requires a court with jurisdiction over a particular matter to take jurisdiction." HOUSE REPORT, *supra* note 17, at 325, [1978] U.S. CODE CONG. & AD. NEWS at 6281; SENATE REPORT, *supra* note 62, at 35, [1978] U.S. CODE CONG. & AD. NEWS at 582. In 1962, however, the Bankruptcy Act was amended to authorize the bankruptcy court in its discretion to withhold or suspend the exercise of jurisdiction of a case concerning a debtor that had been judged bankrupt in a foreign country. Bankruptcy Act § 2a(22). See Kennedy, *Bankruptcy Legislation of 1962*, 4 B.C. IND. & COM. L. REV. 241, 246-48 (1963). The statute dictated that the court exercise its discretion with "regard to the rights or convenience of local creditors and to all other relevant circumstances." Bankruptcy Rule 119, promulgated in 1973, authorized the court to exercise its discretion with "regard to the rights and convenience of local creditors and to all other relevant circumstances," and to dismiss or suspend a case on appropriate terms when the purpose of a foreign proceeding by or against a debtor was liquidation or rehabilitation. The rule retained the direction to have regard for local creditors and other circumstances. The Commission recommended the inclusion of a provision in its Bankruptcy Act of 1973 similar to Rule 119 but omitted any reference to the rights or convenience of local creditors. COMMISSION REPORT II, *supra* note 9, § 4-103(a). Section 2a(22) of the Bankruptcy Act, Rule 119, and the cases construing these provisions are discussed in Nadelmann, *Rehabilitating International Law: Lessons Taught by Herstatt and Company*, 52 N.Y.U. L. REV. 1, 18-21 (1977) [hereinafter cited as Nadelmann]. The legislative reports make no reference to this background for § 305.

Section 304 supersedes Rule 119 except possibly insofar as the rule requires notice to the petitioner or petitioners and such other persons as the court may direct. The rule has been criticized for not specifically requiring notice to the debtor and the creditors generally. Nadelmann, *supra*, at 20.

²³⁰ See, e.g., *SEC v. United States Realty & Improvement Co.*, 310 U.S. 434, 455-58 (1940); *Zeitinger v. Hargadine-McKittrick Dry Goods Co.*, 244 F. 719, 772-23 (8th Cir.), *cert. denied*, 245 U.S. 667 (1917); cf. Nadelmann, *supra* note 229, at 19.

clude the court from conditioning a dismissal or suspension.²³¹ Thus, the court may condition a dismissal on the commencement of a proceeding in another country or the commencement of a case in this country under another section of Title 11.²³² Except insofar as the court may in its order of dismissal or suspension enjoin parties within its jurisdiction from pursuing other remedies, they are presumably free after dismissal or during suspension to seek whatever nonbankruptcy relief is available respecting the debtor and his property.²³³ In any event, a dismissal or suspension under section 305 is not reviewable in any manner.²³⁴

IV. CONCLUSION

The Bankruptcy Code incorporates most of the reforms respecting the commencement of a case recommended by the Commission on the Bankruptcy Laws. The Bankruptcy Reform Act did not, however, establish the United States Bankruptcy Administration as recommended by the Commission, or any comparable agency, to perform the many administrative functions involved in the commencement of a case under the bankruptcy laws. The United States trustee serving in one of the 18 pilot districts selects an interim trustee prior to the order for relief in an involuntary case when ordered to do so by the court, but his involvement in the early stages of such a case is typically minimal. The legislative history accompanying the Bankruptcy Reform Act discloses a purpose to relieve the court of administrative responsibilities, but the implementation of the Congress-

²³¹ See Samuels, *supra* note 62, at 92, arguing that § 305 should be amended to provide that a bankruptcy court, "having found that a debtor is within the jurisdiction of the court, may dictate the terms on which the case shall be dismissed."

²³² As observed in Samuels, *supra* note 62, at 91 n. 182, the court may not order turnover of property to a foreign representative as a condition to dismissal of a case under § 305(a)(1), unless there is a foreign representative to receive the property. The court may nevertheless suspend proceedings in a case for a time to permit the commencement of a foreign proceeding and the appointment of a foreign representative qualified to take over the property.

Professor Samuels raises the question whether the court, after avoiding a transfer in a case commenced under § 301, 302, or 303 may convert the case to an ancillary case under § 304, under which the court may order a turnover of property to the foreign representative. It seems clear that jurisdiction of part of a case cannot be dismissed or suspended and part retained and exercised under § 305. HOUSE REPORT, *supra* note 17, at 325, [1978] U.S. CODE CONG. & AD. NEWS at 6281; SENATE REPORT, *supra* note 62, at 35, [1978] U.S. CODE CONG. & AD. NEWS at 5821. A court would look askance at a request to convert a case commenced under § 301, 302, or 303 to one under § 304 after a discharge has been obtained, property has been exempted, or a transfer has been avoided.

The bankruptcy court is nevertheless authorized to abstain from exercising its jurisdiction in a particular proceeding under 28 U.S.C. § 1471(d), and its decision to abstain or not to abstain is not reviewable in any manner.

²³³ See Samuels, *supra* note 62, at 91, suggesting doubts as to a state's jurisdiction after dismissal by the bankruptcy court under § 305 and the possible advisability of simultaneous actions by a creditor under bankruptcy and nonbankruptcy law when discretionary dismissal seems a likely eventuality.

²³⁴ Section 303(c).

sional objective falls short. In nonpilot districts the administrative processes are either relegated to performance by unsupervised personnel or involve the bankruptcy judge in these nonjudicial activities. Even in pilot districts the role of the United States trustee in the initial stages of a case is vague and largely undefined.

Cases are commenced under the Bankruptcy Code in much the same way as they were under the Bankruptcy Act. A resulting advantage of this similarity is the minimization of the confusion and litigation that would otherwise have resulted from the lack of new Rules of Bankruptcy Procedure to govern the opening stages of cases filed under the Code. Most of the changes result in the simplification and expedition of the proceedings with attendant benefits of economy of administration and reduced risk of deterioration of the estate during the preliminary stage of the case. The elimination of numerous differences between the rules prescribed for the commencement of a liquidation case and those governing a reorganization or rehabilitation case permits the use of a single, uniform rule and common forms for a case filed under any chapter. More than form is involved, however, in the new authorization for the filing of an involuntary petition for reorganization. The rules and forms prescribed by the Rules of Bankruptcy Procedure for commencing the various kinds of cases are easily adaptable to such a simplified and uniform practice.

The enlargement of the exclusions of financial institutions from eligibility for and amenability to relief under the bankruptcy laws has no self-evident justification. The recommendation of the Commission for eliminating the unwarranted immunity from involuntary petitions of corporations that are not moneyed, business, or commercial was ignored. The explicit authorization for the filing of joint petitions by spouses appears to be a realistic approach to the problems presented by married debtors. The legal and other problems entailed by the authorization should be amenable to judicial resolution under the general terms of the statute.

The most significant reform in respect to the commencement of a case is the abolition of the acts of bankruptcy together with the elimination of the right to jury trial of the issues of the debtor's insolvency and the commission of an act of bankruptcy. Another reform of great significance is the number of options provided the bankruptcy court for achieving rational and fair administration of estates of debtors having assets in more than one country. Although these reforms will affect fewer cases than will be affected by the consolidation of the reorganization chapters, they are important and may have a significant impact on the behavior of financially-distressed debtors and their creditors. The impact will be greatest in cases involving transnational debtors. The net effect of the changes in the bankruptcy law should be favorable to sound, efficient, and fair administration of the bankruptcy laws.

