McGILL LAW JOURNAL
Montreal
Volume 18 1972 *Number 2*

The Need for a Rapprochement of the Bankruptcy Systems of Canada and the United States

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In both Canada and the United States the power to establish uniform laws of bankruptcy have been closely connected with the regulation of trade and commerce. In *Dupon* v. *La Cie de Moulin à Bardeau Chanfréné* [2] Mr. Justice Wurtele of the Superior Court of the Province of Quebec quoted Mr. Wharton's treatise on Private International Law that bankruptcy is a species of national execution against the estate of an insolvent and then went on to say:

> It is... in the interest of the trade and commerce of the whole Dominion that there should be one uniform law for all the provinces, regulating proceedings in the case of insolvent debtors, unrestricted in its operation by provincial boundaries; that it should be possible to obtain a national execution, and not merely a limited provincial one, against the estate of an insolvent debtor, who might hold property in several provinces, or transfer it from one province into another.

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[1] Ed. Note: John Honsberger is a partner in the firm of Raymond and Honsberger of Toronto. He was a member of the Canadian Study Committee on Bankruptcy and Insolvency Legislation which made its Report in December, 1970 and to which some reference is made in this article. He is also a member of the National Bankruptcy Conference and its committee on Canada-United States Relations which in October of 1971 made its Report which is also referred to in this article. It was the recommendation of the latter committee that there should be more comparative study of the bankruptcy legislation of Canada and the United States with the hope that it would lead to the better co-ordination of the two systems that largely prompted the writing of this article. The author would particularly like to acknowledge the great assistance he obtained in the preparation of this article from the many articles on international bankruptcies written by Professor K. H. Nadelmann and from working with him in the National Bankruptcy Conference.

[2] (1888), 11 L.N. 225.

The draftsmen of the Constitution of the United States were similarly aware of the connection between the inter-state trade and a national bankruptcy system. Immediately following each other in the Constitution are to be found the inter-state commerce clause and the clause authorizing uniform bankruptcy laws. *The Federalist* said, in commenting upon this:

> The power of establishing uniform laws of bankruptcy is so intimately connected with the regulation of commerce, and will prevent so many frauds where the parties or their property may lie or be removed into different States, that the expediency of it seems not likely to be drawn into question.[3]

While the bankruptcy systems of Canada and the United States reflect a concern with the protection of inter-provincial and inter-state trade, more and more has business developed along international lines. The development of bankruptcy law, however, has not kept pace with the growth of international trade and commerce and it has been slow to eliminate inequities in international bankruptcies. The concept of creditor equality which has been said to be the ultimate aim of bankruptcy[4] and which perhaps has best been expressed by the *Code Napoleon*[5] which declared that the whole of the property of a debtor is a common pledge for all of his creditors is not universally recognized in international bankruptcies. Canada and the United States are each creditor countries. Each is also the largest trading partner of the other. Each is concerned to promote trade and should be concerned in protecting its traders. In a large measure this could be achieved if the bankruptcy laws of each country were so co-ordinated so as to provide that the whole property of a debtor, where part of it is in one country and part in the other, is, in fact, a common pledge for all his creditors irrespective of which side of the border they reside and where the property is located.

As the bankruptcy laws of each country have not always been drafted having regard to rules of conflict of laws, concurrent bankruptcies are often required to achieve a measure of equality where the creditors and the property of the debtor are divided between the two countries. In 1820 Mr. Chancellor Kent of New York made his often repeated comment concerning the disadvantages of multiple bankruptcies:

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[3] *The Federalist, on the New Constitution,* vol. XLI, (1788), *per* James Madison.

[4] *Clarke* v. *Rogers,* 228 U.S. 534 (1913), at p. 548.

[5] Sections 2092, 2093.

> It would be in the power of the bankrupt to throw his property under the distribution of either commission, at his pleasure; and it would put creditors upon calculations of exclusive advantages, and of running a race of diligence against each other, and of resorting to the one fund or the other, as circumstances may dictate. The perplexities arising from the concurrent operation of distinct commissions would be increased if the commercial house had establishments in different countries, with joint and separate debts belonging to each firm, to be distributed. Such a state of things, and such conflicting systems, would lead to great inconveniences and confusion, and be the source of fraud and injustice, and disturb the equality and equity of any bankrupt system.[6]

Eight years later, Chief Justice Parker of Massachusetts explained how such results could be avoided:

> It may be well at some future time when there shall be bankrupt laws here, to accept the proffer of Great Britain, France, or Holland to reciprocate the benefit of such a system (of unity of bankruptcy), but we are persuaded, if such a change shall take place, it must be under the auspices of the national legislature or the national courts, or some treaty with the commercial nations of Europe, and not by adjudications of a court for one out of the numerous governments that compose the United States.[7]

In 1905 when addressing the Universal Congress of Lawyers and Jurists in St. Louis, Mr. Justice Nesbitt of the Supreme Court of Canada said:

> I think it is a very great pity that there should not be some legislation immediately regulating many questions on international law, at any rate between Canada and the United States. The growing interchange of business, owing to the geographical continuity, makes it very important that there should be well-defined rules applicable to both countries upon many questions which are constantly arising. Take, for instance, bankruptcy, receiverships, administrations, etc.[8]

Professor Kurt H. Nadelmann, almost 40 years later and now almost 30 years ago could only say:

> In view of the developments in other parts of the world, the fact that the United States and Canada, immediate neighbours with a similar bankruptcy law, still are without any agreement on questions of bankruptcy administrations involving both countries, must appear strange.[9]

The *Report of the Study Committee on Bankruptcy and Insolvency Legislation*[10] in 1970 once again referred to the problem

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[6] *Holmes* v. *Remson*, 4 Johns. Ch. 460 (N.Y., 1820), at p. 471.

[7] *Blake* v. *Williams*, 6 Pick 286 (Mass., 1828), at p. 314, *per* Parker, C.J.

[8] *To What Extent Should Judicial Action by Courts of a Foreign Nation be Recognized?*, Universal Congress of Lawyers and Jurists, (St. Louis, U.S.A., 1905), at p. 226.

[9] K. H. Nadelmann, *International Bankruptcy Law; Its Present Status*, (1943), 5 U. of Toronto L.J. 324, at p. 351.

[10] Information Canada, (Ottawa, 1970), at pp. 60-62.

of international bankruptcies and recommended that attempts be made to negotiate international agreements on conflict rules with countries that trade substantially with Canada.

While one swallow does not make the spring, it is not without significance that last year the National Bankruptcy Conference of the United States created a new committee on Canada-United States Relations. In its report to the 1971 Annual Meeting of the Conference this committee stated,

> This committee is... concerned with the particular aspects of the international law of bankruptcy as they relate to the United States and Canada and sees its special function:
>
> 1. to identify situations in international bankruptcies involving nationals of both the United States and Canada
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> (a) that either discriminate or appear to discriminate against the creditors of the one country in the courts of the other, and
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> (b) that make it unnecessarily difficult to resolve legal difficulties which would prevent the most efficient and equitable distribution of estates where the debtor, the creditors and the property of the debtor are not all within the same jurisdiction;
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> 2. to make recommendations leading towards the better co-ordination of the two systems, particularly in conflict situations; and
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> 3. to encourage, thereby, the development of trade, commerce and mutual understanding between the two countries.

This committee specifically recommended that it is both desirable and necessary that there be further study of the bankruptcy legislation of both the United States and Canada. In the comment to the recommendation it was said that "the primary concern of the study would be to work on amendments leading towards the better co-ordination of the two systems without any international commitment". In the long run, it was of the opinion that there should be a joint group established to study the two systems in depth from the point of view of a "rapprochement". The committee acknowledged that this could lead to a subsequent recommendation that there should be a bankruptcy treaty between the two countries but any such recommendation could be made only after the intensive comparative study of the two systems had been completed.

A bankruptcy convention between Canada and the United States certainly would do much to promote trade between the two countries by giving greater protection to traders than now exists. It is possible, however, that many of the inequities that now exist to the detriment of Canadian and American traders and credit grantors could be resolved, and perhaps more successfully, without a convention.

Over the years, in the absence of any bankruptcy convention or statutory guidelines, the courts through practical necessity have had to exercise a choice of law when a bankruptcy occurs and the debtor, his creditors and his property are partly in the one and partly in the other country. In some cases, the courts have applied their own domestic law to situations arising in the other country. In other cases, they have applied the law of the other country to situations arising, at least, in part in their own country.[11] To the extent that courts mutually recognize the bankruptcy proceedings in the other country and ensure that foreign creditors are treated equally with domestic creditors and, in addition have a discretion to refrain, in suitable circumstances, from exercising their jurisdiction, there is a substantial degree of co-ordination between the two systems. Unfortunately, this is not now the case as the legislation of each country has evolved differently and the conflict of laws rules applied by the courts are not always similar. This has led to discrimination and inequities to the detriment of the commercial communities of the two countries.

Since *Solomons* v. *Ross*[12] the doctrine of ubiquity has been held to be a part of the law of England. "The English courts . . . have consistently applied the doctrine of universality, according to which they hold that all movable property, no matter where it may be situated at the time of the assignment by the foreign law, passes to the trustee".[13] The courts of the common law provinces in Canada also follow this doctrine. As an example, they will, as a rule, order movable property within their jurisdictions to be turned over to a trustee in bankruptcy appointed by a competent foreign court even if the property has been attached or garnished after the bankruptcy adjudication.[14]

It was suggested in *Solomons* v. *Ross* that the title of a foreign trustee overrides encumbrances already acquired by third parties over moveable property of the bankrupt situated in England. However, the English courts have not accepted this suggestion. The Canadian Courts would probably come to the same conclusion. Thus, if a foreign creditor should attach, in Canada, moveable

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[11] Dicey and Morris, *Conflict of Laws*, 8th. ed., (1967), at p. 6.

[12] (1764), 1 Hy. Bl. 131. See: K. H. Nadelmann, *Solomons* v. *Ross and International Bankruptcy Law*, (1946), 9 Modern L. Rev. 154.

[13] G. C. Cheshire, *Private International Law*, 8th. ed., (1970), at pp. 549-550.

[14] *Williams* v. *Rice*, [1926] 3 D.L.R. 225 (Man.); *Bank of Nova Scotia* v. *Booth*, (1910), 19 Man. R. 471 (C.A.); *Brand* v. *Green*, (1900), 13 Man. R. 101 (C.A.). See also: Dicey and Morris, *op. cit.*, n. 11, at p. 677; G. C. Cheshire, *op. cit.*, n. 13, at p. 550.

property of a debtor followed by an adjudication of bankruptcy in the foreign country, the attachment ranks prior to the title of the foreign trustee notwitstanding it is considered to be a preference under both the foreign and Canadian law. In such circumstances, equal distribution could be achieved only if a Canadian bankruptcy adjudication could be obtained. If, however, there was merely the presence of assets in Canada, the Canadian courts would not have the jurisdiction to make a bankruptcy order and equality of distribution could not be obtained.[14a]

The principle of universality does not apply to immovables. The rule in the common law provinces of Canada is that the assignment of a bankrupt's property to the representative of his creditors according to the bankruptcy law of any foreign country is not and does not operate as an assignment of any immovables of the bankrupt situated in those provinces.[15] In proper cases, however, a foreign trustee in bankruptcy may be authorized to act as a receiver of immovable property situated in the common law provinces and to sell it and to deal with the proceeds as trustee in bankruptcy.[16]

As the Canadian *Bankruptcy Act* does not provide for the assumption of bankruptcy jurisdiction in the case of a non-resident on the mere presence of assets in Canada[17] which would permit a preference to be voided, the Canadian conflict rule in respect to movables is only just. As Professor Nadelmann has observed "the conflicts rule and the bankruptcy system available are not without relation".[18]

In the province of Quebec, except for judgments from other provinces, conclusive effect is denied to all foreign judgments as a matter of law.[19] A foreign bankruptcy in the absence of a Cana-

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[14a] *Galbraith* v. *Grimshaw*, [1910] A.C. 508; G.C. Cheshire, *op. cit.*, at p. 550 which was considered in *Re Universal Auto Bonders Ltd.*, 24 W.W.R. 600; 13 D.L.R. (2d) 459; 37 C.B.R. 52 (Alta.).

[15] Cheshire, *op. cit.*, n. 13, at p. 551; Dicey and Morris, *op. cit.*, n. 11, at p. 681; *Macdonald* v. *Georgian Bay Lumber Co.*, (1878), 2 S.C.R. 364, holding that an assignment under the United States *Bankruptcy Act* did not transfer immovable property in Canada.

[16] *In re Kooperman*, (1928), 13 B. & C.R. 49; [1928] W.N. 101 (High Ct.).

[17] *Cf.* section 2(1) of the United States *Bankruptcy Act*.

[18] K. H. Nadelmann, *Bankruptcy in Canada: Assets in New York*, (1962), 11. Am. J. Comp. L. 628, at p. 630. A note commenting on *Bank of Buffalo* v. *Vesterfelt*, 232 N.Y.S. 2d 783 (Erie County Ct., 1962).

[19] Civil Code, article 6(2); Code of Civil Procedure, articles 178-180; Johnson, *Foreign Judgments in Quebec*, (1957), 35 Can. Bar. Rev. 911; K. H. Nadelmann, *Enforcement of Foreign Judgments in Canada*, (1960), 38 Can. Bar. Rev. 68.

dian bankruptcy adjudication has no effect in the province whether or not the property of the debtor situated in Quebec is movables or immovables or whether or not the debtor had appeared in the foreign bankruptcy proceedings. In any new action brought within the province to enforce a foreign judgment, the defendant in the Quebec courts may plead to the action on the merits or set up a defence which might have been pleaded in the original proceedings.[20]

In the Quebec case of *Ryan* v. *Pardo,* Mr. Justice Brossard said:

> It is now well settled that, in view of article 210 [now article 178], a foreign judgment... however final it may be [in the foreign jurisdiction] does not constitute [in Quebec] *res judicata* or *chose jugée.* The "full faith and credit" doctrine, as known and applied in the United States between states and as applied in another form in Canada between provinces, does not apply between the province of Quebec, and the State of New York under any text of our law, nor for that matter is there, in this province, any text of law giving general and formal recognition to the doctrine of 'Comity of Nations' or *Comitas gentium.*[21]

The Courts of the United States have not recognized the doctrine of ubiquity first enunciated by *Solomons* v. *Ross* [22] which required a bankruptcy declared in the domicile of the debtor to be recognized everywhere.[23] Instead, the doctrine of territoriality is generally accepted. This provides that an assignment under the insolvency law of one country operates only upon property within that country, so that title acquired by the trustee is of no avail against creditors who attach property under the law of another country where it is actually situated.[24] In most of the states of the United States the conflict rules will, for example, permit local creditors to attach or garnish assets of a debtor notwithstanding the debtor has been adjuged bankrupt in Canada.[25] This denial of extra-territorial effect to a foreign bankruptcy judgment is not unique. It

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[20] Code of Civil Procedure, article 178 provides: "any defence which was or might have been set up to the original action may be pleaded to an action brought upon a judgment rendered out of Canada".

[21] S.C.N. 299,676. Judgment of Nov. 27, 1953. The case was appealed but settled before the filing of factums.

[22] (1764), 1 Hy. Bl. 131.

[23] Nadelmann, *op. cit.,* n. 12.

[24] G. C. Cheshire, *Private International Law,* 7th. ed., (1965), at p. 448, citing *Security Trust Co.* v. *Dodd Mead & Co.,* 173 U.S. 624 (1899) and the doubt at Professor Nadelmann whether this is true since the United States *Bankruptcy Act* of 1898; K. H. Nadelmann, *The National Bankruptcy Act and the Conflict of Laws,* (1946), 59 Harv. L. Rev. 1025, at p. 1027.

[25] Nadelmann, *op. cit.,* n. 18, at p. 628.

is the law of many other jurisdictions including the province of Quebec.

The Supreme Court of the United States on several occasions has held that it is not *ultra vires* for a state to refuse to recognize the transfer of property within the state resulting from a foreign bankruptcy adjudication which conflicts with the rights of local creditors seeking to recover their debts against local property.[26] A state seemingly, could also provide for the payment to foreign creditors be deferred until resident creditors were paid. In most states, however, the courts have held or it has been specifically provided by statute that both foreign and local creditors should share equally.[27]

The possible advantage that local creditors in the United States might receive over Canadian creditors under the provision of state laws is only applicable in any event to proceedings outside of bankruptcy. The legislative grant of power over the subject of bankruptcy is given by the United States constitution to Congress.[28] Whether or not local creditors are entitled in a bankruptcy to priority to foreign creditors is governed by federal law exclusively. The present United States *Bankruptcy Act* provides that "debts have priority, in advance of the payment of dividends to creditors that by the laws of the United States (are) entitled to priority".[29] Neither the *Bankruptcy Act* nor any other federal statute discriminates between local or foreign creditors. Thus, if a Canadian creditor is faced by discrimatory state legislation or rulings by state courts in attempting to attach or garnish property of the debtor within the state, the creditor may circumvent such discrimination by petitioning for a bankruptcy order. Moreover, under the American Act the court has jurisdiction in bankruptcy if there is property of the debtor within the jurisdiction of the court whether or not the debtor is a resident.[30] Once a bankruptcy order is made

[26] *Clark* v. *Williard*, 292 U.S. 112 (1934), *Cert.* to Sup. Ct. Mont.; *Clark* v. *Williard*, 294 U.S. 211 (1935) *aff'd; United States* v. *Belmont*, 301 U.S. 324 (1937) in which it was said, at p. 335 by Stone, J.:

> But it is a recognized rule that a State may rightly refuse to give effect to external transfers of property within its borders so far as they would operate to exclude creditors suing in its courts.

[27] K. H. Nadelmann, *Foreign and Domestic Creditors in Bankruptcy Proceedings: Remnants of Discrimination*, (1943), 91 U. of Pa. L. Rev. 601, at p. 606.

[28] Art. 1, s. 8, cl. 4.

[29] U.S. *Bankruptcy Act* (1968), s. 64a(5).

[30] Section 2a(1).

payments made to local creditors within four months prior to bankruptcy are subject to being set aside as preferential payments.

In practice, however, a Canadian creditor could be under some disadvantage in competing against local creditors in a state that permits local creditors to be paid in priority to foreign creditors. Under the United States *Bankruptcy Act* if there are more than twelve creditors, a petition for a bankruptcy order can only be brought if three creditors join in the petition.[31] Where local creditors have an advantage in attaching local assets, they may be reluctant, being against their interest, to assist a foreign creditor to obtain a bankruptcy order which would have the effect of reducing their distributive share in the debtor's property.[32]

Some of the difficulty in reconciling the conflict of law rules of the two countries arises out of different approaches towards the enforcement and recognition of foreign judgments. Foreign judgments were originally enforced in England because it was considered that the law of nations required the courts of one country to assist those of another. This theory is generally known as the doctrine of comity.

Although there are many definitions of comity, a generally accepted definition is that of the Supreme Court of the United States found in the case of *Hilton* v. *Guyot*[33] in which comity in its legal sense was defined as "neither a matter of absolute obligation on the one hand, nor of mere courtesy and goodwill, upon the other. But it is the recognition which one nation allows within its territory to the legislative, executive, or judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citizens or of other persons who are under

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[31] Section 59(b),(d).

[32] Where a claim is purchased to institute bankruptcy proceedings in the United States, it should be noted that General Order 5(2) provides that there shall be annexed "to each of the triplicate petitions a copy of all instruments of assignment or transfer, and an affidavit setting forth the true consideration paid for the assignment or transfer of such claims and stating that the petitioners are the *bona fide* holders and legal and beneficial owners thereof and whether or not they were purchased for the purpose of instituting bankruptcy proceedings". Proposed new bankruptcy Rule 104(d) provides: "a person who has transferred or acquired a claim for the purpose of commencing a bankruptcy case shall not be a qualified petitioner..." (similar language to the first part of General Order 5(2)).

[33] 159 U.S. 113 (1895), at pp. 163, 164.

the protection of its laws". It is, however, at most, only a rule of practice and not of law.[34]

As long ago as 1835, English courts disapproved the doctrine that private rights and duties are recognized by reason of comity between nations [35] although the recognition of these private rights and duties, as distingnished from their enforcement, may still be said to be conceded *ex comitate.*[36] English and Canadian common law courts when faced by a foreign bankruptcy order would, as a rule, take the position that they were being asked to recognize and enforce rights conferred by foreign law and duties that are thereby imposed and might speak of the legal obligation of foreign judgments. American courts, on the other hand, more often speak in terms of comity. In a very recent case, for example, a federal court judge in Hawaii said:

> The mere fact of the foreign (Canadian) appointment of a receiver in bankruptcy does not, standing alone, come into conflict with domestic bankruptcy policies. Since application of our bankruptcy law is limited to "proceedings under this title", 11 U.S.C. s. 11(a), it is clear that this court can look into controversies arising under bankruptcy laws of foreign nations without defeating principles of uniformity enunciated in our law (so long as jurisdiction is otherwise proper). Thus, in the absence of international treaties on the subject, one must look to principles of comity to discover whether foreign receivers may entertain suits in local courts to recover debts for the bankrupt estate.[37]

As a general rule, an American trustee can reach assets in Canada, other than the province of Quebec, more easily than assets in the United States can be reached by a Canadian trustee. The different conflict rules and the variation in their application causes uncertainty, inconvenience and, in some cases, hardship. In order to more nearly reach equality among creditors in international bankruptcies concurrent bankruptcies are too frequently necessary. This complicates the administration of the assets, increases the costs of administration and reduces the assets available for distribution among the creditors.

The failure of the present bankruptcy systems of Canada and the United States to adequately protect international credit relations between the two countries, to the extent it might, to the detriment of the trader and credit grantor and to the embarassment of their

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[34] *Gillette Safety Razor Co.* v. *Hawley Hardware Co.*, 60 F. 2d 1019 (Conn. Dist. Ct., 1932).

[35] *Warrender* v. *Warrender*, (1835), 2 Cl. & Fin. 488 (H.L.).

[36] See: *In Re Askew*, [1930] 2 Ch. 259, at pp. 264, 275.

[37] *Waxman* v. *Kealoha*, (1969), 296 F. Supp. 1190 (Hawaii Dist Ct., 1969), at pp. 1193.

professional advisers leads one to a consideration of the possibility of negotiating a bankruptcy convention between Canada and the United States.

At the outset, it should be recognized, and history more than confirms it, that bankruptcy conventions are very difficult to negotiate. Indeed, all efforts towards drafting a bankruptcy treaty for universal application have so far failed. On the other hand, it must be admitted that there have been several bi-lateral and multi-lateral bankruptcy treaties negotiated, for the most part, between adjoining States.[38] These treaties have all provided for a single bankruptcy administration governed by a special code of rules.

It is of course more difficult to negotiate a treaty between countries that have very different bankruptcy systems. Fortunately Canada and the United States have reasonably similar systems in that both have the same origins. The similarity, however, is often more apparent than real. One need only mention the differences between the two systems in respect to the suspect periods for attacking settlements and for setting aside preferences, the treatment of liens and tax claims, the status of bankruptcy, the right to a discharge and the debts released on a discharge, to indicate just some of the differences in substance between the legislation of the two countries. More minor differences but which nevertheless cause administrative difficulties in providing equality among creditors are different orders of priority in payment of dividends and different time limits during which rights accrue or proceedings are barred.

An example of the magnitude of the problem of negotiating a bankruptcy treaty may be seen in the Common Market draft conven-

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[38] France, for example, has negotiated a series of conventions with a number of its neighbours which includes the *Franco-Swiss Convention* of June 15, 1869, the *Franco-Belgium Convention* of July 8, 1899, the *Franco-Italian Convention* of June 3, 1930, the *French Saar Convention* of March 3, 1950 and May 20, 1953 and the *Franco-German* treaty on the Saar of October 27, 1956. In 1928, the Sixth Pan-American Conference in Havana adopted the *Bustamante Code* of Private International Law which contains a Part relating to bankruptcies. Fifteen countries have adhered to this Code. In 1933, the Scandinavian countries of Denmark, Finland, Iceland, Norway and Sweden entered into a bankruptcy convention. The Common Market countries after several years of study have recently completed a draft of a convention on bankruptcy, compositions and related proceedings. For a study of the existing international treaties dealing with bankruptcy, see K. H. Nadelmann, *International Bankruptcy Law, Its Present Status,* (1944), 5 U. of Toronto L.J. 324.

tion designed to make a bankruptcy declared in one of the states effective in the entire community. All of the states are civil law countries and the draft convention does not deal with adjudications in bankruptcy of nationals by courts of states that are not members of the community. Nevertheless, the draft treaty is some 59 pages in length including annexes. The actual treaty is 30 pages long and contains some 82 articles.

Certainly before a bankruptcy convention can be negotiated between Canada and the United States an intensive comparative study of the two bankruptcy systems must be undertaken along the lines suggested by the Canada-United States Relations Committee of the National Bankruptcy Conference. It may be, however, that the best preparation for negotiating a treaty is to go as far as one can in the unification of the substantive law of bankruptcy by reciprocal legislation. Professor Nadelmann who has been a leading advocate for this approach has recently written:

> The failures of international endeavors to deal with the subject of bankruptcy are well known. In the opinion of this writer, the best approach to the problem is not necessarily work on a convention securing a single administration in all cases. A more productive approach may be revision of faulty local conflicts law. As in all areas of conflicts, in bankruptcy the most serious difficulties come from statutory provisions preventing courts from reaching reasonable and equitable results. Local law reform can produce a more favourable general situation and reveal as well more clearly what has to be done internationally.[39]

Through reciprocal legislation whereby Canada and the United States would enact legislation similar to each other identical international results can be obtained without a treaty and very much more quickly. The American observers to the eighth session of the Hague Conference on Private International Law in 1956 suggested to the Conference that it consider the use of uniform legislation as well as conventions.[40] The proposal was not well received possibly by reason of the fact that there had not been any previous wide use of this method among European countries, although the German states over 100 years ago had used legislation to unify the law of

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[39] K. H. Nadelmann, *Assumption of Bankruptcy Jurisdiction over Non-Residents*, (1966), 41 Tul. L. Rev. 75, at p. 81.

[40] K. H. Nadelmann & W. L. M. Reese, *The American Proposal at the Hague Conference on Private International Law to Use the Method of Uniform Laws*, (1958), 7 Am. J. Comp. L. 239; K. H. Nadelmann, *Uniform Legislation Versus International Conventions Revisited*, (1968), 16 Am. J. Comp. L. 28.

bills of exchange [41] and the Scandinavian countries have had a long history of co-operation in the field of legislation.[42]

Canada and the United States have also had long and comparatively successful histories of working with uniform legislation at the constituent level in each country. In the United States, there is the National Conference of Commissioners on Uniform State Laws and in Canada the Conference of Commissioners on Uniformity of Legislation. The single most successful uniform statute has been the *Uniform Commercial Code* of the United States which has been adopted with only minor variations in 49 of the 50 States and Article 9 of the Code has now been exported to Canada in the form of the Ontario *Personal Property Security Act.*[43]

While there has been reasonable progress towards uniform legislation within the two countries it is remarkable that on the international level between Canada and the United States there has not been greater co-operation in the joint drafting of legislation. Professor Nadelmann once said in reference to the Canadian Uniform *Enforcement of Foreign Judgments Act* that:

> Unilateral drafting, however, is not the best way to reach results... Co-operation in drafting commends itself and the two Conferences of Commissioners should join hands for that purpose. Many a student of the close relations between the two "neighbours without a frontier" has been wondering at the lack of co-operation on that level. It contrasts with what has been done elsewhere for unification of law between neighbours, and even for entire regions, generally and, in particular in the matter of recognition and enforcement of judgments.[44]

These comments are equally applicable to bankruptcy legislation but as the constitutional grant of legislative power over the subject matter of bankruptcy in both countries is at the federal level co-operation in drafting should be a much simpler matter in that it would involve only two governments.

As a first step towards co-operative drafting each country should unilaterally attempt to achieve a greater degree of co-ordination in its legislation so as to better ensure equality among

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[41] K. H. Nadelmann, *Uniform Legislation Versus International Conventions Revisited, id.*, citing Hudson & Feller, *The International Unification of Laws Concerning Bills of Exchange,* (1931), 44 Harv. L. Rev. 333, at p. 335.

[42] K. H. Nadelmann, *Uniform Legislation Versus International Conventions Revisited, id.* Ekeberg, *The Scandinavian Co-operation in the Field of Legislation,* in Unification of Law, (International Institute For the Unification of Private Law, Rome, 1948), at pp. 321, 329.

[43] R.S.O. 1970, c. 344.

[44] K. H. Nadelmann, *Enforcement of Foreign Judgments in Canada,* (1960), 38 Can. Bar. Rev. 68, at p. 88.

creditors and to avoid needless duplication of administrations. Courts should be given the jurisdiction to achieve reasonable and equitable results and jurisdictional competition between the courts of the two countries should be discouraged. In this regard, much could be accomplished if the laws of each country purported to give the same effect to a bankruptcy declaration on property situated outside the country of the adjudication and the courts of each country had uniform discretionary powers where bankruptcy jurisdiction is assumed over debtors who are not domiciled in the country. At a later stage, through co-operative drafting, increasing uniformity in the legislation could be progressively attained.

Already the provisions of the Canadian and American Bankruptcy Acts are substantially the same in respect to the vesting of property located outside of the country of the bankruptcy adjudication. Under the Canadian *Act*, property is defined as being property "whether situate in Canada or else-where" [45] and the property divisible among a debtor's creditors "... shall comprise... all property wherever situated of the bankrupt at the date of his bankruptcy or that may be acquired by or devolve on him before his discharge".[46] While based upon the English Act this language is peculiar to the Canadian Act. Since 1952, the United States *Act* declares that the trustee has title to the property of the bankrupt "wherever located".[47] While such declarations in either statute in respect to the title to foreign assets cannot bind the courts of the other country at least trustees in both countries can rely on an express declaration in their statute that their title extends to property wherever located. This cannot but help to strengthen the position of the trustee in the courts of the other country in situations where the courts might otherwise be hesitant in permitting a foreign trustee to seize local assets. The similarity between the vesting provisions in the legislation of the two countries is an example of how the two systems hopefully could be co-ordinated to the advantage of the commercial community of each country.

Since the United States Act of 1898, the presence of assets in the United States has been a sufficient ground to the United States courts for the assumption of bankruptcy jurisdiction.[48] Thus, a non-resident debtor can be adjudged bankrupt in the United States

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[45] Section 2(o).

[46] Section 47.

[47] Section 70a as amended by P.L. No. 456, 66 Stat. 429-430 (1952), 82d Cong., 2nd Sess. s. 23a.

[48] Section 2(1)(a).

courts if he has assets in the United States. The Canadian courts, on the other hand, do not have this jurisdiction. This can cause difficulties particularly in the case of a United States debtor owning immovable property in Canada. A United States bankruptcy or turn over order would not be recognized in Quebec and would probably not be recognized elsewhere in Canada unless on the grounds of comity when the courts might co-operate in the liquidation of the property for the benefit of the estate.[49] If the Canadian court refused to co-operate with the United States trustee, it would not be possible to obtain a Canadian bankruptcy order and thereby reach the immovables for the benefit of the American creditors assuming the debtor did not reside or carry on business in Canada. The United States trustee, however, could demand the bankrupt to convey the Canadian immovables to him and thereby circumvent the impossibility of obtaining a Canadian bankruptcy order and the refusal of the Canadian courts to recognize an American judgment in respect to immovables.[50] The trustee, nevertheless, could be embarassed by a recalcitrant bankrupt or a bankrupt who had absconded. In this case, it would be a reasonable step towards the co-ordination of the two bankruptcy systems if the Canadian legislation also provided that the courts could assume bankruptcy jurisdiction if there were assets of the debtor within the jurisdiction of the court. Such a provision would also be useful to get around the difficulty created by *Galbraith* v. *Grimshaw* which, in effect, requires a local bankruptcy (which may be difficult to obtain if there was not jurisdiction to make such an order on the mere presence of assets) in order for a foreign trustee to override encumbrances already acquired over property of the bankrupt situated in Canada.[50a]

A small matter, mentioned earlier,[51] that sometimes discriminates against a Canadian creditor wishing to petition for a bankruptcy order in the United States easily could be rectified. The necessity of three petitioning creditors for a bankruptcy order where there

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[49] See: In re Kooperman, *op. cit.*, n. 16 where a Belgium trustee was appointed, on an *ex parte* application, receiver in England with authority to sell immovables and deal with the proceeds as trustee in the foreign bankruptcy.

[50] Section 7(a)(5) provides that "The bankrupt shall... (5) execute and deliver to his trustee transfers of all his property in foreign countries". *Cf.* s. 129(1) of the Canadian *Act:* "The bankrupt shall... execute such powers of attorney, conveyances, deed and instruments as may be required".

[50a] See *supra* f.n. 14A.

[51] See *supra,* at p. 155.

are more than twelve creditors is believed peculiar to the United States. The original purpose for such a provision probably was to prevent frivilous petitions. The United States might consider whether this provision still serves a useful purpose and if not, whether in the interest of uniformity and to give both domestic and foreign creditors the equal opportunity to appear before the bankruptcy courts, it might be sufficient for a single petitioning creditor as is the rule in Canada and all other countries.

Probably, one of the most important areas for co-ordination of the two bankruptcy systems and which would not be difficult to accomplish is for the courts of each country to be given a clear discretion to refuse to exercise its bankruptcy jurisdiction in appropriate cases so as to minimize the number of concurrent bankruptcies. This is not to say, however, that it is always desirable that there be a single administration in a bankruptcy involving property or creditors in both countries. If, for example, an attaching creditor will not voluntarily release the property of the debtor that he has obtained and which would be considered to be preferential, concurrent bankruptcies are necessary. Concurrent bankruptcies may also be desirable in certain circumstances to give the court of the other country jurisdiction to impose criminal sanctions against a fraudulent debtor who could not be reached by the courts of the first country. Nevertheless, where a bankruptcy order has already been made in one country and the court in the other is of the opinion that the bankruptcy can be handled as well as, or better, by the foreign administration, without any detriment to local creditors, it should have the discretion to refuse to exercise its bankruptcy jurisdiction.

This is, however, an area where the *Bankruptcy Acts* of each country are either silent or not necessarily in conflict. There are provisions in both statutes which permit courts to refuse to exercise their bankruptcy jurisdiction and thereby prevent concurrent bankruptcies. It would, however, be preferable if these provisions were more closely similar and in respect of the Canadian statute, it specifically authorized that which now can only be implied.

In the case of a petition for a receiving order, the Canadian legislation permits the court to dismiss a petition if it is of the opinion that for "sufficient cause no order ought to be made" [52] or for "sufficient reason" to stay "the proceedings under a petition, either altogether or for a limited time, on such terms and subject

[52] Section 25(7).

to such conditions as the court may think just".[53] If a bankruptcy order is made without knowledge that an earlier bankruptcy order was made, for example, in the United States, a Canadian court has the jurisdiction to annul bankruptcy if it is of the opinion that "a receiving order ought not to have been made".[54] A Canadian court may also "review, rescind or vary any order made by it under its bankruptcy jurisdiction".[55]

Since September 25, 1963, the United States courts have been invested with jurisdiction to "exercise, withold or suspend the exercise of jurisdiction, having regard to the rights or conveniences of local creditors and to all other relevant circumstances, where a bankrupt has been adjuged bankrupt by a court of competent jurisdiction without the United States".[56] The addition of this sub-section was to ensure that jurisdiction over persons adjudged bankrupt by a court of competent jurisdiction outside the United States would not be considered compulsory.[57]

Some years before this amendment was made in the United States *Act*, Professor Nadelmann had written:

> Needless duplication of administrations should of course be avoided. Courts should have discretion to refuse adjudication where administration abroad will suffice. It is submitted that laws making adjudication mandatory upon a petition in due form should be amended accordingly. After adjudication, the courts should likewise have power to dispense with local administration in appropriate cases and to approve arrangements between the administrations found to be beneficial or convenient with due regard to the rights of the creditors who have proved their claims.[58]

While there is a very wide discretion given to Canadian courts to exercise or suspend the exercise of its bankruptcy jurisdiction, it would be helpful if the Canadian courts were specifically given the jurisdiction that the American courts are given by section 2(22) of the United States *Act* to withhold or suspend the exercise of its bankruptcy jurisdiction where the debtor has been adjudged bankrupt by a foreign court. Under the present Canadian *Act*, courts might be under some doubt that such expressions as "sufficient cause", "sufficient reason" or "of the opinion a receiving

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[53] Section 25(11).
[54] Section 151(1).
[55] Section 157(5).
[56] Section 2(22).
[57] H. R. Rep. No. 1208, 87th. Cong., Sess. 1, 4 (1961).
[58] K. H. Nadelmann, *Revision of Conflicts Provisions in the American Bankruptcy Act*, (1952) 1 Int'l. and Comp. L. Q. 484, at p. 490.

order ought not to have been made..." does, in fact, empower them to exercise such a discretion. Moreover, if such a provision was contained in the Canadian legislation, it might add very little to the existing state of the law, but it would indicate to the courts that it was the intention of Parliament that a court should not exercise its bankruptcy jurisdiction where a foreign court previously had adjudged the debtor bankrupt unless there was good reason for a concurrent bankruptcy in Canada.

There is, however, a practical limitation on the extent to which a discretion in a court to refuse to exercise its bankruptcy jurisdiction will help minimize the necessity for concurrent bankruptcies and that is the general lack or less than full mutual recognition of the rights of a trustee as conferred upon him by a foreign court. A local court can hardly refuse to exercise its bankruptcy jurisdiction if the foreign trustee is prevented from taking possession of local assets. To overcome this difficulty, the bankruptcy legislation of each country could give jurisdiction to courts while exercising their bankruptcy jurisdiction, the discretion to act in aid of and be auxiliary to each other in all matters of bankruptcy. A somewhat similar jurisdiction already exists in the *Bankruptcy Acts* of the United States and Canada in respect to the jurisdiction of other courts exercising jurisdiction in bankruptcy within the country.

In the United States, for example, courts of bankruptcy are invested, within their respective territorial limits, jurisdiction to:

> exercise ancillary jurisdiction over persons or property within their respective territorial limits in aid of a receiver or trustee appointed in any bankruptcy proceedings pending in any other court of bankruptcy: *Provided, however,* That the jurisdiction of the ancillary court over a bankrupt's property which it takes into its custody shall not extend beyond preserving such property and, where necessary, conducting the business of the bankrupt, and reducing the property to money, paying therefrom such liens as the court shall find valid and the expenses of ancillary administration, and transmitting the property or its proceeds to the court of primary jurisdiction.[59]

In Canada,

> All courts and the officers of all courts, respectively, shall severally act in aid of and be auxiliary to each other in all matters of bankruptcy, and an order of one court seeking aid, with a request to another court, shall be deemed sufficient to enable the latter court to exercise, in regard to the matters directed by the order, such jurisdiction as either the court that made the request or the court to which the request is

[59] Section 2(20) of the United States *Act.*

made could exercise in regard to similar matters within its respective jurisdiction.[60]

The Canadian provision is based upon a similar provision found in the English *Bankruptcy Act* that provides that the courts of England, Scotland, Ireland and "every British court elsewhere" having jurisdiction in bankruptcy shall severally act in aid of and be auxiliary to each other.[61] The New Zealand *Insolvency Act* has a comparable section requiring the New Zealand courts to act in aid and be auxiliary to commonwealth courts with the discretion to act in the aid and be auxiliary to the courts of any country, not a commonwealth country, upon the request of such a court. The section reads:

1. The Supreme Court shall, in all matters of bankruptcy, act in aid of and be auxiliary to any other Court of any Commonwealth country other than New Zealand, being a Court having jurisdiction in bankruptcy, and an order of that Court requesting aid shall be sufficient to enable the Supreme Court to exercise in regard to the matter specified in the order such powers as the Supreme Court might exercise in respect of the matter if it had arisen within its own jurisdiction.
2. The Court may, if it thinks fit, exercise the powers specified in subsection (1) of this section at the request of a Court in any country not a Commonwealth country.[62]

If Canada and the United States would incorporate a provision in their bankruptcy legislation similar to that contained in the New Zealand *Act*, much would be done to resolve the present divergent conflict of laws rules.

The discretionary jurisdiction of the courts to come to the aid of and be auxiliary to other courts would preserve the flexibility in the procedure which is important in dealing with international bankruptcies. This discretion would be presumably exercised having regard to what the court considered was in the best interest of local creditors. In any event, once a decision was made to come to the aid of another court, the court coming to this decision should have, in addition, a discretion as to what assistance it ought to give and the power to impose such conditions and require such undertakings as it may think proper.[63]

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[60] Section 158(2) of the Canadian *Act*.

[61] Section 122 of the *Bankruptcy Act, 1914*, 4-5 Geo. 5, c. 59 (Eng.), s. 122.

[62] *Insolvency Act, 1967*, 16 Eliz. II c. 54, s. 135 (Statutes of N.Z.).

[63] Where the Manx Bankruptcy Court asked the aid of an English court for getting in movable and immovable property in England, the English court held that it was bound to give assistance, but had a discretion as to what assistance it ought to give, and could impose such conditions and require such undertakings as it may think proper: *Re Osborn*, [1931-32] B. & C.R. 189.

Another important area of the law where it is desirable that there be uniformity is the marshalling of assets. This plays an important function in maintaining equality among creditors when the assets of a debtor in the one country cannot be included in the bankruptcy in the other country either because the title of the trustee is not recognized in the other country or the debtor has been ajudged bankrupt in both countries. Individual creditors may obtain dividends or payments from both sets of assets. The problem is how to provide for equalization.

Canadian courts follow the hotchpot rule which requires that a creditor who proves in the Canadian bankruptcy after having obtained property of the bankrupt situated abroad must bring into the common fund the property so acquired whether it represents the proceeds of movable or immovable property.[64] The inclusion of the words "movable and immovable" in the definition of "property" in the Canadian *Bankruptcy Act*[65] has the effect of forcing a creditor to bring the proceeds of immovable property into account. In effect, a creditor who has received a payment from property of the debtor located abroad and who wishes to prove in the Canadian bankruptcy of the debtor is required to have his share calculated on the basis of a fund in which the money received abroad is included. The rule, which is based upon the principle that he who asks for equity must do equity, has been applied in England since at least 1762.[66]

The *Bankruptcy Act* of the United States is one of the few acts that expressly provides that a creditor who proves a claim in a domestic distribution must account for payments received abroad. The act provides:

> Wherever a person shall have been adjudged a bankrupt by a court without the United States and also by a court of bankruptcy, all creditors with claims allowed by the court of bankruptcy who have not had a dividend paid or declared in their favour by a court without the United States shall first be paid a dividend equal to that paid or declared in such foreign court in favour of other creditors of the same class under this Act, before creditors who have had a dividend paid or declared in their favour by such foreign court shall be paid any amount in the court of bankruptcy.[67]

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[64] Dicey & Morris, *op. cit.*, n. 11, at p. 671.

[65] Section 2(o).

[66] *Rickards* v. *Hudson* as reported in *Smith Appeals to the Privy Council from the American Plantations* 490 (1950).

[67] Section 65(d). See generally: K. H. Nadelmann, *op. cit.*, n. 58, at pp. 487-488; K. H. Nadelmann, *op. cit.*, n. 24, at pp. 1049-1051; Dicey, *Conflict of Laws*, 7th. ed., (1958), at pp. 693-696.

There is no reason why the Canadian *Act* should be silent in respect of such an important principle as the hotchpot rule which is so basic to the principle that there should be equality among creditors. In the interest of making it clear to all foreign creditors who might seek to prove a claim in a Canadian bankruptcy, it would be useful if the Canadian *Act* clearly stated that the hotchpot rule applied by adding to the Canadian *Act* a similar section to that contained in the American *Act*. However, as well as possible situations that might occur are not covered by the American section, it would be useful to have specialists of each country to jointly work on a new uniform text which would better insure equality amongst creditors.

One final example of an aspect of international bankruptcy law which Canada and the United States could co-operate in by enacting similar legislation is the matter of the recovery of preferences acquired in the one country after a bankruptcy adjudication in the other country. The recovery of preferences acquired abroad has always caused difficulties. If the preference was within the appropriate delay prior to bankruptcy, the case is covered by the *Bankruptcy Acts* of both Canada and the United States. What is not clear is the case of a preference acquired abroad after a bankruptcy adjudication. Some countries, such as the Netherlands have specific provisions in their statutes requiring creditors to refund preferences acquired abroad after the bankruptcy declaration. The section in the Netherlands *Act*, for example, provides:

> Creditors who, after the bankruptcy declaration, obtain satisfaction, fully or in part, by attaching assets of the bankrupt abroad on which they had no priority right, shall refund to the estate what they have received.

Professor Nadelmann has suggested that rather than rely on analogies, it might be advisable to include in the United States *Bankruptcy Act* an express provision similar to that contained in the Netherlands *Act*.[68] Similarly, a comparable provision in the Canadian *Act* would be helpful.

Conclusion

The growth in the mutual trade and commerce between Canada and the United States has outpaced the development of the bankruptcy conflict of laws rules of each country. Old inequities still exist and it is often difficult for professional advisers to protect creditors from discrimination. Bankruptcy still only provides for

[68] K. H. Nadelmann, *op. cit.*, n. 24, at p. 1055.

a national execution against an insolvent debtor with assets and creditors on each side of the border. Creditors, as a body, are often hurt while a minority of creditors, financiers, lawyers and trustees may benefit from the complexity of the law and from situations that amount more or less to a legal "no man's land". "Raubsystem" is the German term for such a system. Others have called it a system of legal robbery.[69] It is in the national interest of both countries to find a remedy for this situation.

In the long run, it may be desirable for Canada and the United States to negotiate a bankruptcy convention. It is not necessary, however, to look only towards a convention to obtain relief. Moreover, any convention designed to provide for only a single administration, in all cases, might not be desirable as it would not give the degree of flexibility to cope with the variety of situations that can arise. No one rule or code of rules can be expected to solve all situations equally satisfactorily in this complex field of laws.

Much, however, can be done to provide reasonable remedies through unilateral improvements in the conflict rules of the bankruptcy legislation of the two countries. To obtain the greatest benefit and to minimize future conflicts, it is desirable that the conflict rules of each country be as similar as possible, if not uniform, to each other. At the same time, a wide discretion should be given to the courts not only to assure the equal distribution of the debtor's assets, but to promote the social and economic rehabilitation of the debtor and commercial morality.

To achieve a desirable level of uniformity in the bankruptcy legislation of Canada and the United States so as to co-ordinate the two systems will require close co-operation between the bankruptcy and conflicts specialists of the two countries. It will also require a degree of commitment similar to that exhibited by the European Economic Community in its efforts to simplify the formalities of the recognition of all judgments of member states. Article 220 of the Convention of March 25, 1957[70] provides, for example, that:

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[69] Qu'arrive-t-il maintenant? Le jugement prononçant la faillite n'est pas exécutoire dans un autre pays. Et quelle est la conséquence? Que des créanciers sans foi ni honneur saisissent dans le dernier pays à leur profit les biens de la faillite qui se trouvent dans ce pays. Et le syndic ou curateur n'y peut rien. L'existence de cet état de chose a été qualifiée de véritable scandale. C'est un vol plus ou moins légalement organisé. Rahusen, *Report of the Fourth Conference on Private International Law at the Hague.*

[70] (1957), 51 Am. J. Int'l. L. 865, at p. 930.

> Member States shall, so far as necessary, engage in negotiations with each other with a view to ensuring for their nationals ... the simplification of the formalities governing the reciprocal recognition and execution of judicial decisions and arbitral awards.

It is not too much to hope that Canada and the United States would feel similarily committed to improve the simplification of the formalities governing the reciprocal recognition and execution of bankruptcy adjudications.

Much intensive research involving a comparative study of the bankruptcy systems of the two countries along the lines suggested by the Canada — United States Relations Committee of the National Bankruptcy Conference must be undertaken. If this is to be done, some consideration should be given to the institution that should be responsible for this research or at least, for its co-ordination. This could be an existing institution, a partnership of existing institutions or some new institution created for the purpose.

In the summer of 1970, a three day round table was held in Milan to study the problems of international bankruptcies within the Common Market.[71] A similar conference involving Canadian and American specialists could provide a forum for a discussion of the problems of international bankruptcies involving Canada and the United States with the positive aim of attempting to arrive at a "rapprochement" between the bankruptcy systems of the two countries. From such a beginning involving the exchange of information and the discussion of different viewpoints, an orderly system of research and study could be co-ordinated. As Professor Nadelmann, who has devoted much of a working lifetime to the study of international bankruptcies, once said, "after a full coverage of the subject, the possibilities for greater uniformity will appear automatically."[72]

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[71] The proceedings of this Conference have just appeared: *Les problèmes internationaux de la faillite et le marché Commun,* (Edizioni Cedam: Padova, 1971).

[72] K. H. Nadelmann. *Concurrent Bankruptcies and Creditor Equality in the Americas,* (1947), 96 U. of Pa. L. Rev. 171, at p. 187.