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CROSS-BORDER INSOLVENCY THEORIES AND THE PUBLIC POLICY EXCEPTION

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ABSTRACT

This paper critically examines Article 6 of the UNCITRAL Model Law on Cross-Border Insolvency, 1997, prominently known as "the public policy exception". It highlights the tension between the theories of Territorialism and Modified-Universalism in interpreting the "manifestly contrary clause" contained within this exception, reflecting a broader tension between the desire for international legal harmonization and the preservation of national legal autonomy. By exploring the diverse enactment and interpretation of Article 6 among Model Law, 1997 adoptee countries, this article reveals that narrow interpretation aligns with Modified-Universalism, while broad interpretation corresponds to Territorialism. Case analysis indicates Territorialism as an antithesis to the harmonization efforts sought by the Model Law, 1997. Additionally, it is noted that some Asian Countries have enacted Article 6 in a manner that allows wide interpretation, which is against the guidelines of Model Law, 1997. This article concludes with a compelling call for greater international

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cooperation, recommending uniform enactment and interpretation of Article 6 to enhance global legal consistency in cross-border insolvency cases.

Key Words: *Public Policy Exception, Modified-Universalism, Manifestly Contrary Clause, Cross-Border Insolvency, Article 6*

TABLE OF CONTENTS

I. INTRODUCTION

Domestic insolvency law is the backbone of a nation's economic framework, while cross-border insolvency law connects global economies. The history of domestic insolvency law dates back to ancient Roman times, the Middle Ages, and notably in Napoleon's commercial code viz. "the *Code de Commerce* of 1807".[1] Despite this long history, there was no uniform cross-border insolvency law to manage cases involving creditors or assets in different countries. As a result, countries relied on traditional methods such as bilateral and multilateral treaties and conservative approaches like Territorialism. This lack of uniformity turned into a major crisis with the 1991 collapse of *Maxwell Communication Corporation Plc.*[2] The event triggered insolvency proceedings around the world and highlighted the need for harmonized laws.[3] The case concluded in 1996 with the aid of bilateral treaty and protocol, after which a movement begins for enacting internationally uniform cross-border insolvency laws.[4] United Nations Commission on International Trade Law ("**UNCITRAL**") responded to the pressing need for uniform insolvency laws by developing the Model Law on Cross-Border Insolvency, 1997 (hereinafter referred as 'Model

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[1] BOB WESSELS ET AL., INTERNATIONAL COOPERATION IN BANKRUPTCY AND INSOLVENCY MATTERS (2009).

[2] Re Maxwell Communication Corp. Plc, 186 B.R. 807 (S.D.N.Y. 1995).

[3] Re Bank of Credit and Commerce International SA (1992) BCC 83 (Ch) 89; Re Paramount Airways Ltd (1993) Ch 223 (CA) 239; Barclays Bank Plc v. Homan (1992) BCC 757 (CA).

[4] INTERNATIONAL INSOLVENCY LAW: THEMES AND PERSPECTIVES (Paul J. Omar, 2008).

Law, 1997').[5] Emerging cross-border insolvency theories, combined with Model Law, 1997 began to transform international insolvency law.

A. CROSS-BORDER INSOLVENCY AND ITS THEORIES

"Cross-border insolvency" might roll off the tongue with ease, yet its regulation is anything but straightforward. It paints a picture of insolvency that transcends national boundaries, weaving a complex web where assets and creditors are not confined to one jurisdiction but are spread across the globe. This international entanglement introduces complexity as courts in different countries, each with their own set of laws, claim the right to adjudicate, turning what could have been a straightforward procedure into a multifaceted legal puzzle. At the forefront of this discussion stands the Model Law, 1997, renowned for its ambitious endeavor to streamline the complexities of this area. Despite its success, it fails to provide a formal definition for the term, leaving a blank space for interpretation and further exploration in the complex world of cross-border insolvency.

Since the advent of cross-border insolvency as a specialized field, its jurisprudence has gradually expanded, signaling the emergence of multiple theories within this sphere.[6] At the forefront is *Universalism*, a theory Lord Hoffmann famously described as *"the golden thread of common law"*.[7] This theory revolves around the general principle of private international law which demands an insolvency proceeding to be unitary

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[5] UNCITRAL Model Law on Cross-Border Insolvency, June 21, 1985, UN Doc A/40/17, Annex I.

[6] Sefa M.Franken, *Three Principles of Transnational Corporate Bankruptcy Law: A Review,* 11 ELJ 232 (2005).

[7] Re HIH Casualty and General Insurance Ltd, [2008] UKHL 21.

and universal.[8] Universalism suggests that one insolvency proceeding with one law in one country should handle all aspects of an insolvency case, including all assets and creditors, and the results of this proceeding would be accepted worldwide.[9] For example, if a company having assets and creditors in multiple countries goes bankrupt, Universalism would recommend that a single court of one country with one law to manages the whole process. The decision of this court would then be accepted by all the countries involved, simplifying the process and ensuring equal treatment for all creditors. While many praise the theory for its idealistic approach, critics argue that it limits sovereign independence in the cross-border insolvency matters.[10] This is because each country would have to adhere to single court's ruling even if it conflicts with their economic interests. Nevertheless, Universalism is helpful in specific areas of insolvency proceedings such as the discharge of debts, the distribution of assets and the avoidance of antecedent transactions.[11]

In contrast, the theory of *Territorialism* holds an opposite notion, asserting that insolvency proceedings should be strictly domestic, wherein the local creditors are preferred over the foreign creditors.[12] For example, if a company having creditors and assets in multiple countries goes bankrupt, Territorialism would recommend that each country would use their domestic laws to discharge the debts of their domestic creditors with

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[8] Gerard McCormark, *Universalism in Insolvency Proceedings and the Common Law,* 32 Oxford J. of Legal STUD. 325 (2012).
[9] L Perkins, *A Defense of Pure Universalism in Cross Border Corporate Insolvencies,* 32 NYU J. INT'L L. & Politics 787 (2000).
[10] F Tung, *Is International Bankruptcy Possible?,* 23 Mich. J. of INT'L L. 31 (2001).
[11] Gerard McCormark, *supra* note 9.
[12] IAN BROWNLIE, PRINCIPLES OF PUBLIC INTERNATIONAL LAW 105 (5th ed. 1998).

the local assets of that company. This theory is closely associated with the *Grab Rule,* wherein local assets are grabbed for the advantage of local creditors, ignoring the claims of foreign creditors.[13] However, this inherent discrimination can disrupt the balance of global relations and international politics.[14] A concern echoed by Gerard McCormack, who pointed out that *"National Chauvinism is especially unappealing if it overtly discriminates against foreign creditors."*[15]

A classic 134-year-old case of *Gibbs and Sons v La Societe Industrielle* illustrated the use of Territorialism by English courts wherein it was held that "foreign liquidation laws could discharge foreign debts, but a claim of English creditor could only be discharged by English laws."[16] This decision gained extensive criticism as being against the modern notion of globalisation, reinforcing Territorialism, undermining decisions of foreign courts.[17] The ex post facto effect of *Gibbs Doctrine* raised a serious question as *'which approach should be adopted to distribute insolvent debtor's assets, Territorialism or Universalism?'*.[18] A discussion that remained unsolved until Lord Hoffman's liberal interpretation planted seeds of Modified-Universalism in the firm field of common law.

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[13] R N Robertson, *Enforcement and Other Problems in International Insolvencies*, The Meredith Lectures, McGill University, Montreal 267 (1985).
[14] Lynn M. LoPucki, *Cooperation in International Bankruptcy: A Post- Universalist Approach*, 84 Cornell L. REV. 760 (1999).
[15] Gerard McCormark, *supra* note 9, at 3.
[16] Gibbs and Sons v. La Societe Industrielle 25 (CA) 399 (QBD, 1890); Global Distressed Alpha Fund Ltd partnership v. PT Bakrie Investindo (Comm) 256 (EWHC, 2011).
[17] IAN FLETCHER, INSOLVENCY IN PRIVATE INTERNATIONAL LAW (2nd ed. 2005).
[18] Look Chan Ho, *Recognising Foreign Insolvency Discharge and Stare Decisis,* 26 JIBLR 266 (2011).

Universalism and Territorialism were being rejected due to the apparent conflict between *local protection* versus *international cooperation.*[19] Countries begin to manage cross-border insolvency by allowing claims of both domestic and foreign creditors, but keeping domestic creditors at priority. Professor LoPucki labelled the then-prevalent situation as *Cooperative Territorialism*.[20] This theory prevailed until the late twentieth century when a gradual shift toward more cooperative practices in insolvency proceedings began to emerge, which eventually led to the creation of the Model Law in 1997.[21]

The Model Law, 1997 is rooted in the theory of *Modified Universalism*, acts as a middle point between the extreme theories of Territorialism and Universalism.[22] It acknowledges the central premise of Universalism that asset countries should have a universal administration while also enabling concurrent legal proceedings in domestic jurisdictions, thus incorporating elements of Territorialism.[23] It outlined distinctions between 'main' and 'non-main' proceedings by stressing the importance of fairness of procedure, transparent disclosures, protection of domestic creditors, and adherence to public policy.[24] Furthermore, it empowered courts to deny assistance and recognition to foreign proceedings that contravened these fundamental domestic principles.

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[19] Bob Wessels, *supra* note 2, at 2.
[20] Lynn M. LoPucki, *supra* note 15.
[21] NEIL FRANCIS HANNAN, CROSS BORDER INSOLVENCY – THE ENACTMENT AND INTERPRETATION OF THE UNCITRAL MODEL LAW (2017).
[22] *Id.*
[23] Jay L. Westbrook, *Choice of Avoidance Law in Global Insolvencies* 17 BROOK. J. of INT'L L. 499 (1991).
[24] Paul J. Omar, *supra* note 5, at 2.

While no definitive litmus test exists to declare which theory reigns supreme, Professor Paul J Omar's *Universalism-Territorialism Paradigm*, as illustrated in Table 1.1., provides a valuable framework for understanding these theories' operational dynamics. This paradigm allows for a deeper understanding of how each theory addresses the intricacies of cross-border insolvency.

Exercise of Jurisdiction Recognition and Enforcement of Principal Administration	⇨ **Unity** ⇩	**Plurality**
Universal	**Universalism** **Modified Universalism**	**Secondary Insolvency**[25]
	[Administration with	**Cooperative Territoriality**

[25] Paul J. Omar, *supra* note 5, at 2; H Hanisch, *Universality versus Secondary Bankruptcy: A European Debate* 2 International Insolvency Review 151 (1993).

Territorial	no multi-state elements]	**Territoriality**

The Universalism-Territorialism Paradigm [26]

Table 1.1

B. UNCITRAL MODEL LAW ON CROSS BORDER INSOLVENCY, 1997

The economic downturn of the early 1990s underscored the need for a standardized approach to address cross-border insolvency, prompting Working Group V of UNCITRAL to develop the Model Law on Cross-Border Insolvency, which was adopted on May 30, 1997.[27] This initiative sought to provide states with modern guidelines to be followed while enacting cross-border insolvency laws.[28] Emphasizing harmonization over unification, the Model Law introduced fundamental principles such as Access, Recognition, Relief, Coordination, and Cooperation, structured within 5 chapters and 32 articles.[29] Additionally, UNCITRAL has issued supplementary texts to remove implementation barriers.[30] As of now, the

[26] Paul J. Omar, *supra* note 4, at 2.
[27] UNCITRAL, *supra* note 5.
[28] UNCITRAL, GUIDE TO ENACTMENT AND INTERPRETATION OF THE UNCITRAL MODEL LAW ON CROSS BORDER INSOLVENCY (U.N. 2014), https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/1997-model-law-insol-2013-guide-enactment-e.pdf.
[29] *Id.* at 5.
[30] UNCITRAL, *supra* note 5; UNCITRAL Guide 2014, *supra* note 28; UNCITRAL Legislative Guide on Insolvency law was enacted in four parts in the years 2004, 2010, 2019 and 2021 respectively; UNCITRAL, PRACTICE GUIDE ON CROSS BORDER

Model Law, 1997 has been embraced by 59 countries, marking a significant step towards a streamlined and effective cross-border insolvency framework.[31]

II. ARTICLE 6 OF MODEL LAW, 1997: UNDERSTANDING THE PUBLIC POLICY EXCEPTION AND THE MANIFESTLY CONTRARY CLAUSE

The "public policy exception" is a basis for bankruptcy courts to deny recognition or assistance in cross-border insolvency cases. Courts invoke this exception to refuse reliefs that would ultimately hamper the public policy of their country. "Public policy" is a dynamic concept that keeps on changing according to the legal and societal norms of each jurisdiction. Due to its diverse interpretation across countries, there is no strict, universally accepted definition of what constitutes the public policy exception. Courts consider the economic and political interests of their jurisdiction and international relations when defining the public policy exception.

The UNCITRAL Model Law's Guide to Enactment and Interpretation discusses broad and narrow interpretation of 'public policy'. It is broad when interpreted as per the *"mandatory rule of national law"* and narrow when it is used to interpret *"fundamental principles of law, particularly*

INSOLVENCY COOPERATION (U.N. 2009); UNCITRAL, MODEL LAW ON CROSS BORDER INSOLVENCY: THE JUDICIAL PERSPECTIVES (U.N. 2013); UNCITRAL, MODEL LAW ON RECOGNITION AND ENFORCEMENT OF INSOLVENCY RELATED JUDGMENTS (U.N. 2018); UNCITRAL Model Law on Enterprise Group Insolvency, July 15, 2019, https://uncitral.un.org/en/MLEGI; UNCITRAL, DIGEST OF CASE LAW ON THE UNCITRAL MODEL LAW ON CROSS BORDER INSOLVENCY (U.N. 2021).

[31] UNCITRAL Secretariat, *Status: UNCITRAL Model Law on Cross-Border Insolvency (1997)*, U.N., https://uncitral.un.org/en/texts/insolvency/modellaw/cross-border_insolvency/status.

constitutional guarantees." International cooperation will be promoted only when the public policy exception is narrowly interpreted, but domestic interest will be protected when this exception is widely interpreted. The use of phrase 'manifestly contrary' in public policy exception reflects its narrow interpretation; however, by omitting this phrase, countries can broaden their interpretation of public policy exception.

Article 6 of the UNCITRAL Model Law enacts the 'public policy exception' in the following manner:

> *"Nothing in the present Law prevents the court from refusing to take an action governed by the present Law if the action would be manifestly contrary to the public policy of this State."*

Article 6 of the UNCITRAL Model Law states that recognition of foreign insolvency proceedings can be refused if it is "manifestly contrary" to the public policy of the state considering the recognition.[32] Public policy is generally a broad term. However, the added prefix 'manifestly' reflects the intention of the drafter of model law to interpret it narrowly, viz, in exceptional and limited circumstances.[33] When considering recognition applications, *The Guide* recommends a narrow interpretation of public policy, reserving its use for fundamental points of law, specifically those with constitutional importance of enacting state.[34] It cautions against a broad application in the realm of international cooperation, warning that

[32] UNCITRAL Guide, *supra* note 29, at 5.
[33] Neil Hannan, *supra* note 22, at 4.
[34] Neil Hannan, *supra* note 22, at 4.

such an approach could dilute the very essence of the public policy exception, stripping it of its intended impact. *'What qualifies as a matter of fundamental importance?'* is truly in the eye of the beholder. *The UNCITRAL Model Law on Cross-Border Insolvency: The Judicial Perspective* suggests that the heart of this decision beats within the constitutional and legal veins of the receiving state. The UNCITRAL Judicial Perspective details six key cases to elucidate the concept of public policy exception concept.

In the *re Ephedra Products Liability Litigation case* involving the U.S. and Canada, the core issue was Canada's inability to conduct jury trials, which are constitutionally mandated in the U.S. This situation led to arguments in U.S. courts that Canada's incapacity represented a violation of U.S. public policy. Nonetheless, the Southern District Court of New York (SDYN) adopted a narrow interpretation and declined to trigger the public policy exception. The court determined that *"despite the constitutional significance of jury trials in the United States, the procedures in Canada still provided claimants with a fair and impartial hearing. This compliance with fair process standards, even in the absence of a jury trial, was deemed sufficient under the equivalent provisions of U.S. law related to Article 6"*, thereby obviating the need for the public policy exception.[35]

In the second case, *re Gold and Honey*, involving the U.S. and Israel, the U.S. initiated bankruptcy proceedings against a corporate debtor, leading to an automatic stay under Article 20 of the model law. At the same time, a receivership order was issued by Israel. Subsequently, there was an attempt to obtain recognition of the Israeli proceedings in the U.S. court.

[35] Re Ephedra Products Liability Litigation, 349 B.R. 333 (SDNY 2006).

However, recognition was denied on two grounds: firstly, the Israel proceedings did not meet the criteria for a collective proceeding outlined in Chapter 15; and secondly, the receivership order violated the United States's automatic stay. The court deemed this violation as a breach of a fundamental insolvency policy of U.S. It held that, *"granting recognition would severely hinder United States bankruptcy courts' abilities to carry out two of the most fundamental policies and purposes of the automatic stay – namely, preventing one creditor from obtaining an advantage over other creditors, and providing for the efficient and orderly distribution of a debtor's assets to all creditors in accordance with their relative priorities."*[36]

In the case of *re Zetta Jet Pte. Ltd,* which involved a dispute between the U.S. and Singapore, the Singapore Court issued a moratorium to halt proceedings. However, this stay order was disregarded by the U.S. court, which continued with further actions in the U.S. proceedings.[37] When an application for recognition was brought before the Singapore Court, a departure from previous precedents occurred.[38] Traditionally, contravening a stay order was seen as a violation of public policy and grounds for refusal of recognition.[39] Surprisingly, the Singapore court took a different stance. Instead of outright refusal, it granted *limited recognition*. The decision enabled the initiation of proceedings to challenge or overturn the injunction issued in Singapore. This innovative approach was interpreted as either a modification of recognition under Article 17, Paragraph 4 of the model law,

[36] Re Gold and Honey Ltd., 410 B.R. 357 (Bankr. E.D.N.Y. 2009).
[37] Re Zetta Jet Pte Ltd 16 (SGHC 2018).
[38] Re Gold and Honey, *supra* note 37.
[39] *Id.*

or as a form of relief under Article 21, Paragraph 1 of the model law.[40] However, the Singapore court later went on to recognize the United States as the corporate debtor's Centre of Main Interest ("**COMI**"). In doing so, it concluded that *"prior actions that contravened the Singapore injunction did not rise to the level of a public policy violation that would preclude recognition."*

The fourth case, *re Toft*, involved a dispute between the U.S. and Germany. This case was adjudicated by the Southern District Court of New York ("**SDNY**") wherein U.S. courts were asked to recognize German insolvency proceedings. The German courts had issued a 'mail interception order' against a debtor who was not cooperating, an order that courts in England upheld. Nonetheless, when it came to implementing the 'mail interception order' from Germany, the U.S. courts opted not to enforce it, invoking the public policy exception as outlined in section 1506 of the Bankruptcy Act. The U.S. court held *"the relief sought exceeded the traditional limits on the powers of a trustee in bankruptcy under United States law and providing such relief without notice to the debtor would also be contrary to United States law."* Consequently, the request for ex parte relief was refused, determining it to be fundamentally at odds with U.S. public policy.[41]

In the fifth case, *Re Creative Finance Ltd.*, which concerned proceedings between the U.S. and the British Virgin Islands, the U.S. court was approached with a plea to acknowledge insolvency proceedings initiated in the British Virgin Islands.[42] The argument presented was that these proceedings were initiated in bad faith, and thus recognition should

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[40] UNCITRAL Guide, *supra* note 28, at 5.
[41] Re Dr. Juergen Toft 453 B.R. 186 (2011).
[42] In Re Creative Finance Ltd, 543 B.R. 498 (Bankr. S.D.Y.N. 2016).

be refused under public policy grounds. Despite the court expressing disapproval towards the debtor's actions, it chose not to apply the public policy exception, citing the *lack of precedential support for refusing recognition based solely on the debtor's misbehaviour*.[43]

In the sixth case, *Ivan Cherkasov*, between the U.K. and Russia, the English Court initially recognized Russian insolvency proceedings. However, it later emerged that there was a lack of full and frank disclosure during those proceedings. Key factual details, especially those highlighting the case's politically sensitive nature, were not sufficiently presented to the U.K. Court, due to which the court was unable to apply the U.K. government's policy regarding non-assistance in criminal proceedings.[44] This policy aimed to protect the sovereignty, security, and public order of the United Kingdom. Consequently, the England and Wales High Court of Justice, Chancery Division, Companies Court ruled that "previously granted recognition order should be set aside ab initio due to material non-disclosure. When seeking recognition full and frank disclosure must be made to the court concerning the consequences of recognition on third parties who were not before the court, including from intended future applications enabled by recognition." *The court emphasized that it should have been fully informed to determine whether recognition would have been manifestly contrary to public policy, as stipulated in Article 6 of Schedule 1 to the Cross-Border Insolvency Regulations* (CBIR) *(Article 6 MLCBI).*[45]

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[43] Nordic Trustee A.S.A. v. OGX Petroleo e Gas S.A, 121 Bus. L.R (2016).
[44] Ivan Cherkasov, William Browder, Paul Wrench v. Nogotkov Kirill Olegovich, The Official Receiver of Danny ca 789 Bus. L.R (2018).
[45] Cross Border Insolvency Regulation, 1030 (2006).

As reflected in the UNCITRAL *Judicial Perspective* text, these six cases illustrate six approaches for invoking or refusing the public policy exception. It's like a roadmap for judges interpreting this exception. Generally, the exception shouldn't be invoked simply due to differences in legal systems if foreign proceedings are conducted fairly.[46] However, it can be used to refuse relief that doesn't align with the fundamental policies of domestic jurisdiction.[47] It can be invoked when there is a breach of an injunction or moratorium.[48] However, this exception cannot be invoked retrospectively to challenge acts of prior foreign proceedings.[49] Full and frank disclosure in recognition application and good faith can also shape a public policy requirement.[50] These instances attempt to form a foundational skeleton of what constitutes 'manifestly contrary to the public policy' prominently known as the 'public policy exception'.

III. ENACTMENT OF PUBLIC POLICY EXCEPTION BY UNCITRAL MODEL LAW COUNTRIES

In this part, the discussion centers on how different countries have incorporated the public policy exception into their legal frameworks. Countries that adhere to the model law's approach by incorporating the term *'manifestly'*, aligning with the principles of Modified-Universalism, are enumerated in subpart A. Conversely, subpart B lists countries that have adopted a broader interpretation of this exception, deliberately avoiding the

[46] Re Ephedra Products Liability Litigation, 349 BR at 333, 335 (SDNY 2006).
[47] Re Toft, *supra* 42, at 8.
[48] Re Gold and Honey, s*upra* 37, at 7.
[49] Re Zetta, *supra 38*, at 7.
[50] Ivan Cherkasov, *supra 45*, at 8.

use of *'manifestly'*, thus broadening the scope of their public policy exception within their legal frameworks by maintaining a territorialistic stance.

A. COUNTRIES FOLLOWING MODIFIED UNIVERSALISM APPROACH IN PUBLIC POLICY EXCEPTIONS

Before exploring the adoption of the Modified-Universalism principle concerning the public policy exception by UNCITRAL member nations, it is essential to acknowledge the *European Insolvency Regulation* ("**EIR**") *of 2000*.[51] It is the second critical international framework, after the Model Law, 1997 for addressing cross-border insolvencies within the European region. This regulation was updated with the *EIR Recast* in 2015.[52] Notably, within Chapter II, Article 33 of the EIR Recast, the legislation articulates a public policy exception, uniquely qualifying it with the term 'manifestly'.[53]

> *"Any Member State may refuse to recognise insolvency proceedings opened in another Member State or to enforce a judgment handed down in the context of such proceedings where the effects of such recognition or enforcement would be manifestly contrary to that State's public policy, in particular its fundamental principles or the constitutional rights and liberties of the individual."*

[51] European Council Regulation 1346/2000, 2000 O.J. L 160.
[52] Council Regulation No 1346/2000, 2000 O.J. L 160.
[53] Regulation 2015/848, 2015 O.J. L 141.

United States of America: In the global landscape, the U.S. has emerged as a leading nation in regulating cross-border insolvencies, particularly with the introduction of Chapter 15 in its Bankruptcy Code of 1978. This inclusion was facilitated by the Bankruptcy Abuse Prevention and Consumer Protection Act, 2005 which replaced Section 304.[54] Specifically, Chapter 15, Sub-chapter I, Section 1506, addresses the public policy exception, stating:

> *"Nothing in this chapter prevents the court from refusing to take an action governed by this chapter if the action would be manifestly contrary to the public policy of the United States."*

Canada: In 2005, Canada and the United States incorporated the Model Law 1997 into their legal systems to manage cross-border insolvency issues. This adoption is enumerated in two key legislations: the Bankruptcy and Insolvency Act, 1985 and the Companies Creditors Arrangement Act, 1985.[55] Both acts include a provision for a public policy exception, uniformly articulated in Part IV, section 61 (2) of the Companies' Creditors Arrangement Act and Part XIII, section 284 (2) of the Bankruptcy and

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[54] *11 U.S.C. § 1506 - Public policy exception,* (Apr. 20, 2005).

[55] Bankruptcy and Insolvency Act, R.S.C. 1985, c. B-3, https://laws-lois.justice.gc.ca/eng/acts/B-3/page-36.html#h-28988; Companies' Creditors Arrangement Act, R.S.C. 1985, c. C-36, https://www.laws-lois.justice.gc.ca/eng/acts/C-36/.

Insolvency Act, stating that courts have the discretion to refuse actions that would contravene public policy:

> *"Nothing in this Part prevents the court from refusing to do something that would be contrary to public policy."*

In North America, the United States is a prominent proponent of the model law, including its public policy exception as specified in Article 6.[56] The American judiciary has set a global standard in the interpretation and evolution of this exception.[57] On the other hand, Canada's version of the public policy exception, despite its seemingly broad language, has seen a narrower interpretation by Canadian courts, in line with the directives provided in the UNCITRAL Guide.[58]

South Africa: South Africa took early steps to align its insolvency laws with the global standards set by the Model Law, 1997 by introducing the Cross-Border Insolvency Act in 2000.[59] Within this act, the public policy exception is articulated in Chapter I, Section 6, incorporating the

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[56] Michael A. Garza, *When is Cross Border Insolvency Recognition Manifestly Contrary to Public Policy,* 38 Fordham INT'L L.J. 1587 (2015).
[57] *Id.*
[58] Explanatory Memorandum, Cross-Border Insolvency Bill 21 Cth (2008); Ackers v. Deputy Commissioner of Taxation 57 (FCAFC, 2014).
[59] Cross Border Insolvency Act 42 of 2000, https://www.gov.za/sites/default/files/gcis_document/201409/a42-000.pdf.

term 'manifestly' in a manner that closely reflects Article 6 of the Model Law,[60] as outlined below:

> *"Nothing in this Act prevents the court from refusing to take an action governed by this Act if the action would be manifestly contrary to the public policy of the Republic."*

Australia: Following the example set by South Africa, Australia has also legislated the Cross-Border Insolvency Act of 2008, aligning with the 1997 Model Law principles. The act integrates certain aspects of the model law with adjustments for the domestic legal environment. It attaches the Model Law, 1997 within Schedule 1.[61] This annexure serves as a reference for provisions not explicitly enacted in the act. Although the act itself does not expressly detail the public policy exception, this exception is accessible by referencing Article 6 in Schedule I, as indicated below:

> *"Nothing in the present Law prevents the court from refusing to take an action governed by the present Law if the action would be manifestly contrary to the public policy of this State."*

[60] *Id.*
[61] *Cross Border Insolvency Act 2008* (Cth).

United Kingdom: The UK incorporated the 1997 Model Law via the Cross-Border Insolvency Regulations of 2006.[62] The public policy exception is specified in Article 6, found in Schedule 1 of this regulation, and distinctively uses the word 'manifestly' in its phrasing.[63] The provision is enacted as follows:

> *"Nothing in this Law prevents the court from refusing to take an action governed by this Law if the action would be manifestly contrary to the public policy of Great Britain or any part of it."*

B. COUNTRIES FOLLOWING TERRITORIALISTIC APPROACH IN PUBLIC POLICY EXCEPTIONS

Japan: Japan became the first Asian country to align its laws with the contemporary Model Law, 1997, by amending its existing insolvency laws and enacting the Recognition of and Assistance for Foreign Insolvency Proceedings Act, 2000.[64] Article 21, clause (iii) of this act outlines the requirements for recognizing foreign insolvency proceedings.[65] It reveals that Japan has adopted the "public policy exception" as outlined in Article 6 of the Model Law but does not include the word "manifestly", as highlighted below:

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[62] The Cross-Border Insolvency Regulation 2006, https://www.legislation.gov.uk/uksi/2006/1030/made.

[63] The Cross-Border Insolvency Regulation 2006, https://www.legislation.gov.uk/uksi/2006/1030/contents/made.

[64] Gaikoku tosan syonin enjo ho (Recognition of and Assistance for Foreign Insolvency Proceedings Act) Law No. 129 of 2000); Hideo Horikoshi, *Guide to Japanese Cross-Border Insolvency Law*, 9 LAW & BUS. REV. AM. 725 (2003), https://scholar.smu.edu/cgi/viewcontent.cgi?article=1917&context=lbra.

[65] *Id.*

> *"Where it is contrary to public policy in Japan to render a disposition of assistance for the foreign insolvency proceedings pursuant to the provisions of the following Chapter."*

Republic of Korea: Following Japan, South Korea became the second Asian nation to embrace cross-border insolvency reform by incorporating the 1997 Model Law. This was achieved through the enactment of the Debtor Rehabilitation and Bankruptcy Act in 2005, officially adopted in 2006.[66] Part V of the aforementioned act addresses cross-border insolvency issues, with Article 632, section 2 detailing the conditions under which a court may reject a request to recognize foreign bankruptcy proceedings.[67] Specifically, section 2(3) introduces the "public policy exception" in a way that diverges from Article 6 of the Model Law, notably excluding the term "manifestly", as shown below:

> *"Where approving the foreign bankruptcy procedures is contrary to the good public morals and social order of the Republic of Korea."*

Singapore: Singapore joined as the 42nd nation worldwide to embrace the 1997 Model Law through Sections 251-253 in Part 11 of the Insolvency, Restructuring, and Dissolution Act of 2018. This act, together

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[66] Debtor Rehabilitation and Management Act, Act No. 7428, Mar. 31, 2005, amended by Act No. 15158, Dec. 12, 2017, https://elaw.klri.re.kr/eng_service/lawViewTitle.do?hseq=46315.
[67] *Id.*

with its Third Schedule, outlines Singapore's adaptation of the model law.[68] Notably, within Schedule III, Article 6 codifies the public policy exception, distinctively leaving out the word 'manifestly' in its formulation:

> *"Nothing in this Law prevents the Court from refusing to take an action governed by this Law, if the action would be contrary to the public policy of Singapore."*

Myanmar: Myanmar recently reformed its insolvency law by replacing the Yangon Insolvency Act, 1909 and the Myanmar Insolvency Act, 1920 to introduce the Insolvency Act, 2020. Part X of this act addresses cross-border insolvency. Within this part, Division 2 outlines general provisions, with section 374 specifically addressing the public policy exception, notably without including the word "manifestly".[69] It is enacted as follows:

> *"A Court which has jurisdiction under this Part may refuse an application if it would be contrary to the public policy of the Union."*

In analyzing how the public policy exception is framed within the legislation of countries like Japan, the Republic of Korea, Singapore, and Myanmar, it becomes clear that these nations have deliberately omitted the term "manifestly" from Article 6 of the Model Law, 1997. The creators of the model law intended for the public policy exception to be applied

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[68] Insolvency, Restructuring and Dissolution Act 2018 (Sing.), https://sso.agc.gov.sg/Act/IRDA2018?ProvIds=P111-#pr251-.
[69] Pyidaungsu Hluttaw Law No. 01/2020, § 374 (2020).

restrictively and exceptionally. They inserted the word "manifestly" to convey this intention. However, by omitting this word, these countries retain broad discretionary powers, which could be leveraged to their economic advantage. The omission of "manifestly" also indicates that these countries have reservations about fully embracing the modified Universalism model. The Asian version of the model law is ***"Quasi Modified-Universalistic"*** in nature. In contrast, the Modified Universalism-based model law has been formally adopted in letter, but its spirit aligns more closely with the principles of Territorialism.

IV. EXAMINING THE GROUNDS FOR GRANTING AND REFUSING THE PUBLIC POLICY EXCEPTION

The UNCITRAL Judicial Perspective failed to explain the phrase 'public policy exception.' Still, it lists few cases that laid the foundation for understanding this concept.[70] However, this was insufficient for shaping this exception. The lack of precedents for interpreting public policy exception was seen in the *Re Legend International Holdings case*, where an endeavour to employ this exception to dispute the recognition granted by the U.S. under Chapter 11 proceeding was unsuccessful in an Australian court.[71] Highlighting the judiciary's reluctance, the Legend Court marked that hesitation in applying the public policy exception may be because of lack of precedent in this area. Therefore, it is crucial to examine more cases

[70] Michael A. Garza, *supra* 57, at 10.
[71] Indian Farmers Fertiliser Coop. Ltd. v. Legend Int'l Holdings Inc. [ARBN 120 855 352] [2016] VSC 308.

where the public policy exception has been applied, whether in a broad or narrow context, to understand its application and implications better.

Wide interpretation & invoking the public policy exception

Globally, the U.S. judiciary is recognized as a leader in shaping and interpreting the public policy exception, mainly because acts as a central investment hub for multinational corporations. The predominance of U.S. in this area was reflected in the case of *Re Gold and Honey Ltd.*, ruled by the U.S. Bankruptcy Court in the Eastern District of New York, wherein an Israeli receiver's appointment was rejected claiming it to be an infringement of Chapter 11's automatic stay, deemed it directly in conflict with the U.S. public policy.[72] This decision drew criticism for its departure from the narrower interpretation advocated by Section 1506, diverging from the original intentions of the model law's drafters.

Invoking the public policy exception is not confined to the initial stages of refusing recognition, as there are precedents where it has also been applied at later stages to deny further relief. This flexibility in its application was evident in the *Re Toft case*, highlighted in *the Judicial Perspective*. In this case, the U.S. court declined to grant a mail interception order already authorized in the German insolvency proceedings. The U.S. court justified its decision by stating that *"it would fall within the public policy exception because it exceeded the traditional limits on the powers of a trustee under United States law, constituted relief that was banned by statute in the United States."* It was also

[72] Re Gold and Honey, s*upra* 37, at 7.

observed that such a request for relief on an ex parte basis would violate the public policy of the U.S.[73]

Another significant legal battle unfolded between the U.S. and Germany in the *Re Qimonda AG Bankruptcy Litigation, 2011*. The Bankruptcy Court for the Eastern District of Virginia had to determine "whether applying German insolvency law to deny patent licensees the protection of section 365 was manifestly contrary to the public policy of the United States?" The court held, *"The public policy favouring technological innovation is one of the most fundamental policies of the United States, and accordingly, the failure to protect this was manifestly contrary to the public policy of the United States."*[74] While examining Section 1506, the court also clarified the scope of the public policy exception to encompass three specific circumstances, offering illustrative examples that were not exhaustive:

(i) It was emphasized that the public policy exception cannot be invoked solely due to a conflict between foreign law and United States law without considering other factors. It was emphasized: *"Conflict between foreign law and United States law is a necessary prerequisite to the section 1506 analysis — for absent such conflict, the comity and public policy exception questions become moot."*

(ii) Public policy exception could be invoked to refuse any application which would ultimately frustrate the courts power to supervise the proceedings under Chapter 15 or if it would affect a statutory or constitutional right;

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[73] Re Toft, *supra* 42, at 8.
[74] Re Qimonda AG Bankruptcy Litigation 433 B.R. 547 (2011).

(iii) The public policy exception could be applied when the procedural fairness of a foreign proceeding is questionable and cannot be remedied by introducing additional protections.

In the *Re Vitro S.A.B. de CV case*, the U.S. Court of Appeals for the Fifth Circuit rejected a request to impose a stay on creditor's actions against non-debtor guarantors in a Mexican reorganization proceeding.[75] Although the court didn't directly assess if the reorganization plan contradicted U.S. public policy, it later found elements of the plan violated U.S. principles on protecting third-party claims in bankruptcy cases, rendering the plan unenforceable.[76]

Narrow interpretation & refusal to allow public policy exception

The Model Law, 1997 encourages a limited application of the public policy exception, suggesting it should be used only under extraordinary circumstances. In line with modified Universalism, this approach is demonstrated by cases where courts have refrained from invoking the exception. An example is the *Re Hartford Computer Hardware Inc. case*, decided by the Ontario Supreme Court in 2012, involving cross-border insolvency between the U.S. and Canada.[77] The Canadian court utilized Section 61(2) of the Companies Creditors Arrangement Act ("**CCAA**") to interpret the public policy exception narrowly. It concluded that there was no breach of public policy, allowing recognition of the U.S. proceedings as foreign main proceedings. This highlights the Canadian judiciary's commitment to

[75] Re Vitro, S.A.B. de C.V. 473 B.R. 117 (Bankr. N.D. Tex 2012).
[76] Michael A. Garza, *supra* 57, at 10.
[77] Re Harford Corp., 18 B.R. 536 (Bankr. S.D.N.Y. 1982).

limiting the use of the public policy exception, consistent with the principles outlined in the Model Law, 1997. Despite Canada's omission of the term "manifestly," it adheres to a narrow interpretation, reflecting the intentions of the model law.

In the case of *Re Millennium Global Emerging Credit Master Fund Limited*, the appellate court identified Bermuda as the COMI for the funds and rejected claims that the lower court breached U.S. public policy.[78] The court emphasized that the 'public policy exception' should be invoked only in clear violations against the most fundamental U.S. policies. It clarified that *"maintaining openness in courtrooms is not a fundamental public policy. While the right to public access to records and proceedings is generally supported, it is not an absolute right, and courts retain the discretion to restrict access to documents.*". Ultimately, the court concluded that no breach of public policy had occurred and dismissed the appeal.[79]

Similarly, in *Re ABC Learning Centres Limited n/k/a ZYX Learning Centres Limited & ABC USA Holdings Pty Ltd.,* a cross-border insolvency dispute between the U.S. and Australia, the Bankruptcy Court of Delaware was tasked with recognizing Australian insolvency proceedings, transitioning from voluntary administration to liquidation. Opponents argued it would unfairly favour certain creditors, violating the U.S. public policy. The court, however, recognized the Australian proceedings as a 'Foreign Main Proceeding' and dismissed the public policy exception,

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[78] Re Millennium Global Emerging Credit Master Fund Limited, 471 B.R. 342 (Bankr. S.D.N.Y. 2012).
[79] *Id.*

emphasizing that *"the public policy exception should be interpreted narrowly and dismissed concerns over unfair creditor treatment as inconsistent with the laws of both the United States and Australia."* [80]

In another case of *Re Gerova Financial Group Ltd.*, the argument that allowing a single creditor to initiate involuntary insolvency proceedings in the U.S. would conflict with public policy was rejected.[81] The court noted that *"a foreign nation's insolvency laws do not need to mirror perfectly with U.S. laws for recognition under Chapter 15"*. It also pointed out that Bermudan laws allow for insolvency initiation by a single creditor and do not limit post-application payments by the debtor. As a result, it concluded that recognizing the Bermudan proceedings did not violate U.S. public policy.[82]

The case of *Re Ashapura Minechem Ltd.*, decided by the U.S. District Court for the Southern District of New York in 2012, involved a dispute between India and the U.S. regarding recognising insolvency proceedings under India's Sick Industrial Companies Act, 1985. Despite objections from a creditor, the court upheld the recognition, citing the creditors' participation rights and the court-like powers of India's Board for Industrial and Financial Reconstruction ("**BIFR**"). The court found no grounds to believe that recognizing these proceedings would violate Chapter 15 or U.S. public policy.[83]

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[80] Re ABC Learning Centres Limited n/k/a ZYX Learning Centres Limited & ABC USA Holdings Pty Ltd., 445 B.R. 318 (Bankr. D. Del. 2011).
[81] Re Gerova Financial Group Ltd., 482 B.R. 86 (Bankr. S.D.N.Y. 2012).
[82] *Id.*
[83] Re Ashapura Minechem Ltd. 480 B.R.129 (S.D.N.Y. 2012).

In the 2008 case of *Re Klytie's Developments, Inc.*, heard by the U.S. Bankruptcy Court for the District of Colorado, the court confronted fraudulent activities involving an Israeli couple operating businesses in the U.S. and Canada.[84] Despite creditor objections, the court opted to recognize Canadian insolvency proceedings, stressing that *"the public policy exception was to be applied narrowly and should be invoked only when the most fundamental policies of the United States were at risk, referring to the legislative history of Chapter 15 and the decision in Ephedra."* [85] Additionally, the court underscored the importance of ensuring equal treatment for all defrauded investors, regardless of nationality or location.[86]

The Bankruptcy Court for the Southern District of Florida addressed the recognition of Brazilian insolvency proceedings in the case of *re Petroforte Brasileiro de Petroleo Ltda.* granted discovery relief against two debtors and several non-debtor entities, exceeding typical U.S. federal rules and Article 21(1)(d) of Model Law, 1997 limits. Despite objections citing potential infringement upon U.S. constitutional due process rights and exceeding judicial authority, the court deemed the Brazilian orders compatible with U.S. public policy, acknowledging procedural differences but not considering them fundamentally opposed to U.S. standards.[87]

In *re: North American Steamships Ltd.,* a case from the U.S. Bankruptcy Court for the Southern District of New York, Canadian proceedings were

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[84] Re Ephedra Products Liability Litigation, 349 B.R. 333 (S.D.N.Y. 2006), see also CLOUT case 765).
[85] Re Klytie's Developments, Inc., 383 B.R. 773 (Bankr. D. Colo. 2008).
[86] *Id.*
[87] Re Petroforte Brasileiro de Petroleo Ltda. 542 B.R. 899 (Bankr. S.D. Fla. 2015).

recognized as 'foreign main proceeding'.[88] The court reaffirmed *"There were no public policy grounds to deny recognition under 11 U.S.C. § 1506 [Art. 6]: the legislative history demanded a narrow construction that only applied to the most fundamental policies of the United States."*

In *Re Takata Corporation*, adjudicated by the District Court of Delaware, Takata and two other Japanese debtors applied for recognition of civil rehabilitation proceedings of Japan. Despite U.S. plaintiffs' objections on public policy grounds, due to differing claims procedures that could deny U.S. creditors rights and violate due process, the court dismissed these concerns and recognized the Japanese proceedings.[89] Further, In the case of *Re Agrokor DD*, the court found that differences in Croatian and English law regarding reorganization or liquidation priorities did not constitute a public policy violation, nor did potential deviations from the *pari passu principle* in future settlements.[90] Similarly, the public policy exception was not invoked in *Re Katsumi Iida*, underscoring a consistent judicial preference for a narrow application of this principle, in line with the Model Law, 1997 and the overarching intent to facilitate cross-border insolvency proceedings without compromising fundamental legal principles.[91]

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[88] Re North American Steamships Ltd., 267 (BCSC 2007).
[89] Re Takata Corporation, Case No. 17-11713 (BLS).
[90] Re Agrokor DD 64 Bus L.R. (2017).
[91] Re Katsumi Iida 377 B.R. 243 (B.A.P. 9th Cir. 2007).

V. OBSTACLES TO PUBLIC POLICY EXCEPTION IN CROSS-BORDER INSOLVENCY CASES

Inconsistency in enacting and interpreting the public policy exception is due to several factors. These include differences in national legal traditions and principles, varying the thresholds for what constitutes a violation of public policy across jurisdictions, and the subjective nature of interpreting what is fundamentally contrary to a nation's core values. Additionally, the lack of uniform global standards for applying this exception contributes to these disparities, as does the dynamic and evolving nature of public policy, which can change over time and be influenced by new legal precedents, societal values, and international relations. This complexity necessitates a careful, case-by-case approach by courts to reconcile international cooperation in insolvency proceedings with the protection of domestic legal principles.

In the United States, the federal judicial system introduces complexity to this scenario. U.S. bankruptcy courts interpret the public policy exception has frequently been criticized for its lack of consistency. This system is characterized by each circuit having its hierarchy of courts, including district courts, special courts, and courts of appeal. In bankruptcy cases, appeals from district court decisions are typically heard by the Bankruptcy Appeal Panel ("**BAP**"). Given the federal structure, courts in one circuit are not obligated to adhere to the precedents set by the courts of appeal, particularly the BAP, in another circuit. However, such decisions may carry persuasive value. As a result, there is variation in applying the public policy exception, and only cases of substantial importance are

considered for appeal to the U.S. Supreme Court. One proposed solution to mitigate this inconsistency is the establishment of a singular appellate authority for bankruptcy issues, alternatively assigning bankruptcy appellate jurisdiction to the federal circuit to ensure uniformity and predictability in bankruptcy proceedings.[92] Uniformity in interpreting public policy exception within the U.S. is the need of the hour, as it is the forerunners with the opportunity to shape cross-border insolvency laws.

The UNCITRAL texts set a high bar for invoking the public policy exception, stipulating that courts should exhaust other provisions before considering this route. This guideline ensures the exception is applied judiciously, underscoring the importance of a consistent and coherent approach. By integrating these considerations, the legal community can work towards harmonizing the application of the public policy exception, aligning it more closely with international standards and the protective instincts of domestic legal frameworks.

VI. CONCLUSION

"Public policy may provide a basis for refusing recognition but it may also be an unruly horse to ride."

~ Gerard McCormark[93]

The analysis of the public policy exception, as enumerated under article 6 of the Model Law, 1997 illuminates a significant dichotomy in its application and interpretation. After analyzing the enactment of this exception by the countries that have enacted their cross-border insolvency

[92] Neil Hannan, *supra* note 22, at 4.
[93] Gerard McCormark, *supra* note 9, at 3.

laws as per the guidelines of Model Law, 1997 it is observed that mostly Asian Jurisdictions have adopted a different approach. Model Law, 1997 is famous for embracing modified Universalism, which suggests narrow interpretation for this exception. However, Asian Jurisdictions, particularly Japan, the Republic of Korea, Singapore, and Myanmar has attempted to provide a wide scope of interpretation for this exception by omitting the word "manifestly". The authors have termed this practice as **"Quasi Modified Universalistic"** wherein countries are embracing Model Law, 1997 in letter, but in spirit they are deeply rooted in Territorialism to protect their economic interest. While protective of national interests, this approach risks fragmenting the legal landscape and complicates cross-border insolvency proceedings, ultimately calling into question the efficacy of the Model Law, 1997 in these jurisdictions. As the global economy continues to integrate and cross-border insolvency cases become more common, the tension between Universalism and Territorialism, as embodied in the interpretation and application of the public policy exception, will remain a pivotal area of debate and development in international insolvency law.