# JURISDICTION AND STRUCTURE OF THE BANKRUPTCY COURT

The power of a court is defined by its jurisdiction. Accordingly, the jurisdiction of a court should be based on the importance of the issues it must address, the need to enforce its orders, and the reliance placed on the soundness and finality of those orders by participants in the system. The jurisdiction of a court thus must be the form that follows the court's function. The function of the bankruptcy court is to provide a collective proceeding to treat *all* claims and interests in the property of a debtor's estate. The cost of administering these proceedings is borne by creditors. Principal goals of the bankruptcy process are to maximize the return to creditors and provide debtors with a fresh start or the ability to reorganize. A quick, efficient, and final determination of the claims and interests in property of the estate accomplishes these goals.

Granting bankruptcy courts broad jurisdiction so that they may quickly, efficiently, and finally resolve claims and interests in property of the estate is not a new idea.[1728] Questions about the scope of bankruptcy court authority, however, continue to plague litigants, adding cost and delay to a system that seeks to achieve speed, efficiency, and finality. All of the Commission's Recommendations on the structure of the bankruptcy court are designed to reduce the cost, delay, and redundancy that is inherent in the current system.

[1728] he 1970 Commission, in an effort to combine the cumbersome and costly bifurcated jurisdiction under the 1898 Bankruptcy Act, recommended the creation of a single bankruptcy court with full jurisdiction to dispose of bankruptcy cases. REPORT OF THE COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, Part I at 93-94 (1973). (Hereinafter cited as COMMISSION REPORT). Similarly, the House Bill (H.R. 8200) echoed these goals and proposed an Article III bankruptcy court. The House Report cited "forum shopping and jurisdictional litigation that have plagued the bankruptcy systems, the unfairness to defendants from 'jurisdiction by ambush,' and the dissipation of assets and the expense associated with bifurcated jurisdiction will be eliminated by the jurisdiction proposed by this bill." H.R. REP. NO. 95-595, at 49 (1977).

# RECOMMENDATIONS

### 3.1.1 *Establishing the Bankruptcy Court under Article III of the Constitution*

**The bankruptcy court should be established under Article III of the Constitution.**

### 3.1.2 *Transition to an Article III Bankruptcy Court*

**As of the enactment of legislation to establish an Article III bankruptcy court, sitting bankruptcy judges should be permitted to finish their current fourteen year terms. As vacancies are created through attrition (including expiration of current statutory term, appointment as an Article III judge, resignation, retirement prior to end of term for any reason, or death), Article III bankruptcy judges should be appointed by the President upon the advice and consent of the Senate to fill those positions. Sitting bankruptcy judges should be permitted to apply for any Article III judgeship positions while remaining on the bench. Nothing in the Recommendation will affect the length of the current term, salary, retirement benefits, or other attributes of sitting bankruptcy judges.**

**During the transition period, bankruptcy jurisdiction should be treated in the following manner: as Article III bankruptcy judges are appointed, the jurisdiction provisions under 28 U.S.C. §§ 1334 and 157 should be transferred on a district-by-district basis to the Article III bankruptcy judge sitting in that district. Consequently, bankruptcy jurisdiction would reside in the Article III bankruptcy judge, including the power to refer and withdraw cases and proceedings. While a district is without an Article III bankruptcy judge, the Judicial Council for that circuit should be authorized to: (1) determine the need for an Article III bankruptcy judge in that district, and (2) if necessary, designate an Article III bankruptcy judge from another district (within the circuit) to sit in that district. In the event the judicial council determines a need for an Article III bankruptcy judge and one has not yet been appointed to sit within that circuit, the Chief Justice, upon receiving a certificate of necessity from the chief judge of the circuit, should be authorized to designate an Article III bankruptcy judge from another circuit to fulfill the request.**

### 3.1.3 *Bankruptcy Appellate Process*

**The current system which provides two appeals, the first either to a district court or a bankruptcy appellate panel and the second to the U.S. Court of Appeals, as of right from final orders in bankruptcy cases should be changed to eliminate the first layer of review.**

### 3.1.4 *Interlocutory Appeals of Bankruptcy Orders*

**28 U.S.C. § 1293 should be added to provide, in addition to the appeal of final bankruptcy orders, for the appeal to the courts of appeals of interlocutory bankruptcy court orders under the following circumstances: (1) an order to increase or reduce the time to file a plan under section 1121(d); (2) an order granting, modifying, or refusing to grant an injunction or an order modifying or refusing to modify the automatic stay; (3) an order appointing or refusing to appoint a trustee, or authorizing the sale or other disposition of property of the estate; (4) where an order is certified by the bankruptcy judge that (x) it involves a controlling issue of law to which there is a substantial difference of opinion, and (y) immediate appeal of the order may materially advance resolution of the litigation, and leave to appeal is granted by the court of appeals; and (5) with leave from the court of appeals.**

### 3.1.5 *Venue Provisions under 28 U.S.C. § 1408*

**28 U.S.C. § 1408(1) should be amended to prohibit corporate debtors from filing for relief in a district based solely on the debtor's incorporation in the state where that district is located.**

**The affiliate rule contained in 28 U.S.C. § 1408(2) should be amended to prohibit a corporate filing in an improper venue unless such debtor's corporate parent is a debtor in a case under the Bankruptcy Code in that forum. Section 1408(2) should be amended as follows:**

> **(2) in which there is pending a case under title 11 concerning such person's affiliate, as defined in section 101(2)(A) of title 11, general partner, partnership, or a partnership controlled by the same general partner.**

**The court's discretionary power to transfer venue in the interest of justice and for the convenience of the parties should not be restricted.**

# DISCUSSION

The structure of a federal court establishes the constitutional limit on the "judicial power" exercised by the judge. A fundamental element of the separation of powers between the judicial branch and the other two branches of government is Article III's requirement that "[t]he judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish."[1729] Bankruptcy courts are not established under Article III of the Constitution. Instead, bankruptcy courts operate as "units" of the district court.[1730] As non-Article III courts, bankruptcy courts cannot exercise the "judicial power" of the United States.[1731]

The Supreme Court has recognized that not every adjudication constitutes an exercise of the "judicial power" of the United States.[1732] At what point a bankruptcy judge exercises the "judicial power" of the United States and is thus in violation of Article III is not easily discerned.[1733] The Supreme Court in *Marathon* held that a

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[1729] U.S. CONST. art. III, § 1.

[1730] 28 U.S.C. § 151 (1994) ("[i]n each judicial district, the bankruptcy judges in regular active service shall constitute a unit of the district court to be known as the bankruptcy court for that district. Each bankruptcy judge as a judicial officer of the district court, may exercise the authority conferred under this chapter with respect to any action, suit, or proceeding and may preside alone and hold a regular or special session of the court, except as otherwise provided by law or by rule or order of the district court.").

[1731] *See* Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 87 (1982) (holding that the 1978 Reform Act "has impermissibly removed most, if not all, of the 'essential attributes of the judicial power' from the Art. III district court, and has vested those attributes in a non-Art. III adjunct. Such a grant of jurisdiction cannot be sustained as an exercise on Congress' power to create adjuncts to Art. III courts.").

[1732] *Marathon*, 458 U.S. at 80 ("it is clear that when Congress creates a substantive federal right, it possesses substantial discretion to subscribe the manner in which that right may be adjudicated — including the assignment to an adjunct of some functions historically performed by judges. Thus *Crowell* recognized that Art. III does not require 'all determinations of fact [to] be made by judges,' [citation omitted] with respect to congressionally created rights, some factual determinations may be made by a specialized fact-finding tribunal designed by Congress, without constitutional bar").

[1733] A recent Supreme Court case — not in the bankruptcy context — held that "the judicial power of the United States" is exercised when a judge makes a "dispositive judgment." Plaut v.

non-Article III bankruptcy judge "cannot constitutionally be vested with jurisdiction to decide [a] state-law contract claim."[1734] Because bankruptcy judges had jurisdiction to hear and determine this type of claim, the Supreme Court held unconstitutional the broad grant of jurisdiction in the 1978 Reform Act.

In response to *Marathon*, Congress divided proceedings in bankruptcy cases into those over which a bankruptcy judge could preside and enter a final order (*i.e.*, those where the bankruptcy judge arguably was not exercising the "judicial power" of the United States, referred to in the judicial code as "core" proceedings) and those in which the bankruptcy judge could submit findings of fact and conclusions of law to the district court judge for entry of a final order (*i.e.*, those where the bankruptcy judge would be exercising the "judicial power" of the United States, commonly referred to as "noncore" proceedings). The resulting bifurcation of bankruptcy jurisdiction between these two types of proceedings has led to a great deal of needless cost, confusion and delay because the authority of the bankruptcy judge to enter a final order can often be disputed.

The Commission's Recommendation on the authority of the bankruptcy court would create a constitutionally sound structure and eliminate costly litigation over bankruptcy court authority. The appeals process Recommendation focuses on improving *stare decisis* and reducing the excessive cost and delay in the current appeals system. The Recommendation on venue eliminates place of incorporation or organization as a valid bankruptcy venue in favor of bankruptcy venue options in either the debtor's principal place of business or the location of principal assets.

### 3.1.1 *Establishing the Bankruptcy Court under Article III of the Constitution*

**The bankruptcy court should be established under Article III of the Constitution.**

The evolution of the bankruptcy court has not kept pace with the system's need for the efficient and final determination of bankruptcy and bankruptcy-related issues. How best to structure the bankruptcy court system in order to accomplish these goals has been debated twice since the 1970 Commission recommended the creation of an independent bankruptcy court with pervasive jurisdiction over all

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Spendthrift Farm, Inc., 514 U.S. 211, 219-20 (1995). For a discussion of the impact of this case on bankruptcy courts, see Richard Lieb, *Can a Bankruptcy Judge Constitutionally Hear and Determine a "Core" Proceeding*, 6 NORTON BANKR. L. ADV. 1 (June 1997) (arguing that in light of *Plaut* as well as other Supreme Court precedent since *Marathon*, core bankruptcy jurisdiction is unconstitutional and bankruptcy courts should be established under Article III).

[1734] *Marathon*, 458 U.S. at 87 n.40.

bankruptcy and bankruptcy-related matters.[1735] Both sides of the debate agreed that the bankruptcy court must have pervasive jurisdiction over all bankruptcy and bankruptcy-related matters in order to effectively and efficiently adjudicate bankruptcy cases and proceedings. The difference lay in what each side of this debate believed was necessary to achieve efficient and effective bankruptcy courts. During the congressional deliberations culminating in the 1978 Bankruptcy Reform Act, the House determined that expansive jurisdiction could only be granted to an Article III bankruptcy court.[1736] The Senate determined that expansive jurisdiction could be granted to a non-Article III court and therefore Article III status was unnecessary.[1737] The Senate view prevailed and Article III status was not granted to the bankruptcy courts under the 1978 Bankruptcy Reform Act.

The attempts in the 1970s and 1980s to increase the efficiency and enhance the reputation of the bankruptcy courts should be continued in the 1990s.[1738] It is not merely a matter of cosmetics or appearance. The present bankruptcy system comes into contact with more individuals and entities and handles more money than the rest of the federal court system combined.[1739] The soundness and efficiency of the bankruptcy system is therefore paramount. Two reforms will greatly enhance the efficiency and reliability of the present system. These reforms are (1) granting bankruptcy judges Article III status, and (2) giving the bankruptcy court unfettered, pervasive jurisdiction over any matter related to a case filed under the Bankruptcy Code.

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[1735] COMMISSION REPORT, at 90-91.

[1736] H.R. REP. 95-595, at 22 (1977).

[1737] S.2266, 95th Cong. (1978).

[1738] Over 25 years ago, Congressman Rogers of Colorado stated that "more people appear in our bankruptcy courts than in all other Federal courts combined. . . ." CONG. REC. H6215 (June 30, 1970). That statement was reiterated in hearings before Congressional subcommittees in the late 1970s when the present Bankruptcy Code was being considered by the Congress. His observation would carry more force today, particularly with the extraordinary increase over the past two decades or two of filings under the Code. The statement includes not only debtors filing under the various chapters of the Code but takes cognizance of the participation of creditors of all kind and other nondebtor parties. In fact, for most people who appear in federal court, their only exposure to the federal court system is the bankruptcy court.

[1739] This was true in 1977, when the House Report stated that over 254,000 bankruptcy cases were being filed annually. H.R. REP. 95-595, at 21 (1977). Over 1.2 million cases were filed in 1996. Similarly in 1977, Judge Conrad K. Cyr cited a caseload survey finding that bankruptcy cases pending at that time reflected in excess of $27 billion in assets and $42 billion in liabilities. *Id.* at Appendix I. No asset and liability estimates are available for cases pending today, but expanding the figures available in 1977 at the same rate as the bankruptcy caseload has expanded would result in approximate assets administered of $127 billion and liabilities of $198 billion.

These two reforms are inextricably intertwined. The Supreme Court has ruled that a grant by Congress of pervasive jurisdiction to a non-Article III court is unconstitutional. Thus, Article III status is a *sine qua non* for accomplishing the jurisdictional goal. At its most fundamental, an Article III bankruptcy court would permit service by bankruptcy judges during good behavior and bar any reduction of salary while in office. These are the only two requirements under Article III. There is no constitutional requirement that Article III bankruptcy judges be given the same treatment as other Article III judges. Matters of salary, pension, and color of judicial robes can be completely different from that prescribed for other Article III judges.

Article III status will also eliminate the need for procedural complexities and devices such as the core/noncore distinction that add a great deal of delay and expense to the current system. It will also eliminate the need for other jurisdictional requirements that have no bearing on the constitutionality of the current bankruptcy court such as mandatory withdrawal, mandatory abstention, and liquidation of personal injury claims. For example, proceedings involving the interpretation and application of a nonbankruptcy federal statute would not have to be kept from the bankruptcy judge. An Article III bankruptcy judge would be sufficiently similar to the federal district judge in ability and outlook that any doubts about the resolution of this type of litigation should be dispelled. Special rules for personal injury litigation would be unnecessary because jury trials could be retained as of right and they could occur in the bankruptcy court.

The key to efficiency in bankruptcy is speed and finality. Resources in bankruptcy are limited and creditors bear the costs of administration. Under the current core/noncore system, disputes over the jurisdiction of the court can take years. Extended litigation over the jurisdiction of the court with no determination on the merits of a dispute diminish the creditors' recovery. Resources that would otherwise be available to pay unsecured creditors and fund the debtor's ongoing operation are instead used to litigate the boundaries of bankruptcy court jurisdiction. The jurisdictional inefficiency of the system thus threatens two bedrock principles of bankruptcy: maximizing recovery for creditors and providing debtors with the ability to reorganize or obtain a fresh start.

The cost of uncertainty in the present system will also be eliminated if bankruptcy courts are established under Article III. The present system generates repetitious litigation over highly technical jurisdictional issues. Only sophisticated parties who can afford to litigate these issues obtain a determination of the bankruptcy court's power in certain circumstances. Parties in bankruptcy proceedings who can not afford to litigate these issues are left with uncertainty as to the bankruptcy courts' power. This uncertainty is costly, time consuming and alters negotiating leverage between the parties who can afford to litigate and those who cannot.

Article III status will also, in synergy with these reforms, promote the goal of achieving a high quality judicial system. Critics of the current system argue that bankruptcy judges are too debtor-oriented and as a result the system is too insular and self-referential. Article III status may address some of these concerns.[1740] Lifetime appointment may encourage and provide an incentive for high quality generalists who will bring a generalist perspective to the whole system to seek bankruptcy judge appointments.

The net result would be a more prestigious, more efficient court authorized to resolve quickly and completely all in a single setting the proceedings that come before it.

## A. Background on Structure of the Bankruptcy Courts

### 1. Bankruptcy Act of 1898

Under the Bankruptcy Act of 1898,[1741] the jurisdictional scheme of the referees in bankruptcy (who later became bankruptcy judges) to decide contested proceedings was divided between summary and plenary jurisdiction. Bankruptcy referees could preside over contested proceedings only if summary jurisdiction existed.[1742] If summary jurisdiction was lacking, only plenary jurisdiction existed and the contested proceeding had to be resolved in the nonbankruptcy forum in which the debtor could have brought suit had there been no bankruptcy. The resulting divided jurisdiction led to delay and increased expense to the estate, the creditors, and the third party litigants.

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[1740] H.R. REP. 95-595, at 22 (1977). The House Report recognized that [a] life-tenured judgeship is a more prestigious position than a term judgeship. The Department of Justice recently observed that the more prestigious the position, the better the judges that will be attracted." The House Report concluded by stating that "[b]ankruptcy litigants are entitled to no less qualified judges than other federal litigants." *Id.*

[1741] Act of July 1, 1898, ch. 541, 30 Stat. 544 (as amended) (repealed 1979).

[1742] Act of July 1, 1898, ch. 541, 30 Stat. 544 (as amended) (repealed 1979). Summary jurisdiction, *i.e.*, jurisdiction that allowed a bankruptcy judge to decide a dispute, existed (1) if the proceeding involved property in the actual or constructive possession of the bankruptcy court; (2) if the third party consented to the exercise of summary jurisdiction by the bankruptcy court; or, (3) over a counterclaim asserted by the third party. Within these categories, subgroups were formed. For example, consent was divided into actual and implied consent; failure to object timely to the exercise of such jurisdiction constituted implied consent. It was clear that such jurisdiction existed over a compulsory counterclaim but it was not clear whether it existed over a permissive counterclaim even to the last days of the Bankruptcy Act. Charles Seligson & Lawrence P. King, *Jurisdiction & Venue in Bankruptcy*, J. NAT. ASS'N REF. IN BANKR. (April- July, 1962).

The rather routine process that developed under the Act when a third party was sued by the bankruptcy trustee was as follows:

1. Suit filed in the bankruptcy court.
2. Timely objection to the summary jurisdiction of that court.
3. Decision by the bankruptcy judge.
4. Appeal to the district court.
5. Decision by the district court.
6. Appeal to the court of appeals.
7. Decision by the court of appeals.
8. Petition for certiorari.
9. Denial of petition for certiorari.

No matter how the Court of Appeals decided the issue, it was still only a decision on the jurisdictional issue. While it may have taken seconds to read the above items, that time translated into months and years in the process before the parties could turn to the merits either in the bankruptcy court or the nonbankruptcy forum, which was the court where the debtor could have sued had there been no intervening bankruptcy. The cost of litigation is an administrative expense and is borne by unsecured creditors. The delay inherent in protracted litigation also harms the debtor's chances of reorganizing successfully or in the case of an individual, obtaining a fresh start.

The system just described was, very obviously, inefficient, time consuming and expensive. As bankruptcy filings increased and became more complicated in the 1950s and 1960s, the summary and plenary structure became virtually unworkable.[1743] The unworkability of this system was one of the main reasons behind the creation of the Commission on the Bankruptcy Laws of the United States in 1970.[1744]

2. Commission on the Bankruptcy Laws of the United States

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The principal objective of the 1970 Commission was to streamline the bankruptcy process in order to make it more efficient.[1745] This goal was achieved in

[1743] H.R. REP. 95- 595, at 21 (1977).

[1744] Act of July 24, 1970, Pub. L. No. 91-354, 84 Stat. 468.

[1745] The inefficiencies arising out of the Act's distinction between summary and plenary jurisdiction led the 1970 Commission to conclude that:

> The most serious objection to the division of jurisdiction is the frequent, time-consuming, and expensive litigation of the question whether the bankruptcy court has jurisdiction of a particular proceeding. As Professor MacLachlan has observed, "When a 'summary' proceeding in the bankruptcy court is appropriate and when a plenary suit is required is one of the most involved and controversial questions in the entire field of bankruptcy."

part by granting broad jurisdiction to the newly-created bankruptcy courts over all property of the debtor and over all proceedings "arising out of any bankruptcy or rehabilitation case."[1746] In proposing a broad grant of jurisdiction to the bankruptcy courts in an effort to solve the problems that arose out of divided jurisdiction, the Commission Report concluded:

> A comprehensive grant of jurisdiction to the bankruptcy courts over all controversies arising out of any bankruptcy or rehabilitation case would greatly diminish the basis for litigation of jurisdictional issues which consumes so much time, money, and energy of the bankruptcy system and of those involved in the administration of debtors' affairs. It would foster the development of a more uniform, cohesive body of substantive and procedural law which would be applicable to the administration of estates under the Bankruptcy Act. The withdrawal from state and federal district courts of jurisdiction of the so-called plenary proceedings, when coupled with the establishment of uniform federal standards and rules, as proposed by the Commission for adoption and application in lieu of the diverse state laws governing debtors' and creditors' rights, should eliminate a source of uncertainty and division of authority which has characterized bankruptcy law.[1747]

Two very basic propositions emanated from the work of the 1970 Commission. One was a recognition that the bankruptcy judge required the legal authority to dispose of any disputes "arising in" or "related to" a pending bankruptcy case.[1748] The second

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> Generally, time is on the side of the defendant. If he can subject the plaintiff trustee to the necessity of suing in another court, he can gain the additional time which that necessity imposes on the trustee. Similarly, the extra expense entailed by the estate when the trustee is forced to sue elsewhere gives his adversary a counter for bargaining with him. Even when the trustee is likely to prevail in a contest over whether the bankruptcy court has jurisdiction, the adversary by merely litigating the issue of jurisdiction may gain most of the advantages he would get if he won on the jurisdictional issue, *viz*, time and bargaining leverage against the trustee. Thus, the adversary has a strong incentive to press his jurisdictional objections to the bankruptcy court's jurisdiction up through the appellate courts.

COMMISSION REPORT, *supra* note 1728, at 90.

[1746] *Id.*

[1747] *Id.*, at 91.

[1748] The Commission Report, over the dissent of one of its nine members, proposed granting bankruptcy judges the power "to determine most controversies arising from cases commenced" under the new bankruptcy act. COMMISSION REPORT, *Id.* at 85. The jurisdiction of the newly created bankruptcy court proposed by the Commission extended to "determination of all controversies"

was the necessity for upgrading the bankruptcy court in order to attract the highest level of qualified persons possible to that bench.[1749] The first point was accomplished in the Commission Report by granting to the bankruptcy court jurisdiction over all proceedings "arising in" or "related to" a bankruptcy case.[1750] The second, even complementary to the first, was to have the bankruptcy judges appointed by the President with the advice and consent of the Senate.[1751] At this time, the Commission was not concerned about any issue of constitutionality because it felt that Congress had the constitutional power to create such a court with such expanded jurisdiction.[1752]

### 3. Bankruptcy Reform Act of 1978[1753]

In the hearings during the 1970s before the House Subcommittee on the bills that were introduced to carry forward the Commission's recommendations, there was no dispute as to the wisdom of the recommendation to give the bankruptcy court pervasive jurisdiction over disputed matters. Consistent with the recommendation of the 1970 Commission, Congress incorporated a broad grant of jurisdiction to the

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arising out of a case commenced under the proposed act. Proposed Bankruptcy Act of 1973, § 2-201.

[1749] The Commission Report recommended extending the term for referees from six years to fifteen years, in order to make the position far more attractive to appointees. COMMISSION REPORT, *supra* note 1728, at 94-95.

[1750] Proposed Bankruptcy Act of 1973, § 2-201.

[1751] *Id.* §§ 2-201, 2-103, 1-104. Under the 1898 Act, bankruptcy judges were appointed by the district court for a term of six years.

[1752] On the subject of such a broad grant of jurisdiction to the newly-created bankruptcy courts, the Commission Report concluded

> The constitutionality of a grant of jurisdiction in such comprehensive terms should not be subject to any serious doubt. The jurisdictional grants to the court of bankruptcy by the Acts of 1841 and 1867 were almost as extensive, and the Supreme Court gave the provisions of those Acts a generous construction and approval of their constitutionality. There appears to be no reason why Congress cannot in the exercise of its power under the Bankruptcy Clause of the Constitution confer jurisdiction over all litigation having a significant connection with bankruptcy.

COMMISSION REPORT, *supra* note 1728, at 92.

[1753] Pub. L. No. 95-598, 92 Stat. 2549 (1978).

bankruptcy courts into the legislation it drafted.[1754] There was, however, a recognition that a constitutional problem might be created by granting such broad jurisdiction to a non-Article III court.[1755] When issues of constitutionality were raised, the House granted Article III status to bankruptcy judges in order to put those concerns to rest.[1756] A House bill was introduced to avoid any constitutional issue by creating the bankruptcy court under Article III of the Constitution.[1757] In fact, H.R. 8200 eventually passed the House of Representatives and would have passed the Senate had a hold not been placed on it by a single Senator.[1758]

In contradistinction, the Senate bill did not confer Article III status on bankruptcy judges.[1759] Despite this significant difference, the Senate bill still conferred the same broad jurisdiction over proceedings in bankruptcy cases as the House version.[1760] The bill that became the Bankruptcy Reform Act of 1978 retained the

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[1754] 1 COLLIER ON BANKRUPTCY ¶ 1.03[1], at 1-9 (Lawrence P. King et al. eds., 15th ed. 1996).

[1755] H.R. REP. 95-595, at 36-39 (1977). The House Report discusses the constitutional requirements of an independent bankruptcy court with a broad grant of jurisdiction over bankruptcy cases, concluding

> [i]n sum, the Constitution suggests that an independent bankruptcy court must be created under Article III. Article III is the constitutional norm, and the limited circumstances in which the courts have permitted departure from the requirements of Article III are not present in the bankruptcy context. Even if they were present, the text of the Constitution and the case law indicate that a court created without regard to Article III most likely could not exercise the power needed by a bankruptcy court to carry out its proper functions. In view of Congress' independent obligation and the Congressional oath to support the Constitution, the decision on this issue should not simply be thrown to the courts. *Congress should establish the proposed bankruptcy court under Article III, with all of the protection that the Framers intended for an independent judiciary.*

*Id.* at 39 (emphasis added).

[1756] H.R. 8200, 95th Cong. (1978).

[1757] *Id.*

[1758] App. Vol. 2 COLLIER ON BANKRUPTCY xxii (15th ed. Matthew Bender).

[1759] S. 2266, 95th Cong. (1978).

[1760] *Id.* Indeed, the Senate Report confirmed that one of the principle goals of revising the Bankruptcy Act was "the need to enlarge the jurisdiction of the bankruptcy court in order to eliminate the serious delays, expense and duplications associated with the current dichotomy between summary and plenary jurisdiction, a wasteful remnant of the referee system left over from the pre-Chandler Act era." S. REP. NO. 939, 95th Cong., 2d Sess. 14-15 (1978).

pervasive jurisdiction but provided for bankruptcy judges to be appointed by the President with the advice and consent of the Senate for a term of 14 years.

4. *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*[1761]

In *Marathon*, the Supreme Court held that the grant of jurisdiction to bankruptcy courts under the 1978 Bankruptcy Reform Act was an unconstitutional violation of Article III.[1762] A plurality of the Court held unconstitutional the jurisdictional framework of the 1978 Reform Act because it authorized bankruptcy judges (who, as adjuncts to the district courts, lacked Article III salary and tenure protections) to hear state-law claims asserted in a bankruptcy proceeding.[1763]

All of Title II of the 1978 Bankruptcy Reform Act (particularly section 1471(c)) was found unconstitutional by the *Marathon* court because it granted too much jurisdiction to a non-Article III court.[1764] As enacted originally, Congress expressly provided in section 1471(c) and the remainder of Title II that there was to be *no limitation* of the bankruptcy court's authority. For example, 28 U.S.C. § 1480 retained the right to jury trial as it existed on September 30, 1979, which was to be exercised in the bankruptcy court.[1765] Section 1481 gave the bankruptcy court the powers of a court at law, equity and admiralty, but it could not enjoin another court, or punish for criminal contempt not committed in its presence or that warranted incarceration.

Under *Marathon*, the lack of Article III status for bankruptcy judges proved fatal to the portions of the 1978 Reform Act that attempted to resolve the jurisdictional problems under the Bankruptcy Act by granting broad jurisdiction to bankruptcy judges.

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[1761] 458 U.S. 50 (1982).

[1762] *Id.* at 87. ("We conclude that § 241(a) of the Bankruptcy Act of 1978 has impermissibly removed most, if not all, of the 'essential attributes of the judicial power' from the Article III district court, and has vested those attributes in a non-Article III adjunct. Such a grant of jurisdiction cannot be sustained as an exercise of Congress' power to create adjuncts to Art. III courts.")

[1763] *Id.* at 56.

[1764] *Id.*

[1765] *See* 28 U.S.C. § 1869, as amended by section 243 of the Reform Act, Pub. L. No. 95-598 (1978).

### 5. Bankruptcy Amendments and Federal Judgeship Act of 1984[1766]

In all the legislation, proposed and enacted up until 1984, there were no provisions regarding permissive or mandatory withdrawal, permissive or mandatory abstention, delegation of personal injury actions to another court, or, obviously, any reference to core and noncore proceedings. The Bankruptcy Amendments and Federal Judgeship Act of 1984 ("BAFJA") was Congress' legislative response to the Supreme Court's decision in *Marathon*.[1767] BAFJA divides the authority of the bankruptcy court into core and noncore proceedings in order to buttress the constitutionality of the system.[1768] As compared with the distinction under the Act between summary and plenary jurisdiction, under section 157(b), a bankruptcy judge may "hear and determine" all core proceedings, similar to the summary jurisdiction granted under the Act. Under section 157(c), however, a bankruptcy judge may hear a noncore proceeding, but may submit only proposed findings of fact and conclusions of law to the district court judge.[1769] Two judges are thus required to review a noncore proceeding, with the district judge entering the final order or remanding it back to the bankruptcy judge for further review. Noncore proceedings are similar to the plenary jurisdiction under the 1898 Bankruptcy Act, except that a bankruptcy judge under the Act did not have *any* jurisdiction to hear a plenary action.

A comparison of the pre-*Marathon* legislation and the legislation responding to *Marathon* adds some clarity to the amendments adopted under BAFJA. Section 1471 in the 1978 Reform Act had three subsections: subsection (a) vested the district court with original and exclusive jurisdiction over all cases under title 11, a Chapter 7 or 11 case; subsection (b) vested the district court with original but not exclusive jurisdiction over proceedings arising under title 11, in a case under title 11, or related to a case under title 11; and, subsection (c) provided that the jurisdiction under subsections (a) and (b) "shall" be exercised by the bankruptcy court. Subsection (c) led to the *Marathon* Court's declaration of unconstitutionality.

The jurisdiction debate that began during the deliberations on the 1978 Reform Act was rekindled immediately following the *Marathon* decision and continued during the deliberations over the enactment of BAFJA. A number of organizations and prominent commentators argued that bankruptcy courts must be

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[1766] Pub. L. No. 98-353, 98 Stat. 333 (1984).

[1767] For a chart of all of the jurisdictional provisions enacted under BAFJA, see Annex A.

[1768] *See* 28 U.S.C. §§ 157(b) and 157(c) (1994).

[1769] The parties to a noncore proceeding may consent to the entry of a final order by the bankruptcy judge. *See* 28 U.S.C. § 157(c)(2) (1994). Consent to the entry of a final order must be explicit. A party who would benefit from delay of the action has to merely withhold consent.

established under Article III in order to be constitutional.[1770] The Judicial Conference argued that *Marathon* did not require Article III status for bankruptcy judges.[1771] Some bankruptcy judges, however, disputed the viability of the alternatives proposed and the arguments raised by the Judicial Conference.[1772]

In 1984, Congress passed BAFJA, the current law, in response to *Marathon.* Section 1334 was substituted for section 1471. Section 1334, in title 28, contains two of the above three subsections. Section 1334(a) and (b) read word for word the same as former section 1471(a) and (b). A related subsection (c) is not included and, in its place, Congress enacted 28 U.S.C. § 157(a), (b), and (c). It is these three subsections which currently establish the authority of the bankruptcy court in what, it is hoped, is a constitutional system.

To put it another way: jurisdiction *qua* jurisdiction over bankruptcy cases and proceedings is set forth in 28 U.S.C. § 1334(a) and (b). Reference of that jurisdiction to bankruptcy judges is discretionary with the district judges, pursuant to section 157(a). Automatic reference under section 157(a), however, has been accomplished nationwide either by local rule or order.[1773] Subsections (b) and (c) of section 157

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[1770] *See, e.g.*, Letter from Charles A. Horsky, Chair, National Bankruptcy Conference to Senator Dennis DeConcini (May 23, 1984) (urging that bankruptcy judges be given Article III status); Letter from Joel Zweibel, Chair, Committee on Bankruptcy and Corporate Reorganization, The Association of the Bar of the City of New York to Louis A. Craco, President, The Association of the Bar of the City of New York (April 11, 1983) (urging the Bar Association of the City of New York to adhere to its endorsement of an Article III bankruptcy court); Letter from Professors Vern Countryman, Frank R. Kennedy, and Lawrence P. King to Representative Peter Rodino, Senator Robert Dole and Senator Strom Thurmond (September 20, 1982) (outlining inaccuracies of Judicial Conference Report to Congress and urging enactment of an Article III bankruptcy court); Letter from Kenneth N. Klee to Senator Strom Thurmond (August 20, 1982) (arguing that Article III status is the only means to cure the jurisdictional faults noted in *Marathon*); Letter from Robert M. Zinman, Chair, American Council of Life Insurance to Senator Robert J. Dole (September 13, 1982) (urging that Article III status for bankruptcy judges is the only mean to cure the jurisdictional infirmities under *Marathon*).

[1771] *See* Report of the Judicial Conference of the United States, Northern Pipeline Construction Co. v. Marathon Pipe Line Co., et al. and Proposals for Remedial Congressional Action (1982) (arguing that Article III status for bankruptcy judges was not necessary and not advisable).

[1772] *See, e.g.*, Letter from Judge George C. Paine, II and Judge Keith M. Lundin, to All Federal Judges (August 20, 1982) (arguing that the Article III alternatives proposed by the Federal Judicial Conference "would result in a return to a system in which some bankruptcy-related matters would be tried in the federal district courts, some in state courts and others in bankruptcy courts.")

[1773] *But see* In re Referral of Title 11 Proceedings to the United States Bankruptcy Judges for This District, dated Jan. 23, 1997 (D. DE 1997) (withdrawing standing order automatically referring Chapter 11 cases to bankruptcy court as of February 3, 1997; Chapter 11 cases in Delaware

prescribe the parameters of a bankruptcy judge's authority in the exercise of the district court's jurisdiction. These limits are that the bankruptcy judge may hear and enter a final order in a matter that is listed as a core proceeding (section 157(b)), and it may hear a noncore proceeding (that which is not core) but may only submit proposed findings of fact and conclusions of law to the district court judge, unless the parties consent to entry of a final order by the bankruptcy judge.[1774]

Section 157 has other subsections, *e.g.*, permissive and mandatory withdrawal and handling of personal injury and wrongful death claims, but it is really only the level of authority over core and noncore proceedings that would render the scheme constitutional.

B. Constitutionality of Current Bankruptcy System

The Supreme Court has not ruled on the constitutionality of the 1984 amendments. The issues raised by the Court in *Marathon* such as the adjudication of public v. private rights, whether consent of the parties satisfies Article III infirmities, and others that are determinative of the limits of an non-Article III court are nebulous at best.[1775] Even with the delineation of core proceedings in section 157(b)(2), the precise authority of a bankruptcy judge to adjudicate certain matters cannot be authoritatively answered today, thirteen years after BAFJA.

The delineation between core and noncore proceedings remains in considerable dispute. Uncertainty creates fertile ground for delay tactics that force the estate to engage in wasteful litigation over the jurisdiction of the court. In an effort to make the current system work, however, some courts find that certain issues are core proceedings even though they bear a marked resemblance to the issues in *Marathon*. For example, some courts have held that an action to recover an outstanding account receivable of the debtor is a core proceeding that may be decided

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are now assigned to district court judges and bankruptcy judges by the chief district judge on a case-by-case basis).

[1774] The list of core proceedings in section 157 is not exclusive. As a result, a determination of whether a proceeding is core or not core is required for every proceeding that is not listed.

[1775] *See* Granfinanciera, S.A. v. Nordberg, 492 U.S. 33 (1989); Commodity Futures Trading Comm'n v. Schor, 478 U.S. 833 (1986); Thomas v. Union Carbide Agric. Prods., 473 U.S. 568 (1985).

by the bankruptcy judge.[1776] No distinction exists, however, between that type of proceeding and the contract damages cause of action in the *Marathon* case.

While other parts of BAFJA are questionable, no case has been reviewed by the Supreme Court raising a constitutional contest on the core/noncore distinction. Whether permissive counterclaims are truly core proceedings as Congress has stated is questionable.[1777] A recently proposed amendment to section 157(c) might have been the catalyst for Supreme Court involvement if enacted. It provided for the entry of a final order by the bankruptcy judge in a noncore proceeding if, after the hearing, no objection is raised to the proposed findings of fact and conclusions of law submitted by the bankruptcy judge. As a result, parties to noncore bankruptcy proceedings would be bound by a final order entered by the Non-Article III bankruptcy judge, unless they object to the proposed findings of fact and conclusions of law. This provision would further attenuate the core/noncore distinction by giving bankruptcy judges the power to do that which BAFJA forbid in light of *Marathon*: enter final orders in noncore proceedings. Whether such implied consent alleviates the Article III requirement is problematical but untested. This provision was in the Federal Courts Improvement Act of 1996 but was deleted in the House just before that Act was passed.[1778]

1. *Granfinanciera, S.A. v. Nordberg*[1779]

The Supreme Court has never ruled on the constitutionality of the core/noncore distinction. The closest it has come was in *Granfinanciera* where it held that a party who had not filed a claim against the debtor retained its Seventh Amendment right to a trial by jury of the fraudulent transfer action seeking a money judgment filed by the trustee.[1780] The Supreme Court found that the defendant retained a right to a jury trial despite the fact that section 157(b)(2)(H) defines an

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[1776] *See In re* Baldwin-United Corp., 48 B.R. 49 (Bankr. S.D. Ohio 1985) ("the collection of a debtor's accounts receivable and other assets is a critical part of the administration of a bankrupt estate traditionally pursued in the Bankruptcy Court."); *In re* Belles Terres Partners, No. 85 C 5355, 1985 WL 3443 (N.D. Ill. 1985) (breach of contract, conversion, and tortious interference with business relations called core proceedings); *In re* L.A. Clarke and Sons, 51 B.R. 31 (Bankr. D.D.C. 1985) (action to collect accounts receivable and defendant's breach of contract counterclaim are core proceedings).

[1777] Under 28 U.S.C. § 157(b)(2)(C) counterclaims are listed as core proceedings.

[1778] Pub. L. No. 104-317, 110 Stat. 3847 (signed Oct. 19, 1996).

[1779] 492 U.S. 33 (1989).

[1780] *Id.* at 36.

action to avoid a fraudulent transfer as a core proceeding.[1781] In so holding, the Court found that Congress could not delegate a private legal right of action to a non-Article III tribunal without violating a litigant's Seventh Amendment right to a jury trial.[1782]

As a result of the Supreme Court's decision in *Granfinanciera,* the issue of jury trials under the Seventh Amendment and the ability of the bankruptcy judge to conduct a jury trial is subject to strategic consideration and delay tactics by attorneys.[1783] For example, something as simple as a jury request in response to the debtor's complaint seeking to enforce certain prepetition contract rights halts the debtor's action and raises a series of time-consuming threshold issues that must be resolved before the substance of the debtor's action can proceed. First, a determination must be made whether the debtor's action is a core or noncore proceeding. Whether an action seeking to enforce a contract right is a core proceeding is the subject of considerable conflict in the courts and is not easily discerned.[1784] If the proceeding is found to be core, the court must determine whether the defendant has a right to a jury trial. If the defendant has a right to a jury trial, the court must determine whether the defendant has waived its right to a jury trial.[1785] If the defendant has not waived its right to a jury trial, the parties consent, and the district court has authorized the bankruptcy court in that district to conduct jury trials,

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[1781] Section 157(b)(2)(H) provides that "Core proceedings include, but are not limited to... (H) proceedings to determine, avoid, or recover fraudulent conveyances;..."

[1782] *Granfinanciera*, 492 U.S. at 54. The Court concluded that "[i]f a statutory right is not closely intertwined with a federal regulatory program that Congress has the power to enact, and if that right neither belongs to nor exists against the Federal Government, then it must be adjudicated by an Article III court. If the right is legal in nature, then it carries with it the Seventh Amendment's guarantee of a jury trial." *Id.* at 54-55.

[1783] For example, in a recent decision, *In re* Green, 200 B.R. 296 (S.D.N.Y. 1996), the district court withdrew an entire adversary proceeding (commenced to determine the dischargeability of a claim under section 523(a) and (d)) because the third-party complaint of the debtor raised noncore issues, a timely demand for a jury trial was made by third-party defendant, and the bankruptcy court may not conduct the jury trial.

[1784] Orion Pictures Corp. v. Showtime Networks, Inc. (*In re* Orion), 4 F.3d 1095 (2d Cir. 1993) (holding that action on the alleged prepetition breach of a prepetition contract was a noncore proceeding and bankruptcy court could not conduct the jury trial), *cert. dismissed*, 114 S. Ct. 1418 (1994); Ben Cooper, Inc. v. Insurance Co. of Pennsylvania (*In re* Ben Cooper), 896 F.2d 1394 (2d Cir. 1990) (holding that action on alleged postpetition breach of postpetition contract was a core proceeding), *vacated on other grounds*, 111 S. Ct. 425 (1990), *reinstated*, 924 F.2d 36 (1991).

[1785] *See, e.g.*, Langenkamp v. Culp, 498 U.S. 42, 44 (1990) (creditor who filed proof of claim against debtor's estate waived Seventh Amendment right to jury trial) *reh'g denied*, 498 U.S. 1043 (1991).

the bankruptcy judge may hear the proceeding.[1786] If any of these prerequisites are missing, the action must be litigated in the district court.

*Granfinanciera* erodes the basic principle of the current jurisdictional scheme that the core proceedings listed[1787] in section 157(b)(2) are entirely and appropriately within the jurisdiction of the bankruptcy court. Core proceedings are never defined in the Bankruptcy Code. The list of core proceedings in section 157(b)(2) is not an exclusive list. As a result, whether a proceeding is a core proceeding or not may always be the subject of a dispute between the parties. If all core proceedings are subject to disagreement, debtors and creditors are at the mercy of parties who can afford to litigate the bankruptcy court's authority until the other party capitulates. Needless litigation depletes the estate of resources and unsecured creditors as a result receive very little or nothing at all. Bankruptcy jurisdiction must be clearly defined in order for the bankruptcy system to benefit creditors and debtors by avoiding cost and delay.

C. Academic Consensus on Constitutionality of Current System

A number of commentators conclude that the bankruptcy court under BAFJA is constitutional.[1788] These commentators find congressional authority to designate

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[1786] The bankruptcy judge may conduct a jury trial in a core proceeding if the applicable district court has so designated and the parties consent. 28 U.S.C. § 157(e) (1994).

[1787] Even more surprising is the fact that section 157(b)(2) is not meant to be an exclusive list of all core proceedings. Notwithstanding the specific reference to fraudulent transfer actions in section 157(b)(2)(H), the implication of *Granfinanciera* calls into question all core proceedings, whether listed or not.

[1788] *See* Paul Bator, *The Constitution as Architecture: Legislative and Administrative Courts Under Article III*, 65 IND. L.J. 233 (1990) (current system is constitutional; non-Article III courts can perform adjudicative functions consistent with the Framers' intent as well as modern interpretations of the requirements of Article III; bankruptcy judges should not be accorded Article III status, as it would destroy the Article III notion of "revered elite generalists entrusted with judicial powers."); Erwin Chemirinsky, *Ending the Marathon: It is Time to Overrule Northern Pipeline*, 65 AM. BANKR. L.J. 311 (1991)(current bankruptcy system is constitutional; decision to grant Article III status to bankruptcy judges is a political and not a constitutional issue.); Richard H. Fallon, Jr., *Of Legislative Courts, Administrative Agencies, and Article III*, 101 HARV. L. REV. 915 (March 1988)(under flexible approach to Article III, both 1978 Act as well as BAFJA are constitutional; adopts appellate review theory which preserves delicate policy concerns while permitting delegation of certain adjudicative functions to non-Article III courts); Daniel J. Meltzer, *Legislative Courts, Legislative Power and the Constitution*, 65 IND. L. REV. 291 (1990) (current bankruptcy system is constitutional; values of Article III should be balanced against legislative purpose behind the creation of a non-Article III tribunal); Ralph U. Whitten, *Consent, Caseload, and Other Justifications for Non-Article III Courts and Judges: A Comment on Commodities Futures Trading Commission v. Schor*, 220 CREIGHTON L. REV. 11 (1986) (BAFJA system is constitutional because (1) "core proceedings involve some form of "public right" that can be adjudicated by a non-Article III court"

the adjudication of certain matters to non-Article III tribunals and that core bankruptcy matters qualify for non-Article III adjudication. They conclude that a final order entered by a bankruptcy judge in a core proceeding is constitutional. At the same time, this consensus acknowledges that the bankruptcy structure is constitutionally weak in certain areas.[1789]

Conversely, a number of commentators have concluded that bankruptcy courts "exercise the essential attributes of the judicial function" (even in core proceedings) and are unconstitutional.[1790] Under this rationale, bankruptcy judges are not authorized to enter final orders in core proceedings and the system does not satisfy Article III.[1791]

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[doubtful after Court's ruling in *Granfinanciera*], and (2) BAFJA provides a greater degree of judicial control over both core and non-core proceedings).

[1789] *See, e.g.*, Erwin Chemirinsky, *Ending the Marathon: It is Time to Overrule Northen Pipeline*, 65 AM. BANKR. L.J. 311 (May 1991) (the fact that *Marathon* remains good law makes it impossible to properly construct an Article I adjudicative court; *Granfinanciera* adds new problems as to the constitutionality of the core/noncore distinction).

[1790] David P. Currie, *Bankruptcy Judges and the Independent Judiciary*, 16 CREIGHTON L. REV. 441(1983) (adopting a literalist approach to Article III and concludes that the 1978 Code was unconstitutional; under a strict interpretation of Article III, the current system under BAFJA would also be unconstitutional); S. Elizabeth Gibson, *Jury Trials and Core Proceedings: The Bankruptcy Judge's Uncertain Authority*, 65 AM. BANKR. L.J. 145 (1991) (under a broad reading of *Granfinanciera*, all core jurisdiction violates Article III; bankruptcy courts, even in core proceedings, exercise the essential functions of the judicial power and are unconstitutional); Thomas G. Krattenmaker, *Article III and Judicial Independence: Why the New Bankruptcy Courts are Unconstitutional*, 70 GEO. L.J. 297 (1981) (system under 1978 Bankruptcy Reform Act was unconstitutional -- arguments apply with equal force to system under BAFJA — because bankruptcy courts are acting like "inferior courts" without Article III protections.); G. Ray Warner, *Rotten to the 'Core:' An Essay on Juries, Jurisdiction and Granfinanciera*, 59 UNIV. MISS. K.C.L. REV. 991 (1991) (the boundaries of core jurisdiction, avoiding powers, turnover actions, lien priority, etc., have been called into question by *Granfinanciera's* narrow view of what is properly delegated to non-Article III forum); Note, *The Bankruptcy Act of 1984: Marathon Revisited*, 3 YALE L. & POL. REV. 231 (1984) (concluding that BAFJA exacerbated the system's constitutional defects; practical problems with BAFJA system include having to litigate noncore proceedings twice and two-tiered system diminishes prestige of bankruptcy court).

[1791] Richard Lieb, *Can a Bankruptcy Judge Constitutionally Hear and Determine a "Core" Proceeding?*, 6 NORTON BANKR. L. ADV. 1 (1997) (arguing that current system is unconstitutional because bankruptcy judges exercise the "judicial power" of the United States even in "core" matters).

## D. The Need for an Article III Bankruptcy Court

### 1. Elimination of Jurisdictional Litigation

The core/noncore distinction has created a judicial system first by necessity and second by design, that is time consuming, unnecessarily expensive, and inefficient. It produces procedural routes that require court and attorney time for purposes having nothing to do with resolving the substantive merits of the controversy. Article III status would clearly eliminate the need for withdrawal provisions, special jury provisions, special abstention provisions, core vs. noncore distinctions, a double layer of litigation at the trial level through the present need for proposed findings by one judge which are given to another judge who can retry the same matter, and the like.

Opponents of the Recommendation argue that disputes over jurisdiction do not arise very often and therefore, no change to the structure of the bankruptcy court system is necessary. But the numbers do not tell the important part of the story. The important fact is that in any single case the parties—the actual debtors, creditors, trustees, employees, etc.—are forced to spend money and time in a fruitless endeavor. That is, they are required to incur litigation expense over nonsubstantive issues. Two recent decisions of the Courts of Appeals are illustrative of this needless litigation.

#### a. *In re Conejo Enterprises, Inc.*[1792]

A recent example of this circular litigation over bankruptcy jurisdiction is *In re Conejo Enterprises, Inc.*, which necessitated two opinions from the Court of Appeals for the Ninth Circuit sandwiched around a third Ninth Circuit decision withdrawing the first opinion. The issue was relatively simple. A breach of contract action was instituted by a creditor of the soon-to-be debtor in state court. While it was pending, the defendant filed a Chapter 11 petition and removed the state court action to the bankruptcy court. A motion for remand was made as was a request for relief from the automatic stay. The bankruptcy court denied both. On appeal to the district court, the bankruptcy court was reversed on both orders.[1793] The district court (1) extended the time for the plaintiff-creditor to file a proof of claim in the Chapter 11 case, which it then did, (2) ordered the civil action remanded to the state court, and (3) lifted the stay.

On appeal to the Ninth Circuit, that court reversed both orders of the district court. Shortly thereafter, it filed a decision withdrawing that opinion. Sometime later, the court of appeals filed another opinion, confessing error in reversing the remand

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[1792] 71 F.3d 1460 (1995), 96 F.3d 346 (1996), 78 F.3d 1456 (1996).

[1793] 174 B.R. 814 (C.D.Cal. 1994).

order in light of the Supreme Court's decision in *Things Remembered, Inc.v. Petrarca*.[1794] It noted that courts of appeal have no jurisdiction over remand orders. The Ninth Circuit went on, however, to the lift stay order. The district court had found that the cause of action constituted a noncore proceeding, making abstention appropriate under section 1334(c)(2) (mandatory abstention). The duplicative result was that the cause of action was separated from the filing of a proof of claim in order to participate in the Chapter 11 distribution.

The Ninth Circuit ultimately held that the state law proceeding could remain in the state court but could not continue because it was subject to the automatic stay in section 362(a). If the creditor-plaintiff desired to participate in the Chapter 11 distribution, it was required to file a proof of claim, which is a core proceeding under section 157(b)(2)(B). Whether or not it files a proof of claim, the claim will be discharged to the extent it is not paid, and, therefore, there is no point in continuing the state court action. Thus, the stay should not be lifted. The point is, here is an uncomplicated set of facts that got litigated repeatedly and needlessly. Simply put, the cause of action centered around a proof of claim, the filing of which triggers the equitable jurisdiction of the bankruptcy court for which no jury trial right exists.[1795] It is irrelevant if a state court action is pending prepetition.

b. *In re Orion Pictures, Corp.*[1796]

Another case emblematic of this type of nonsubstantive litigation is *In re Orion Pictures, Corp.* In *Orion*, the debtor in possession moved to assume an executory contract and instituted an adversary proceeding at the same time for a declaratory judgment claiming anticipatory breach of the agreement and seeking specific performance or damages. The bankruptcy court denied the defendant's jury request, holding that the two proceedings were actually one, based on the motion to assume which necessitated a finding of the existence of the contract.

The Second Circuit reversed and held that the bankruptcy court could only decide the motion to assume, but an adversary proceeding was necessary with respect to the issues of contract existence and breach, which was not a core proceeding. In

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[1794] 516 U.S. 124 (1995) (holding, among other things, that appellate review of district court's remand order was barred by statute, regardless of whether removal was based on bankruptcy removal statute or on general removal statute).

[1795] Langenkamp v. Culp, 498 U.S. 42, 44 (1990) (depositors who filed claims against debtor's estate waived Seventh Amendment right to jury trial for preference action; "by filing a claim against a bankruptcy estate the creditor triggers the process of 'allowance and disallowance of claims,' thereby subjecting himself to the bankruptcy court's equitable power."), *reh'g denied*, 498 U.S. 1043 (1991).

[1796] 4 F.3d 1095 (2d Cir. 1993), *cert. denied*, 511 U.S. 1026 (1994).

other words, the assumption proceeding was a core proceeding but whether a contract existed at all constituted a noncore proceeding. As to the latter, the nondebtor party was entitled to a jury trial and that matter had to be withdrawn. Again, a trip to the court of appeals, via the district court, without anything being decided on the merits of the dispute between the parties. Final resolution of this issue necessitated two trials: one in the bankruptcy court on assumption of the contract and the other in the nonbankruptcy court on the existence of the contract.

These cases demonstrate the confusion that exists over the boundaries of the bankruptcy courts' authority to enter a dispositive order. This confusion creates litigation that is costly not only to the parties involved but to the entire bankruptcy system. Creditors finance litigation under circumstances where parties rarely win. The party who can erect enough jurisdictional roadblocks prevails once the estate can no longer afford to fight.

2. Alternatives to Article III

Article III status was not the only solution the Commission considered to resolve the current jurisdiction quagmire. The Commission also considered a number of alternative "stream-lining" proposals. Extensive discussions were held, but the Commission did not make any recommendation with regard to these proposals. The following discussion is included to illuminate why the stream-lining proposals will not solve the fundamental jurisdictional problems in the current system.

As discussed above, the jurisdiction provisions of BAFJA were enacted in response to *Marathon* in an effort to reconstitute a constitutional bankruptcy court.[1797] A number of provisions were added under BAFJA, however, that have no effect on the constitutionality of the bankruptcy court. For example, mandatory withdrawal, mandatory abstention, and the forum for liquidating personal injury claims are all provisions that increase the cost and delay of bankruptcy-related litigation but neither improve nor impair the constitutionality of the current system.

Under *Marathon*, a non-Article III court may not be given pervasive jurisdiction nor may it finally decide a proceeding involving a purely state law cause of action brought by the estate representative against a third party. If bankruptcy courts do not have Article III status, the core/noncore provisions in section 157(c) must be retained. All of the unanswered questions, such as, whether all counterclaims are core proceedings even if so listed in section 157(b)(2)(C) and whether implied consent is constitutionally tolerated under section 157(c)(2), remain as the system continues to struggle with this dichotomy.

[1797] *See infra* Annex A.

All other provisions of a procedural nature affecting trials in the bankruptcy court may be eliminated in order to remove strategic delay-causing devices from the arsenal of litigators.[1798] The delay caused by these provisions is funded by the unsecured creditors who must bear the costs of administration. Because these provisions do not buttress the constitutional nature of the current system they only serve to add further delay and expense to an already lengthy and costly core/noncore procedure.

In addition, the Commission discussed whether bankruptcy judges should be authorized to exercise the broadest contempt powers constitutionally permissible. There is considerable agreement among courts as to what contempt powers a bankruptcy court as a non-Article III court could constitutionally exercise.[1799] The contempt power parameters that a bankruptcy judge may constitutionally exercise include civil contempt power and criminal contempt power for contempt committed in the presence of the court, with no power to incarcerate. This conclusion is consistent with the Judicial Conference's Long Range Plan for the Federal Courts

[1798] These include mandatory abstention provisions, mandatory withdrawal provisions, and special personal injury litigation provisions.

[1799] *See, e.g.*, Eck v. Dodge Chem. Co. (*In re* Power Recovery Sys. Inc.), 950 F.2d 798, 802 (1st Cir. 1991) ("well-settled law that bankruptcy courts are vested with contempt power"; but bankruptcy courts lack power to hold persons in criminal contempt); Griffith v. Oles ( *In re* Hipp, Inc.), 895 F.2d 1503, 1509 (5th Cir. 1990) (with the exception of contempts "in (or near) its presence", bankruptcy courts lack criminal contempt power); Mountain Am. Credit Union v. Skinner (*In re* Skinner), 917 F.2d 444 (10th Cir. 1990) (delegation of civil contempt power to bankruptcy courts proper and does not offend separation of powers portion of constitution); Hicks v. Pearlstein (*In re* Magwood), 785 F.2d 1077 (D.C. Cir. 1986) (bankruptcy courts lack criminal contempt power unless exercised within the limitations provided by (now revoked) section 1481); Burd v. Walters (*In re* Walters), 868 F.2d 665, 668 (4th Cir. 1989) (plain-meaning of section 105(a) gives bankruptcy court civil contempt power); Utah State Credit Union v. Skinner (*In re* Skinner), 90 B.R. 470, 476 (D. Utah 1988) ("the current version of the Bankruptcy Code implicitly recognizes the inherent contempt powers of the bankruptcy court in Section 105(a)."); Stock-Schalaeder & McDonald v. Kittay (*In re* Stockbridge Funding Corp.), 145 B.R. 797, 804 (Bankr. S.D.N.Y. 1992, *aff'd in part and rev'd in part*, 158 B.R. 914 (S.D.N.Y. 1993) ("A bankruptcy court's contempt power is recognized by statute . . . and has been acknowledged or simply assumed to exist in various non-Article III tribunals."); *In re* Galvez, 119 B.R. 849, 850 (Bankr. M.D. Fla. 1990) ("[t]his Court . . . is satisfied that non-Article III courts have inherent power to enforce the lawful court orders issued in a proceeding over which the court had jurisdiction, even absent specific statutory authorization . . . . However . . . this Court . . . finds such authority in § 105 of the Bankruptcy Code."); *In re* McLean Indus., Inc., 68 B.R. 690, 695 (Bankr. S.D.N.Y. 1986) ("the power of the bankruptcy court to issue an order of civil contempt derives from three sources: the inherent power of a court, including an Article I court, the reference of the inherent power of the district court, and the statutory grant contained in 11 U.S.C. § 105.").

specific recommendation that Congress enact legislation granting such contempt power to the bankruptcy court.[1800]

The Commission also discussed whether district court referrals of bankruptcy appeals, noncore proceedings, and withdrawn proceedings to magistrate judges was proper under BAFJA.[1801] The purpose of these provisions under BAFJA was to ensure that an Article III district court judge would review the proceedings. Arguably, if cause exists to withdraw a proceeding from the non-Article III bankruptcy judge, the same cause exists to prevent referral of that matter to a non-Article III magistrate judge. Prohibiting the referral of bankruptcy matters to magistrate judges accords with the recommendation of the Judicial Conference of the United States.[1802] The result would be that a district judge would not be able to refer these matters to magistrate judges.

The net effect of these streamlining proposals would be to assist in reducing cost and increasing efficiency. The delays caused by provisions that do not buttress the constitutionality of the bankruptcy system under BAFJA only serve to exacerbate the problems that already inhere in the core/noncore distinction. The system would only become marginally more efficient by amending these provisions. The same dichotomy between core and noncore proceedings would still have to be maintained and that would lead to the same costly disputes outlined in *Conejo* and *Orion*.

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[1800] Long Range Plan for the Federal Courts of the Judicial Conference of the United States, 52-53, Recommendation 27b (December 1995) (bankruptcy judges should be authorized to exercise civil contempt power and limited criminal contempt power).

[1801] Such referral is not limited to appeals. Even under the appellate proposal adopted by the Commission, the district court may hear noncore proceedings *de novo*. The referral bar should apply to such proceedings as well as to proceedings withdrawn under section 157(d). It seems equally inconsistent with the jurisdictional and procedural scheme enacted in 1984 to permit a referral of a noncore proceeding to a magistrate judge. If permitted, the referral scenario would evolve as follows: trial before the bankruptcy judge who submits proposed findings of fact and conclusions of law to the district judge (11 U.S.C. §§ 157(a), 157(c)(1) (1994)); objection(s) to a finding or conclusion by a party (FED. R. BANKR. P. 9033); submission to the district judge (who should enter a final order after reviewing the objection(s)) (11 U.S.C. § 157(c)(1) (1994)); referral to a magistrate judge (28 U.S.C. § 636 (1994)); if no consent, magistrate judge makes proposed findings and conclusions for a second time (28 U.S.C. § 636(b)(1)(C) (1994)); entry of final order by district judge after, presumably, another possibility of *de novo* review.

[1802] Long Range Plan *supra* note 1800, 48 n.22 (December 1995) ("... the practice of referring bankruptcy appeals to magistrate judges should be discontinued. It is questionable both in terms of efficient resource allocation and in its impact on expeditious resolution of appeals.")

Conclusion

The procedural morass of the bankruptcy judicial system is extraordinarily costly and inefficient. The cost is borne by creditors, debtors, and the court and its administration. Article III status is not a panacea, but it is a miracle cure for the majority of jurisdictional ills that currently afflict the bankruptcy court. It would not relieve the system of a motion raising the basic jurisdiction issue, *i.e.*, "related to" jurisdiction. It would, however, relieve it of all of the other jurisdictional motions which would eliminate a great deal of expense for the estate, the creditors, interested third parties, and the system itself in terms of court and administration time.

### 3.1.2 *Transition to an Article III Bankruptcy Court*

**As of the enactment of legislation to establish an Article III bankruptcy court, sitting bankruptcy judges should be permitted to finish their current fourteen year terms. As vacancies are created through attrition (including expiration of current statutory term, appointment as an Article III judge, resignation, retirement prior to end of term for any reason, or death), Article III bankruptcy judges should be appointed by the President upon the advice and consent of the Senate to fill those positions. Sitting bankruptcy judges should be permitted to apply for any Article III judgeship positions while remaining on the bench. Nothing in the Recommendation will affect the length of the current term, salary, retirement benefits, or other attributes of sitting bankruptcy judges.**

**During the transition period, bankruptcy jurisdiction should be treated in the following manner: as Article III bankruptcy judges are appointed, the jurisdiction provisions under 28 U.S.C. §§ 1334 and 157 should be transferred on a district-by-district basis to the Article III bankruptcy judge sitting in that district. Consequently, bankruptcy jurisdiction would reside in the Article III bankruptcy judge, including the power to refer and withdraw cases and proceedings. While a district is without an Article III bankruptcy judge, the Judicial Council for that circuit should be authorized to: (1) determine the need for an Article III bankruptcy judge in that district, and (2) if necessary, designate an Article III bankruptcy judge from another district (within the circuit) to sit in that district. In the event the judicial council determines a need for an Article III bankruptcy judge and one has not yet been appointed to sit within that circuit, the Chief Justice, upon receiving a certificate of necessity from the chief judge of the circuit, should be authorized to designate an Article III bankruptcy judge from another circuit to fulfill the request.**

Article III status is a prerequisite to exercising "the essential attributes of judicial power."[1803] At first glance, the creation of an Article III bankruptcy court might lead to the conclusion that such judges would have to be given the same salary, chambers, and other benefits enjoyed by district court judges. However, more flexibility exists under Article III of the Constitution than that first glance would indicate. When the Supreme Court declared unconstitutional bankruptcy court jurisdiction granted under 28 U.S.C. § 1471, the Court provided some guidance on Article III's flexibility:

> ...Article III itself permits much flexibility; so long as tenure during good behavior is granted, much room exists as regards other conditions. Thus it would certainly be possible to create a special bankruptcy court under Article III and there is no reason why the judges of that court would have to be paid the same as district judges or any other existing judges. It would also be possible to provide that when a judge of that court retired pursuant to statute, a vacancy for a new appointment would not automatically be created. And it would be entirely valid to specify that the judges of that court could not be assigned to sit, even temporarily, on the general district courts or courts of appeals.[1804]

Flexibility under Article III makes it prudent for the Commission to make recommendations regarding the transition to an Article III bankruptcy court. Legislative ambiguity regarding a judge's Article III status has led to confusion in the past.[1805] Congressional clarity is imperative to ensure a smooth Article III transition for the bankruptcy court.[1806]

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[1803] Northern Pipeline Constr. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 81 (1982).

[1804] *Id.*, at 74 (quoting the *Hearings on H.R. 31 and H.R. 32 before the Subcommittee on Civil and Constitutional Rights of the House Committee on the Judiciary*, 94th Cong. 2697 (1976) (letter of Paul Mishkin)).

[1805] *See* Glidden Co. v. Zdanok, 370 U.S. 530, 582 (1962) (holding that Congress' Article III designations of The Court of Claims and the Court of Customs and Patent Appeals granted life tenure and salary protection to judges sitting at time of statute's enactment; "Since the Court of Claims and the Court of Customs and Patent Appeals are courts created under Article III, their judges--including retired judges, [citation omitted]-- are and have been constitutionally protected in tenure and compensation.") *reh'g denied*, 371 U.S. 854 (1962).

[1806] Remedial legislation was necessary for both the Court of Claims and the Court of Customs and Patent Appeals to clarify that Congress intended each of the courts to be "a court established under article III of the Constitution of the United States." H.R. REP NO. 85-2349, at 3 (1958) (amending section 211 of title 28 to provide that the Court of Customs and Patent Appeals is an Article III court). *See also* H.R. REP. NO. 83-695, at 2 (1953) (clarifying that the Customs Court "was established as a constitutional court pursuant to article III.").

During the debate over how to structure the transition to an Article III bankruptcy court a number of concerns have been raised. Of primary concern is whether one sitting president would have the power to appoint over three hundred life-tenured judges.[1807] Concerns were also raised about protecting the interests of sitting bankruptcy judges. Jurisdictional concerns focused on the constitutional propriety of having an Article III bankruptcy court sitting concurrently with a non-Article III bankruptcy court. The Recommendation attempts to address all of these concerns and balance the interests of those participating in the current system with the desire for as quick and as smooth a transition as possible.

A. Phasing in Article III Bankruptcy Judges

The Recommendation addresses these concerns in a number of fundamental ways. Concern over granting such vast appointment power to a single sitting president is alleviated by phasing-in the appointment of Article III bankruptcy judges over 14 years. The interests of sitting bankruptcy judges are protected under the Recommendation by permitting them to remain on the bench for their statutory term; to seek appointment as Article III bankruptcy judges while remaining on the bench; and to retain all pension and retirement benefits currently provided. The Recommendation will facilitate the development of a higher-quality bankruptcy bench by enabling sitting bankruptcy judges (who have a breadth of specialization, experience and perspective) to seek appointment as Article III judges. In addition, the Recommendation provides fourteen years to develop a firs-rate bankruptcy bench without requiring hundreds of immediate appointments.

Under the Recommendation, Article III bankruptcy judges would be phased-in on an attrition basis. An act of attrition would include (1) expiration of the current fourteen year term of a sitting bankruptcy judge; (2) resignation; (3) retirement from the bench for any reason prior to the expiration of the statutory term; (4) being sworn-in as an Article III judge; or (5) death. Application by a sitting bankruptcy judge for appointment as an Article III bankruptcy judge would not be an act of attrition. The Recommendation permits sitting bankruptcy judges to retain their positions during the application and confirmation process. Once a sitting bankruptcy judge is appointed as an Article III judge, another vacancy would be created that could be filled by yet another Article III bankruptcy judge. The application process for a sitting bankruptcy judge to become an Article III judge will not create a vacancy under the Recommendation; however, the *appointment* of a sitting bankruptcy judge

[1807] The House Report noted that 1970 Commission proposed staggering the appointees to the new bankruptcy court in order to alleviate this concern. H.R. REP. 95-595, at 22 n.135 (1977).

as an Article III bankruptcy judge or any other Article III judge would create a vacancy under the Recommendation.

Historically, Article III judges have been considered "officers of the United States"[1808] and have consequently been appointed by the President with the advice and consent of the Senate.[1809] The Recommendation preserves this method of appointment.

Under the Recommendation, sitting non-Article III bankruptcy judges will be permitted to serve out the remainder of their fourteen year terms. Concurrent with that service, sitting bankruptcy judges are eligible to seek Article III bankruptcy judgeships. If a sitting bankruptcy judge is appointed as an Article III bankruptcy judge, the transfer of that bankruptcy judge to an Article III judgeship would be an act of attrition under the Recommendation. The vacancy left by that judge would create another vacancy on the bankruptcy bench that may be filled by another Article III bankruptcy judge.

Currently, bankruptcy judges are eligible for full pension benefits (1) upon reaching their 65th birthday, and (2) after they have served for fourteen years.[1810] The Recommendation does not affect the pension and other retirement benefits that current bankruptcy judges would otherwise receive in the absence of an Article III transition period.

The Administrative Office has promulgated pension and other benefit transfer provisions for bankruptcy judges that become Article III judges during their tenure

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[1808] For a complete discussion of the appointments clause, see, Morrison v. Olson, 487 U.S. 654 (1988) (holding that independent counsel was an "inferior officer" under the Appointments Clause; appointment by Special Division upon request of the Attorney General did not violate Appointments Clause).

[1809] The appointment power provides that the President

> shall nominate, and by and with the Advice and Consent of the Senate, shall appoint Ambassadors, other public Ministers and Consuls, Judges of the supreme Court, and all other Officers of the United States, whose Appointments are not herein otherwise provided for, and which shall be established by Law: but the Congress may by Law vest the appointment of such inferior Officers, as they think proper, in the President alone, in the Courts of Law, or in the Heads of Departments.

U.S. CONST. art. II, cl. 2.

[1810] For the pension terms for bankruptcy judges, see, 28 U.S.C. § 377 (1996).

on the bankruptcy court.[1811] The Recommendation does not affect these transfer provisions; their operation will remain the same during the transition period. As a result, the Recommendation will not increase the current pension and retirement benefit costs for sitting bankruptcy judges who become Article III judges.

By phasing-in Article III judges on an attrition basis according to the length of the current term of a sitting bankruptcy judge, transition could take a maximum of fourteen years to complete. Critics may argue that fourteen years is too long to maintain two tiers of bankruptcy judges. The current system, however, already incorporates two tiers of bankruptcy judges by vesting bankruptcy jurisdiction in the district court with discretionary referral to bankruptcy judges. The current system, moreover, maintains those two tiers with no movement towards a more efficient and unified bankruptcy court structure. By phasing in Article III bankruptcy judges on an attrition basis, the Recommendation offers a minimum of disruption for all interested parties during the transition to a more efficient bankruptcy court structure. In addition, by phasing in Article III judges, the appointment power will not go to a single sitting president, but would be spread out over fourteen years. The transition period will also foster the development of a high quality bankruptcy bench by spreading the appointment power among several presidents and over the course of a number of years.[1812]

The natural expiration dates of the terms of current bankruptcy judges could have a significant effect on the timing of the transition period and make a difference in the number of non-Article III bankruptcy judges who continue to sit during the transition period. Between 1999 and 2002, the terms of 215 bankruptcy judges will expire. This is in comparison with the terms of 96 bankruptcy judges that will expire between 2003 and 2009.[1813] Depending on the timing of any Article III legislation, the transition period will either include a majority of sitting bankruptcy judges or a majority of Article III bankruptcy judges.

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[1811] *See* Retirement Benefits for Bankruptcy Judges and Magistrate Judges, Administrative Office of the U.S. Courts, 2d ed. (Sept. 1995).

[1812] This aspect of the Recommendation may benefit recent appointees to the bankruptcy bench who have not developed significant bankruptcy expertise when compared to bankruptcy judges who have already served multiple terms. By enabling all sitting bankruptcy judges to complete a minimum of one term on the bench, the Recommendation does not favor more senior bankruptcy judges over those who have recently been appointed.

[1813] For a more complete breakdown of the expiration dates of current bankruptcy judge terms, see the chart provided by the Bankruptcy Judges Division of the Administrative Office of U.S. Courts in the Appendix.

## B. Bankruptcy Jurisdiction During the Transition Period

The U.S. Code in 28 U.S.C. § 1334(a) and (b) currently places bankruptcy jurisdiction in the district courts.[1814] District courts have the power to, among other things, refer bankruptcy cases and proceedings in bankruptcy cases to the bankruptcy judge;[1815] withdraw cases and proceedings from the bankruptcy judge;[1816] liquidate personal injury tort and wrongful death claims asserted in a bankruptcy case;[1817] enter final orders in noncore bankruptcy proceedings;[1818] abstain from hearing certain state

[1814] Section 1334(a) provides "Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11." 28 U.S.C. § 1334(a) (1996). Section 1334(b) provides

> Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

28 U.S.C. § 1334(b) (1996).

[1815] 28 U.S.C. § 157(a) (1996) ("Each district court may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.")

[1816] 28 U.S.C. § 157(d) (1996) ("The district court may withdraw, in whole or in part, any case or proceeding referred under this section, on its own motion or on timely motion of any party, for cause shown. The district court shall, on timely motion of a party, so withdraw a proceeding if the court determines that resolution of the proceding requires consideration of both title 11 and other laws of the United States regulating organizations or activities affecting interstate commerce.")

[1817] 28 U.S.C. § 157(b)(5) (1996) ("The district court shall order that personal injury and wrongful death claims shall be tried in the district court in which the bankruptcy case is pending, or in the district court in the district in which the claim arose, as determined by the district court in which the bankruptcy case is pending.")

[1818] 28 U.S.C. § 157(c)(1) (1996) ("A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de novo those matters to which any party has timely and specifically objected.").

law claims;[1819] hear state law claims removed by the debtor;[1820] and, hear appeals from bankruptcy court orders in core matters.[1821]

Consistent with the Commission's Recommendation to eliminate the district court from the appellate process in bankruptcy, the Recommendation also eliminates the district court from the bankruptcy jurisdictional scheme. Under the Recommendation, bankruptcy jurisdiction would be transferred from the district court to the Article III bankruptcy judge(s) sitting in that district. Bankruptcy jurisdiction, as well as the bankruptcy role of the district court, would thus be with the Article III bankruptcy judge(s) on a district-by-district basis. For example, if only one Article III bankruptcy judge had been appointed in a multi-bankruptcy judge district, the Article III bankruptcy judge would assume the role of the district court and the other bankruptcy judges would sit as adjuncts of the Article III bankruptcy court. The power to, among other things, refer cases, withdraw cases, abstain from cases,

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[1819] Section 1334 (c)(1) and (c)(2) provide:

> (C)(1) Nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11. (2) Upon a timely motion of a party in a proceeding based upon a State law claim or State law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a state forum of appropriate jurisdiction.")

28 U.S.C. § 1334(c)(1) and (c)(2) (1996).

[1820] 28 U.S.C. § 1452(a) (1996) ("A party may remove any claim or cause of action in a civil action other than a proceeding before the United States Tax Court or a civil action by a governmental unit to enforce such governmental unit's police or regulatory power, to the district court for the district where such civil action is pending, if such district court has jurisdiction of such claim or cause of action under section 1334 of this title.")

[1821] 28 U.S.C. § 158(a) (1996). Section 158(a) provides:

> (a) The district courts of the United States shall have jurisdiction to hear appeals
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> (1) from final judgments, orders, and decrees;
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> (2) from interlocutory orders and decrees issued under section 1121(d) of title 11 increasing or reducing the time periods referred to in section 1121 of such title; and
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> (3) with leave of the court, from other interlocutory orders and decrees;
>
> of bankruptcy judges entered in cases and proceedings referred to the bankruptcy judges under section 157 of this title. An appeal under this subsection shall be taken only to the district court for the judicial district in which the bankruptcy judge is serving.

determine noncore matters, hear removed claims, and liquidate personal injury claims would be handled by an Article III bankruptcy judge.

In districts where an Article III bankruptcy judge had not yet been appointed, the district court would retain its current jurisdictional and appellate role, if any, until such time as an Article III bankruptcy judge was appointed to sit permanently in that district. Designation of an Article III bankruptcy judge to sit *temporarily* in a district (discussed *infra*) will have no effect on the jurisdictional and appellate role of that district court.

The length of the transition period combined with the changing workload of the bankruptcy system necessitates a plan to deal with these needs during the transition. An Article III bankruptcy judge would greatly reduce cost and delay by presiding over a case that involves a number of noncore issues that must be resolved. A critical component of the Recommendation is the role of the Judicial Council of the Circuit to address these needs. The political processes involved in nominating and confirming Article III judges virtually guarantee that Article III bankruptcy judges will be confirmed in different districts in a manner that bears little relationship to the needs for an Article III bankruptcy judge. The Judicial Council in each circuit would be authorized to (1) assess the need for an Article III bankruptcy judge in a particular district, and (2) if necessary, designate an Article III bankruptcy judge from another district to sit in that district.

This Recommendation is in keeping with the supervisory role already played by the Judicial Council of the circuit.[1822] The various duties of the Judicial Council include

> [a]ssigning judges to congested districts, and to particular types of cases, directing them to assist infirm judges, ordering them to decide cases long held under advisement, requiring a judge to forego his summer vacation in order to clear his congested docket, compelling multi-judge courts to arrange staggered vacations, and setting standards of judicial ethics.[1823]

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[1822] Chandler v. Judicial Council of the Tenth Circuit of the United States, 398 U.S. 74, 86 n.7 (1970) ("We find nothing in the legislative history to suggest that the Judicial Council was intended to be anything other than an administrative body functioning in a very limited area in a narrow sense as a 'board of directors' for the circuit."), *reh'g denied,* 399 U.S. 937 (1971).

[1823] CHARLES ALAN WRIGHT ET AL., FEDERAL PRACTICE AND PROCEDURE, § 3939 (1996) *citing Fish, The Circuit Councils: Rusty Hinges of Federal Judicial Administration*, 37 U. CHI. L. REV. 203, 207 (1970).

The Judicial Council would be able to address many situations. If, for example, a large mass-tort case is filed in a district without an Article III bankruptcy judge. Rather than permit costly and time-consuming jurisdictional litigation that can currently occur between the bankruptcy judge and the district court, the Judicial Council may choose to designate an Article III bankruptcy judge from another district to hear the case or some portions of the case. As discussed in the Article III Recommendation, no basis would exist to dispute the authority of an Article III bankruptcy judge to hear, determine, and estimate personal injury claims.

Where the Judicial Council of a circuit determines a need for an Article III bankruptcy judge in a district and no Article III bankruptcy judges have been appointed in that entire circuit, the Chief Justice would be authorized to designate an Article III bankruptcy judge to sit in another circuit upon receiving a certificate of necessity from the chief judge of the circuit.

Under the Recommendation, the Judicial Council can respond to the changing needs of each judicial district in order to make the transition as smooth as possible.

C. Suggested Statutory Language

Transitioning the Non-Article III court to an Article III court will be a somewhat complicated process. The following suggested statutory language includes only the broad enabling legislation that would be required to enact an Article III bankruptcy court transition.[1824]

"**28 U.S.C. § 151 Creation and Composition of Bankruptcy Courts**

(a) In each judicial district in which a judge has been appointed to sit pursuant to section 152(a) of title 28, there shall be a court of record known as the United States Bankruptcy Court for the district.

(b) In each judicial district in which a bankruptcy judge has not been appointed under section 152(a) of title 28, the bankruptcy judges shall constitute a unit of the district court to be known as the bankruptcy court for that district. Each bankruptcy judge, as a judicial officer of the district court, may exercise the authority conferred under this chapter with respect to any action, suit, or proceeding and may preside alone and hold a regular or special session of the court, except as otherwise provided by law or by rule or order of the district court."

[1824] Certain sections of this draft statutory language was compiled from two draft statutes provided by Judge Joe Lee, on his own behalf, and by Robert A. Greenfield on behalf of the National Bankruptcy Conference.

"**28 U.S.C. § 152 Appointment and Number of Bankruptcy Judges**

(a) On and after the effective date of this Act, when a vacancy as defined in subsection (c) of this section occurs, the President shall appoint, by and with the advice and consent of the Senate, bankruptcy judges for the several judicial districts as follows: The total number of bankruptcy judges for each judicial district (including those bankruptcy judges appointed under this subsection and appointed under section 152(a)(1) of title 28 as in effect on the day before enactment of this Act) shall be the number authorized under this section before its amendment by the Act enacting this section. A bankruptcy judge appointed under this section shall hold office during good behavior.

(b) The judges of the district courts for the territories shall serve as the bankruptcy judges for such courts.

(c) With regard to a bankruptcy judge appointed under prior section 152(a)(1) of title 28, a vacancy as used in subsection (a) of this section shall occur upon the following events:

(1) natural expiration of the statutory term;
(2) appointment under subsection (a) of this section;
(3) resignation from the bench for any reason, including removal under subsection (e) of this section;
(4) retirement from the bench; or
(5) death."

**"28 U.S.C. § 298 Assignment of Bankruptcy Judges**

(a) The judicial council of each circuit created pursuant to section 332 of this title, may designate and assign one or more bankruptcy judges appointed under section 152(a) of this title, to sit in a district where a bankruptcy judge has not yet been appointed under section 152(a) of this title, whenever the business of that district so requires.

(b) The Chief Justice of the United States may designate and assign temporarily a bankruptcy judge appointed under section 152(a) of this title, of one circuit for service in another circuit, in a bankruptcy court, upon presentation of a certificate of necessity by the chief judge or circuit justice of the circuit wherein the need arises."[1825]

[1825] Proposed section 298(b) is taken from 28 U.S.C. § 205(e)(1) of Pub. L. 95-598 (Nov, 6, 1978), withdrawn by section 122(c) of Pub. L. 98-353 (July 10, 1984).

"**28 U.S.C. § 1334 Bankruptcy Cases and Proceedings**

(a) Except as provided in subsections (b) and (c) of this section, the district court shall have original and exclusive jurisdiction of all cases under title 11.

(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the court with original jurisdiction under either subsection (a) or subsection (c) of this section, the court with original jurisdiction under either subsection (a) or subsection (c) of this section shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to a case under title 11.

(c) Except as provided in subsection (b) of this section and notwithstanding the grant of jurisdiction in subsection (a) of this section, the bankruptcy court established by section 151(a) if this title shall have original and exclusive jurisdiction of all cases under title 11."

"**28 U.S.C. § 157 Procedures**

(a) A district court whose jurisdiction arises under section 1334(a) of title 28, or a bankruptcy court whose jurisdiction arises under section 1334(c) of title 28, may provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district.

[Remaining subsections of section 157 should refer to applicable court referring the case under subsection (a) of this section.]"

Conclusion

A great deal of the opposition to an Article III bankruptcy court may be ameliorated through consensual transition provisions. The Recommendation balances a number of competing interests in an attempt to treat all affected parties fairly. A smooth transition process to an Article III bankruptcy court will ensure that the interests of the sitting bankruptcy judges, court administration, and the users of the system are balanced against the need for a constitutionally sound court that can swiftly and finally decide bankruptcy and bankruptcy related issues. The Recommendation is designed to reduce the cost and delay inherent in the current system over time in order to avoid the confusion that may result from an immediate change.

### 3.1.3 *Bankruptcy Appellate Process*

**The current system which provides two appeals, the first either to a district court or a bankruptcy appellate panel and the second to the U.S.**

**Court of Appeals, as of right from final orders in bankruptcy cases should be changed to eliminate the first layer of review.**

An appellate system should provide stability and consistency in case law decision-making. The American court model is based on a structure in which trial courts make many rulings, some of which conflict with others, and appellate courts review those decisions, resolve disputes and, over time, promote the development of a coherent body of law.

The Constitution authorizes Congress to establish a uniform law of bankruptcies.[1826] Despite this clear constitutional mandate, the current bankruptcy appellate structure has yielded results which are far from uniform. Most appeals from bankruptcy court decisions go to the district courts. The decision of the district court binds the parties in the case but, because there may be multiple district judges in each district; often times the district court judges in the same district do not agree with each other. District court precedent in bankruptcy as a result is often in conflict. Under these circumstances, bankruptcy judges have a choice of which precedent to follow. Certain bankruptcy courts have held that the decision by one district judge does not create binding precedent for all of the bankruptcy judges within the district.[1827] Similarly, Bankruptcy Appellate Panel ("BAP") decisions often do not have precedential effect over either bankruptcy courts or district courts.[1828]

Only when a case is appealed a second time to the court of appeals will the decision create binding precedent within the circuit. Only when decisions from the

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[1826] U.S. CONST. art. I, § 8, cl. 4.

[1827] For cases in which bankruptcy courts have disregarded district court precedent in the same district, *see, e.g.*, *In re* Shattuc Cable Corp., 138 B.R. 557, 565-67 (Bankr. N.D. Ill. 1992); Pereira v. Centel Corp. (*In re* Argo Communications Corp.), 134 B.R. 776, 786 n.9 (Bankr. S.D.N.Y. 1991); *In re* California Gardens Apartments, Ltd., 130 B.R. 509, 514 (Bankr. S.D. Ohio 1991); *In re* Rheuban, 128 B.R. 551, 554-55 (Bankr. C.D. Cal. 1991); *In re* Morningstar Enter., Inc., 128 B.R. 102, 106 (Bankr. E.D. Pa. 1991); First Am. Bank v. Gaylor (*In re* Gaylor), 123 B.R. 236, 241-43 (Bankr. E.D. Mich. 1991).

[1828] For cases that refuse to follow Ninth Circuit BAP precedent, *see, e.g.*, Oregon v. Selden (*In re* Selden), 121 B.R. 59, 62 (D. Or. 1990); *In re* Junes, 76 B.R. 795, 797 n.1 (Bankr. D. Or. 1987), *aff'd on other grounds*, 99 B.R. 978 (B.A.P. 9th Cir. 1989); *In re* Crook, 62 B.R. 937, 941 n.2 (Bankr. D. Or. 1986), *rev'd*, 79 B.R. 475, 477 n.3 (B.A.P. 9th Cir. 1987); *In re* Kao, 52 B.R. 452, 453 (Bankr. D. Or. 1985). *But see* Bank of Maui v. Estate Analysis, Inc., 904 F.2d 470, 472 (9th Cir. 1990) (O'Scannlain, J., concurring); *In re* Windmill Farms, Inc., 70 B.R. 618, 622 (Bankr. 9th Cir. 1987), *rev'd on other grounds*, 841 F.2d 1467 (9th Cir. 1988); Mushkin, Inc. v. Industrial Steel Co. (*In re* Mushkin, Inc.), 151 B.R. 252, 253-55 (Bankr. N.D. Cal. 1993); *In re* General Assoc. Investors Ltd. Partnership, 150 B.R. 756, 760-61 (Bankr. D. Ariz. 1993); Coyne v. Westinghouse Credit Corp. (*In re* Globe Illumination Co.), 149 B.R. 614 (Bankr. C.D. Cal. 1993); *In re* Torrez, 132 B.R. 924, 943 (Bankr. E.D. Cal. 1991).

court of appeals are appealed to the Supreme Court is there a single, uniform rule binding on all bankruptcy courts. Moreover, because even the general rules are the subject of multiple nonbinding authority, even basic issues are litigated again and again.[1829]

Stare decisis is a fundamental tenet of our common law system, defined as "when [a] court has once laid down a principle of law as applicable to a certain set of facts, it will adhere to that principle, and apply it to all future cases where facts are substantially the same."[1830] Consistent application of the law leads to predictable outcomes, which leads to fewer appeals. Minimizing the number of appeals filed is a powerful policy reason behind a need for stare decisis. "Appeals are costly to litigants and society, and lower court departures from established reviewing court precedent would surely multiply appeals. Stare decisis discourages appeals, but this function is served only when litigants have reason to believe that the reviewing court will adhere to its prior decisions."[1831]

The problems that arise from a lack of effective stare decisis in a two-tier appellate system can not be overestimated. Because of the current multiple appellate structure, additional litigation does not result in binding precedent. Just as a lack of stare decisis results in costly and needless litigation, the existence of stare decisis will have the effect of reducing over time the number of bankruptcy appeals as issues of law become binding on a circuit-wide basis.

Concerns over cost and efficiency also support the Recommendation. Under the current system, every bankruptcy appeal is an expensive excursion for both debtor and creditor who must work through two layers of appeals for a final resolution of their disputes.[1832] More importantly, the conflicting opinions and uncertainty that result from district court appellate decisions impose very real costs on all parties who use the bankruptcy system.

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[1829] For examples of bankruptcy issues that are litigated again and again, see Paul M. Baisier & David G. Epstein, *Resolving Still Unresolved Issues of Bankruptcy Law: A Fence or an Ambulance*, 69 AM. BANKR. L.J. 525, 526-27 n.9 (1995)(hereinafter "Unresolved Issues").

[1830] Moore v. City of Albany, 98 N.Y. 396, 410 (1885). *See also* West, *The Doctrine of Stare Decisis*, 21 WAYNE L. REV. 1043 (1975).

[1831] Daniel J. Bussel, *Power, Authority, and Precedent in Interpreting the Bankruptcy Code*, 41 UCLA L. REV. 1063, 1072 (1994) (citing First of Am. Bank v. Gaylor (In re Gaylor), 123 B.R. 236, 241 (Bankr. E.D. Mich. 1991)).

[1832] Hon. Edith H. Jones, *Bankruptcy Appeals*, 16 T. MARSHALL L. REV. 245 (1991) ("disincentives to appeal — the cost, the inevitable delay, the possibility of jurisdictional dismissals that would accomplish nothing — are considerable.").

Without a predictable outcome on even the most basic issues, negotiations outside of court are skewed creating more litigation. Currently, case law can be found to support virtually any position on any issue and as a result, wasteful litigation ensues. Many, although not all, bankruptcy court opinions are published in a separate West and other reporters devoted to bankruptcy cases. Many bankruptcy opinions from the district courts are also published. The consequence is that about fourteen volumes of opinions of West's Reporter alone, few of which are binding on any other future case, are published each year. Practitioners assert that it is possible to find a bankruptcy opinion to support any legal proposition and any side of a legal proposition. As a result, no binding precedent exists in some circuits on certain fundamental bankruptcy issues.[1833]

The current appellate process provides a bankruptcy litigant with more access to direct appeals than a criminal defendant, a tax litigant, a tort victim, or almost anyone else in the federal system. This is a wasteful system in both time and money, with a great deal of duplication. Parties with greater resources to withstand a lengthy and expensive appellate process have a distinct advantage. This advantage is magnified in negotiations between a party who would benefit from delay and can afford to litigate and a party who needs a quick resolution and can not afford lengthy appeals.

A. Jurisdiction and Appellate Process of the Bankruptcy Courts

Original and exclusive jurisdiction of all bankruptcy cases currently resides in the district court.[1834] Similarly, original, but not exclusive, jurisdiction of all civil proceedings arising under, in, or related to, a case under title 11 also resides in the district court.[1835] Under 28 U.S.C. § 151, the bankruptcy courts are units of the district court. The district court has the power to refer "any or all cases under title

[1833] *Unresolved Issues*, *supra* note 1829, at 526-27 (using the example of claim classification as a case in point to list "the seven bankruptcy court decisions, one district court decision, and one court of appeals decision since 1993 that have either allowed or required separate classification of a secured creditor's unsecured deficiency claim, and five bankruptcy court decisions, one district court decision, five court of appeals decisions and two bankruptcy appellate panel decisions since 1991 that have prohibited the separate classification of such a deficiency claim. In other words, seventeen years after the enactment of the Bankruptcy Reform Act of 1978, there is substantial support in the case law for either position, and six of eleven judicial circuits have no binding precedent on this most basic question of substantive bankruptcy law.").

[1834] 28 U.S.C. § 1334 (a) (1994).

[1835] *Id.* at § 1334(b).

11 and any or all proceedings under title 11" to the bankruptcy court for that district and the power to withdraw a referred case or proceeding.[1836]

Title 28 gives the U.S. district courts jurisdiction to hear appeals from final judgments, orders, and decrees of the bankruptcy judges. The district courts also have discretionary jurisdiction to hear appeals from interlocutory orders and decrees of bankruptcy judges. Unless one of the parties opts out, all bankruptcy appeals in districts with bankruptcy appellate panels ("BAP") go from the bankruptcy court directly to the BAP. The courts of appeals have jurisdiction over appeals from all final orders, judgments, and decrees of the district courts and the bankruptcy appellate panels. The jurisdiction of the United States Supreme Court in bankruptcy matters is the same as its jurisdiction in ordinary civil matters.[1837]

B. Prior Attempts to Eliminate District Court Review

Elimination of district court review was considered and rejected by the 1970 Commission. The Commission Report cited (1) the geographic remoteness of the courts of appeals; (2) the risk of an overloaded appellate docket with appeals from litigants who may otherwise have been satisfied with a district court determination; and (3) that the courts of appeals would continue to hear appeals in those cases where "the stakes were sufficiently high" and the "correct resolution sufficiently in doubt" as to warrant review.[1838]

Two separate appellate routes were proposed during the deliberations prior to the enactment of the 1978 Bankruptcy Reform Act. The House Bill vested bankruptcy judges with Article III status and proposed that bankruptcy appeals go directly to the courts of appeals.[1839] The Senate Bill, under which bankruptcy judges did not have Article III status, proposed that bankruptcy appeals go to the district court, presumably following the 1970 Commission recommendation.[1840]

As a compromise of these two schemes, the 1978 Bankruptcy which did not confer Article III status on bankruptcy courts, provided that the initial appeal of a decision of the bankruptcy court would be to a district court, a bankruptcy appellate panel (in circuits where one had been established), or directly to the court of appeals

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[1836] *Id.* § 157(a), (d).

[1837] *Id.*, at § 158(a), (d).

[1838] COMMISSION REPORT, note 1728, at 96-98.

[1839] H.R. REP. NO. 95-595, at 39-43 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6000-04.

[1840] S. REP. NO. 95-989, at 18 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5804.

if both parties consented.[1841] Without explanation, direct appeals to the courts of appeals by consent was not carried over in the Bankruptcy Amendments and Federal Judgeship Act of 1984.[1842]

The factors that influenced the debate nearly thirty years ago have changed. Today, geographic remoteness of the courts of appeals is unlikely to add additional inconvenience and cost. As courts increasingly employ electronic filing and service of notices, appellate records, and briefs, location of the appellate court will matter less and less. Travel may be required only for oral argument and even then may be avoided by waiving oral argument or by video conferencing. The Court of Appeals for the Second Circuit is experimenting with oral argument by video rather than in person. The potential for an overloaded docket is addressed separately.[1843] The hope of the 1970 Commission that only important cases would reach the courts of appeals has not come to pass. The cost of bankruptcy appeals precludes resolution of numerous fundamental bankruptcy issues because the parties cannot afford to litigate them. As previously stated, no binding circuit authority exists for even the most fundamental bankruptcy issues. The cost and delay inherent in taking an appeal all the way to the courts of appeals has foreclosed effective stare decisis in subsequent bankruptcy cases and proceedings.

C. Appeals from Core and Noncore Orders

Section 157(b)(1) provides that bankruptcy judges may "hear and determine all cases under title 11 and all core proceedings arising under title 11" subject to

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[1841] Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, § 236(a), 92 Stat. 2549, 2667, added 28 U.S.C. § 1293(b) which provided:

> A court of appeal shall have jurisdiction of an appeal from a final judgment, order or decree of an appellate panel created under section 160 or a District court of the United States or from a final judgment, order, or decree of a bankruptcy court of the United States if the parties to such appeal agree to a direct appeal to the court of appeals.

*Id.* The consent requirement mitigated "the Senate objections against direct appeal to the court of appeals because it protects the litigants who might otherwise be deterred from appealing small matters to the court of appeals and lessens the caseload burden on the court of appeals." Lissa Lamkin Broome, *Bankruptcy Appeals: The Wheel is Come Full Circle*, 69 AM. BANKR. L.J. 541, 544 n.16 (1995).

[1842] *See* 1984 U.S.C.C.A.N. 576 and 28 U.S.C. § 158 (1994). *See also* REFORMING THE BANKRUPTCY CODE: THE NATIONAL BANKRUPTCY CONFERENCE'S CODE REVIEW PROJECT, FINAL REPORT, 53 (rev'ed. 1997) ("It is unclear whether there was a reason for the repeal of [direct consensual appeal to the court of appeals] or whether its elimination was due to oversight.").

[1843] *See* Section F. *infra*.

standard appellate review as provided in section 158.[1844] Unless the parties consent to the entry of a final order in a "related-to" proceeding (noncore), a bankruptcy judge can submit only proposed findings of fact and conclusions of law to the district judge for "de novo review." Assuming that the core/noncore distinction remains intact and is constitutional, direct appellate review is sound in core proceedings and in those noncore proceedings where the parties have consented to the entry of a final order by the bankruptcy judge.

In a noncore proceeding, where a bankruptcy judge has the authority only to submit proposed findings of fact and conclusions of law, the proceeding goes to the district court for "de novo review." This provision ensures that bankruptcy courts are not acting outside their jurisdiction.[1845] The entry of a final order by the district court is *not* part of the appellate process; it is the basic order from which an appeal is taken directly to the court of appeals as an order in any nonbankruptcy civil action. Sections 1291 and 1292 apply as do the Federal Rules of Appellate Procedure in place of Section 158(d) and Part VIII of the Federal Rules of Bankruptcy Procedure. As previously stated, the jurisdictional and procedural distinction between core and noncore would not be necessary if Congress enacts the Recommendation to grant Article III status to bankruptcy judges.

D. Constitutionality of Direct Appellate Review

The appellate structure has no effect on the constitutionality of the bankruptcy court system. To the extent that the current bankruptcy system is constitutionally sound, the Recommendation is constitutionally sound. To the extent that the current bankruptcy system is constitutionally infirm, the Recommendation does not remedy those faults. Direct appeals may, however, exacerbate the constitutionality problems that inhere in the current non-Article III system. While there is no constitutional distinction between having a case reviewed by the district court and by the court of appeals, the level of control currently exercised by the bankruptcy courts will become more evident if appeals are taken to the courts of appeals.

The constitutional infirmity, if any, rests in the original adjudication, not the appeal process. In the bankruptcy scheme of things, the factual trial is held in the non-Article III bankruptcy court and if the proceeding is noncore, *e.g.*, a *Marathon*-type of state law action, the final order must be entered by the Article III district court that can hear the proceeding de novo. Direct appeal to the circuit court need not eliminate this de novo hearing of noncore matters. The non-Article III debate is thus

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[1844] 28 U.S.C. § 157(b)(1) (1994).

[1845] *See* Survey: *Has Congress Really Solved the Controversy Surrounding the Jurisdiction of Bankruptcy Courts*, 5 J. BANKR. L. & PRAC. 513 (July/August 1996)(warning that expansive interpretation of "core" proceedings may impermissibly expand jurisdiction of bankruptcy courts).

not involved in the appellate review issue. Article III and *Marathon* are satisfied at the trial level.

E. Other Non-Article III Examples of Direct Circuit Court of Appeals Review

A number of non-Article III courts have direct appeals to the courts of appeals.

*Magistrate Judge Model*. The Federal Magistrates Act of 1979 (as amended) authorizes magistrate judges to conduct civil trials and enter judgments with the consent of the parties.[1846] In addition, a district court judge may designate a magistrate to hear and determine any pending pretrial matter *without the consent of the parties*.[1847] A district court judge makes a "de novo determination"[1848] of only those portions of the magistrate judge's report or specified findings to which objection is made.[1849] Final decisions of magistrate judges are directly appealable to the applicable court of appeals and are subject to ordinary appellate review.[1850] Appellate jurisdiction over a magistrate judge's orders is based on the specific grant in section 636(c) rather than on the general grant of appellate jurisdiction in 28 U.S.C. § 1291 over appeals from final orders of district courts.[1851] The Supreme Court has not reviewed whether the authority of magistrate judges to preside over civil trials with the consent of the parties passes muster under Article III.[1852] Eleven circuit

[1846] 28 U.S.C. § 636 (c)(1) (1994).

[1847] 28 U.S.C. § 636(b)(1) (1994) (emphasis added).

[1848] The Supreme Court has held that "de novo determination" does not mean "de novo hearing." United States v. Raddatz, 447 U.S. 667, 673 (1980)("It should be clear on these dispositive motions, the statute calls for a de novo determination, not a de novo hearing. We find nothing in the legislative history of the statute to support the contention that the judge is required to rehear the contested testimony in order to carry out the statutory command to make the required 'determination.'"), *reh'g denied*, 449 U.S. 911 (1980).

[1849] *Id.*

[1850] 28 U.S.C. § 636(c)(3) (1994).

[1851] Garland v. Sullivan, 737 F.2d 1283, 1285 & n.1 (3d Cir. 1984) (appellate jurisdiction over magistrate's orders based on section 636(c) and not section 1291), *aff'd on other grounds*, 474 U.S. 34 (1985).

[1852] The Supreme Court has, however, upheld magistrate judge authority under the following circumstances: McCarthy v. Bronson, 111 S.Ct. 1737 (1991) (prisoner litigation challenging prison conditions); Peretz v. United States, 111 S. Ct. 2661 (1991) (felony voir dire with defendant's consent); Gomez v. United States, 490 U.S. 858 (1989) (felony voir dire over defendant's objection); United States v. Raddatz, 447 U.S. 667 (1980) (evidentiary hearing in motion to suppress

courts, however, have upheld a magistrate judge's jurisdiction over a wide variety of civil cases with the consent of the litigants.[1853]

In June, 1993, the Magistrate Judges Division of the Administrative Office of the U.S. Courts published "A Constitutional Analysis of Magistrate Judge Authority"[1854] noting that *Gomez v. United States*,[1855] and *Granfinanciera, S.A. v. Nordberg*,[1856] "had raised serious questions about what matters non-Article III judicial officers may handle."[1857] The Magistrate Report relied on the "key element of litigant consent" to distinguish both *Marathon* and *Granfinanciera* from the Magistrate Act system.[1858] The importance of litigant consent to support the jury trial right in *Granfinanciera* was reinforced by the Supreme Court's holding in *Langenkamp v. Culp*,[1859] that a defendant in a preference action had no jury trial right where it had filed a claim as a creditor prior to the commencement of the preference action.

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proceedings), *reh'g denied*, 448 U.S. 916 (1980); Mathews v. Weber, 423 U.S. 261 (1976) (Social Security proceedings); Wingo v. Wedding, 418 U.S. 461 (1974) (habeas corpus proceedings).

[1853] *See* Bell & Beckwith v. U.S., 766 F.2d 910 (6th Cir. 1985) (interpleader action over investment account); D.L. Auld Co. v. Chroma Graphics Corp., 753 F.2d 1029 (Fed. Cir.) (patent infringement case; appeal challenging constitutionality of § 636(c) was an abuse "of the judicial process" which warranted an award of attorneys' fees under 35 U.S.C. § 285), *cert. denied*, 474 U.S. 825 (1985); Gairola v. Virginia Dep't of Gen. Servs., 753 F.2d 1281 (4th Cir. 1985) (Title VII action); KMC Co., Inc. v. Irving Trust Co., 757 F.2d 752 (6th Cir. 1985) (breach of contract action); Lehman Bros. Kuhn Loeb, Inc. v. Clark Oil & Refining Corp., 739 F.2d 1313 (8th Cir. 1984) (breach of contract action), *cert. denied*, 469 U.S. 1158 (1985); Collins v. Foreman, 729 F.2d 108 (2d Cir.) (section 1983 action), *cert. denied*, 469 U.S. 870 (1984); Geras v. Lafayette Display Fixtures, Inc., 742 F.2d 1037 (7th Cir. 1984) (state law negligence and strict liability tort action); Goldstein v. Kelleher, 728 F.2d 32 (1st Cir.) (medical malpractice case), *cert. denied*, 469 U.S. 852 (1984); Puryear v. Ede's Ltd., 731 F.2d 1153 (5th Cir. 1984) (breach of contract action); Pacemaker Diagnostic Clinic of Am., Inc. v. Instromedix, Inc., 725 F.2d 537 (9th Cir.) (en banc) (patent infringement case), *cert. denied*, 469 U.S. 824 (1984); Fields v. Washington Metro. Area Transit Auth., 743 F.2d 890 (D.C. Cir. 1984) (personal injury action); Wharton-Thomas v. United States, 721 F.2d 922 (3d Cir. 1983) (lawsuit under federal tort claims act).

[1854] 150 F.R.D. 247 (1993)(hereinafter "*Magistrate Report*").

[1855] 490 U.S. 858 (1989).

[1856] 492 U.S. 33 (1989).

[1857] *Magistrate Report*, *supra* note 1854, at 251.

[1858] *Id.* at 289.

[1859] 498 U.S. 42 (1990), *reh'g denied*, 498 U.S. 1043 (1991).

The Magistrate Report concludes that the Magistrate Act satisfies the personal and structural components of Article III.[1860] Litigant consent to the entry of a final order by the magistrate judge adequately waives the personal right to have a proceeding heard by an Article III judge.[1861] Similarly, as adjuncts of the district court, magistrate courts do not usurp the power of the Article III judiciary, "even when they exercise civil trial authority."[1862] The Magistrate Report concludes that these factors, combined with clear congressional intent, would lead a majority of the Court to "uphold the consensual civil trial authority of magistrate judges if the right case was presented to it."[1863]

*Tax Court Model*. The tax court system also provides for direct court of appeals review of orders by non-Article III courts. At the option of the taxpayer, IRS rulings are reviewable by an Article I tax court.[1864] Final orders of the Article I tax court are reviewable by the court of appeals in the circuit where the taxpayer resides "in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury."[1865] Because Article I review in this context is at the option of the taxpayer, litigant consent exists in this scheme similar to that required under the Magistrate's Act.

*Administrative Agency Model*. In addition to the magistrate and tax schemes, many other administrative schemes provide for direct appeal to the courts of appeals from Article I adjudications. For example, approximately 45 administrative schemes provide for appeals either to the Court of Appeals for the D.C. Circuit or to the regional court of appeals from two types of adjudications: (1) directly from an Article I administrative agency or (2) from the appropriate district court.[1866] Administrative

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[1860] *Magistrate Report*, *supra* note 1854, at 303.

[1861] *Id.*

[1862] *Id.*

[1863] *Id.* at 304. *See* Monique Mulcare, *Article III, The Federal Magistrate, and the Power of Consent*, 1992/93 ANN. SURV. AM. L. 297 (1994) (addressing the proper constitutional role of a magistrate supervising part of a criminal trial); Note, *Federal Magistrates and the Principals of Article III*, 97 HARV. L. REV. 1947 (1984) (concluding that the 1979 Federal Magistrate Act is constitutional).

[1864] 26 U.S.C. § 7429(b)(2) (1994).

[1865] *Id.* § 7482(a).

[1866] *See, e.g.*, 15 U.S.C. § 78y(a)(1) (appeals from decisions of the SEC); 29 U.S.C. § 160(f) (appeals from decisions of the NLRB); 29 U.S.C. § 210(a)(appeals under the Fair Labor Standards Act of 1938); 15 U.S.C. § 57a(e) (appeals under the Federal Trade Commission Improvement Act);

agency determinations under certain legislation may be appealed *only* to the Court of Appeals for the D.C. Circuit.[1867] Moreover, the delegation of certain matters for adjudication by administrative agencies—occasionally without any Article III judicial review—has been countenanced by the Supreme Court.[1868]

F. Impact of Direct Court of Appeals Review

Direct appeals to the courts of appeals may increase the burden on those appellate courts. By eliminating the first round of appeals from the appellate process, more cases will go to the courts of appeals for resolution. Although this will have the salutary effect of establishing consistent legal precedent within the circuit, initially it will impose a somewhat increased decision-making burden on the appellate courts. Over time, however, this burden should decrease as more issues are settled within the circuit and fewer uncertainties linger, necessitating fewer appeals.

*Historical Court of Appeals Statistics.* The data for bankruptcy appeals in the current system may shed some light on the predicted impact of eliminating the first layer of review of bankruptcy orders.[1869] For the year ending June 30, 1997, there

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15 U.S.C. § 1710(a) (appeals under the Housing and Urban Development Act of 1968); 29 U.S.C. § 660(a) (appeals under the Occupational Safety and Health Act of 1970); 42 U.S.C. § 300J-7(a)(2) (appeals under the Safe Drinking Water Act); 45 U.S.C. § 355(f) (appeals under the Railway Labor Act); 5 U.S.C. § 552b(g) (appeals under the Administrative Procedures Act); and 28 U.S.C. § 2343 (review of federal agency orders); *see also* 28 U.S.C. § 1491 *et seq*. (dictating that all appeals from the United States Court of Federal Claims go to the Court of Appeals for the Federal Circuit). *See* Gordon Bermant, The Cases of the United States Court of Appeals for the District of Columbia Circuit, Appendix A, p. 44-45 (Federal Judicial Center 1982).

[1867] *See, e.g.*, 47 U.S.C. § 402(b) (Communications Act Amendments of 1952); 15 U.S.C. § 766(c) (Department of Energy Organization Act); 26 U.S.C. § 9011 (Federal Election Campaign Act Amendments of 1974); 22 U.S.C. § 4109(a) (Foreign Service Act of 1980); 42 U.S.C. § 4915(a) (Noise Control Act of 1972); 42 U.S.C. § 9125 (Ocean Thermal Energy Conservation Act); 43 U.S.C. § 1349(c)(l) (Outer Continental Shelf Lands Act Amendments of 1978); 42 U.S.C. § 6976(a)(1) (Resource Conservation and Recovery Act of 1976); and 42 U.S.C. § 300J-7(a)(1) (Safe Drinking Water Act). *See* Bermant, *supra* note [1866], at 43.

[1868] *See* Thomas v. Union Carbide Agric. Prods., 473 U.S. at 568, 583 ("the Court has long recognized that Congress is not barred from acting pursuant to its powers under Article I to vest decision making authority in tribunals that lack the attributes of Article III courts. Many matters that involve the application of legal standards to facts and affect private interests are routinely decided by agency action with limited or no review by Article III courts." [citations omitted])

[1869] The statistics on appeals to the courts of appeals and the district courts were provided by the Administrative Office of the U.S. Courts (On file with the National Bankruptcy Review Commission). The statistics on appeals to the various Bankruptcy Appellate Panels were provided by the individual clerks in charge of each respective BAP (On file with the National Bankruptcy Review Commission).

were a total of 40,093 appeals for all areas of the law pending in the courts of appeals. Of these appeals, bankruptcy appeals comprised 944 (2% of all appeals filed). In the district courts, 3,588 bankruptcy appeals were filed and a total of 1,293 appeals were filed in the First, Second, Sixth, Eighth, Ninth, and Tenth Circuit Bankruptcy Appellate Panels.[1870] Assuming no other changes in the appellate system, the approximate impact of the Recommendation would result in an increase of 3,937 appeals to the courts of appeals (net increase of 9%).

These predictions (both above and below) represent a worst-case scenario. The post-Recommendation appeals figures assume that (1) every appeal currently filed in the district court would be filed in the court of appeals, and (2) improved stare decisis will not diminish the number of appeals taken. However, these two factors are likely to result in far fewer appeals to the courts of appeals than those predicted. The figures upon which the predictions have been based arose under a multiple appeal system where stare decisis was largely ineffective. In fact, the Recommendation should result in fewer total appeals than those predicted above and below.

[1870] The figures for some of the BAPs do not conform to the statistical year due to the staggered dates when some of them began accepting appeals.

2. Impact By Circuit

**Bankruptcy Appeals as a Percentage of Total Appeals Pending By Circuit**
**July 1, 1996 through June 30, 1997**

| Circuit Court | Before the Recommendation | After the Recommendation (Worst Case Scenario) |
|---|---|---|
| D.C. Circuit | .2% | 1% |
| First Circuit | 2% | 21%[1871] |
| Second Circuit | 2% | 18%[1872] |
| Third Circuit | 4% | 16% |
| Fourth Circuit | 2% | 9% |
| Fifth Circuit | 2% | 8% |
| Sixth Circuit | 2% | 10%[1873] |
| Seventh Circuit | 2% | 11% |
| Eighth Circuit | 2% | 9%[1874] |
| Ninth Circuit | 4% | 15%[1875] |
| Tenth Circuit | 2% | 13%[1876] |
| Eleventh Circuit | 2% | 7% |

G. Bankruptcy Appellate Panel System

Bankruptcy Appellate Panels ("BAP") are alternatives to district court appellate review. Under section 158(c)(1), all appeals from a bankruptcy court in a district that has authorized appeals to the BAP are heard by the BAP, unless one of the parties opts out. Currently, the First, Second, Sixth, Eighth, Ninth and Tenth

[1871] Includes 134 appeals filed in the First Circuit BAP between 7/1/96 and 6/30/97.

[1872] Includes 89 appeals filed in the Second Circuit BAP between 7/1/96 and 9/12/97.

[1873] Includes 91 appeals filed in the Sixth Circuit BAP between 1/1/97 and 8/15/97.

[1874] Includes 82 appeals filed in the Eighth Circuit BAP between 1/1/97 and 9/19/97.

[1875] Includes 783 appeals filed in the Ninth Circuit BAP between 7/1/96 and 6/30/97.

[1876] Includes 114 appeals filed in the Tenth Circuit BAP between 7/1/96 and 9/19/97.

Circuits have BAPs circuit-wide or only in a portion of the circuit and some other circuits are developing such panels.[1877] The Second Circuit BAP system includes the Districts of Connecticut and Vermont, and the Northern District of New York, but excludes the most active districts, the Southern and Eastern Districts of New York.[1878] The Third, Fourth, Fifth, and Eleventh Circuits have decided not to create BAPs. The Seventh Circuit has deferred its BAP decision.

Once a BAP is created, section 158(b)(6) provides that district judges determine whether appeals may be heard by a BAP in lieu of the district court. A BAP consists of three bankruptcy judges sitting as a panel to hear and decide appeals from bankruptcy court decisions. The parties to an appeal must consent to appellate review by a BAP. Failure of one party to consent means that the appeal is heard by the district court. An appeal from the BAP goes to the circuit court.

BAPs are a voluntary alternative to the district court, which means that any party facing an appeal in front of a BAP that previously has ruled unfavorably on the issue presented in the instant case can simply refuse to consent to appellate review by the BAP. The ability of individual districts to "opt out" of the BAP appellate process (within a circuit that has adopted it) further fractures any stare decisis hopes pinned on the BAP system. BAPs may actually accelerate the divergence of views on various legal questions; a combined BAP/district court appellate structure, as exists in all BAP circuits, does not create binding precedent with a single appeal. "Whatever arguments can be made in support of the creation of a bankruptcy appellate panel, the development of binding precedent is not one of them."[1879] The BAP program also

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[1877] The Bankruptcy Reform Act of 1994 made the BAP requirement mandatory unless the judicial council finds that there are insufficient funds or would result in undue delay. 28 U.S.C. § 158(b)(1) (1994).

[1878] With the exception of the Western District of New York (29 bankruptcy appeals filed for the year ended June 30, 1997), the lowest number of bankruptcy appeals to the district court are filed in the Second Circuit BAP districts. For the year ended June 30, 1997: 18 bankruptcy appeals were filed in the District of Connecticut; 32 bankruptcy appeals were filed in the Northern District of New York; and, 18 bankruptcy appeals were filed in the District of Vermont. By way of comparison, a total of 318 bankruptcy appeals were filed in the Eastern and Southern Districts of New York during this same period.

[1879] *Unresolved Issues*, *supra* note 1829, at 531 (citations omitted). BAPs actually exacerbate stare decisis problems because their holdings are not binding. Baisier and Epstein went on to describe the BAP stare decisis problem:

> Looking to the experience of the Ninth Circuit, the precedential effect of a decision of a bankruptcy appellate panel is problematic for at least the following reasons:
>
> 1. The Ninth Circuit has held that the decisions of its bankruptcy appellate panel are not binding on the district courts in the Ninth Circuit because Article III district court judges cannot constitutionally be bound by the decisions of the

"has 'a cost to the system' since 'three judges will be paid to do what one judge is doing now.'"[1880] Moreover, parties may appeal from a BAP decision to the court of appeals, just as they may from a district court decision. Thus, a BAP does not necessarily reduce the number of appeals, it is merely an alternative to the district court.

## H. Academic Analysis of Direct Appellate Review of Final Bankruptcy Court Orders

Currently, section 158(a) provides that all appeals from bankruptcy court orders shall be routed through the district court or the BAP. However, because a final order is subject to ordinary appellate review at the district court or BAP level, "[n]o one has demonstrated why bankruptcy appeals should be burdened by the extra cost and delay of an 'extra' level of appeal at the district court level."[1881]

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> Article I bankruptcy court judges who sit on a bankruptcy appellate panel under 28 U.S.C. § 158(b) (citations omitted);
> 2. Since a bankruptcy appellate panel sits in lieu of a district court, its opinions may only have stare decisis effect within the district from which the appeal was taken;
> 3. If as suggested above, district court opinions do not bind the bankruptcy courts sitting in the same district, then the opinions of the bankruptcy appellate panel (which sits in lieu of the district court) cannot bind those same bankruptcy courts, and thus bind no one; and
> 4. A bankruptcy appellate panel may not have the power to set precedent at all because it is an Article I court and, as such, has authority only to the extent that the parties consent to be bound by it.

*Unresolved Issues*, *supra* note 1829, at 531 (citations omitted).

[1880] Bankruptcy Appeals, *Lawyers Wary of New System Begun This Month*, N.Y.L.J., July 11, 1996 (comments of Judge Tina Brozman, recently appointed to sit on second circuit BAP).

[1881] Nathan B. Feinstein, *The Bankruptcy System: Proposals to Restructure the Bankruptcy Court and Bankruptcy Appellate Processes*, 1995-96 NORTON'S ANN. SURV. BANKR. LAW 517, 521 (hereinafter "Bankruptcy Proposal") (arguing for the removal of district court appellate review of bankruptcy court orders); *accord* Paul M. Baisier & David G. Epstein, *Resolving Still Unresolved Issues of Bankruptcy Law: A Fence or an Ambulance*, 69 AM. BANKR. L.J. 525, 537 (1995) (arguing in favor of the direct appeal of bankruptcy court decisions to an Article III panel of judges); REFORMING THE BANKRUPTCY CODE: THE NATIONAL BANKRUPTCY CONFERENCE'S CODE REVIEW PROJECT, FINAL REPORT 73 (rev. ed. 1997) (proposing that appeals from final bankruptcy court orders should go directly to the courts of appeals if the parties consent); Honorable Steven W. Rhodes, *Eight Statutory Causes of Delay and Expense in Chapter 11 Cases*, 67 AM. BANKR. L.J. 287, 296 (1993) (bankruptcy court decisions should be appealed directly to three-judge panel of Article III judges); *cf.* Daniel J. Bussel, *Power, Authority, and Precedent in Interpreting the Bankruptcy Code*, 41 UCLA L. REV 1063, 1094 (1994) (arguing that direct appeals would over-burden the courts of appeals and lead to excessive delay; proposing that district courts and BAP's be bound by "law of the district" as a way to clarify current stare decisis problems).

Current judicial planning trends also favor expansion of direct non-Article III appeals to circuit level Article III appellate courts.[1882] One commentator has noted the Judicial Conference's specific bankruptcy appeal recommendation that "the dispositive orders of bankruptcy judges should be reviewable *directly* in the court of appeals where the parties stipulate, or the district court or the BAP certifies, that such review is needed immediately to establish legal principles on which subsequent proceedings in the case may depend."[1883] Although the Judicial Conference's bankruptcy proposal is less sweeping than its proposal vis-á-vis other non-Article III courts, it is an improvement over its November 1994 recommendation that appeals from all "[f]inal orders of bankruptcy judges should continue to be reviewable by Article III judges in the district court."[1884] This 'about-face' by the Judicial Conference has been attributed to "vigorous testimony and opposition to its earlier Recommendation by members of the practicing bankruptcy bar and certain academics."[1885]

Another proposal suggested a return to direct court of appeals review with the consent of the parties. All other appeals would continue to go to the district court.[1886] One commentator urges that mandatory direct appeal to the courts of appeals may be more remedy than most parties want or are willing to pay for.[1887]

### 3.1.4 *Interlocutory Appeals of Bankruptcy Orders*

**28 U.S.C. § 1293 should be added to provide, in addition to the appeal of final bankruptcy orders, for the appeal to the courts of appeals of interlocutory bankruptcy court orders under the following circumstances: (1) an order to increase or reduce the time to file a plan under section 1121(d); (2) an order granting, modifying, or refusing to grant an injunction or an order modifying or refusing to modify the**

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[1882] *See* COMMITTEE ON LONG RANGE PLANNING OF THE JUDICIAL CONFERENCE OF THE UNITED STATES, PROPOSED LONG RANGE PLAN FOR THE FEDERAL COURTS (March 1995) (recommending that "[i]n general, the decisions of . . . Article I courts should be reviewable directly in the regional courts of appeals [Recommendation 21, p. 44]).

[1883] *Bankruptcy Proposal*, *supra* note 1881, at 522 (emphasis added).

[1884] *Id*.

[1885] *Id.*, at 522 n.6.

[1886] Lissa Lamkin Broome, *Bankruptcy Appeals: The Wheel Has Come Full Circle*, 69 AM. BANKR. L.J. 541, 546 (1995) (citing statistics demonstrating that direct appeals to the courts of appeals rose "modestly" between 1978 and 1984).

[1887] *Id.* at 549.

> **automatic stay; (3) an order appointing or refusing to appoint a trustee, or authorizing the sale or other disposition of property of the estate; (4) where an order is certified by the bankruptcy judge that (x) it involves a controlling issue of law to which there is a substantial difference of opinion, and (y) immediate appeal of the order may materially advance resolution of the litigation, and leave to appeal is granted by the court of appeals; and (5) with leave from the court of appeals.**

A tangential issue to the Recommendation on direct appeals concerns the types of interlocutory orders that might be directly appealable to the courts of appeals. Even with an expanded bankruptcy concept of finality, a clear definition of appealability remains elusive. Defining the circumstances under which an interlocutory order may be appealed is a necessary step to ensure that the proposed modifications to the bankruptcy appellate process are successful in achieving the desired results, such as stare decisis, while avoiding the pitfalls, such as an overloaded courts of appeals docket. As a result, whether an interlocutory order may be appealed should remain within the discretion of the courts of appeals. This is consistent with the rule currently provided for interlocutory district court orders under 28 U.S.C. §§ 1291 and 1292(b).[1888] Review of the types of interlocutory bankruptcy orders that have warranted appeal and, conversely, those that have been found not final for appeal purposes demonstrates that a clear rule is necessary.[1889]

Section 158(a) currently provides that an interlocutory order of a bankruptcy judge may be appealed to the district court (1) if issued under section 1121(d) to increase or to reduce the time for certain parties in interest to file a plan, or (2) with leave of the district court.[1890] Title 28 also provides that an interlocutory order of a district court judge may be appealed to the court of appeals if (1) it grants, modifies, or refuses to grant an injunction; (2) it appoints a receiver, winds up a receivership, or orders the sale or disposal of property; (3) it determines the rights and liabilities in an appealable admiralty case; or (4) the district judge certifies that the order involves a controlling issue of law to which there is a substantial difference of opinion, and

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[1888] Section 1292 dictates the circumstances under which interlocutory orders of the district courts may be appealed. Specifically, section 1292(b) provides that if a district court judge states in an interlocutory order that (1) it involves "a controlling question of law to which there is substantial ground for difference of opinion" and (2) "an immediate appeal from the order may materially advance the ultimate termination of the litigation" the court of appeals has discretion to permit a timely (within ten days) appeal of the district court's interlocutory order. 28 U.S.C. § 1292(b) (1996).

[1889] *See, e.g.,*CHARLES ALAN WRIGHT, ET AL.,, FEDERAL PRACTICE & PROCEDURE, JURISDICTION & RELATED MATTERS, § 3926.2 (Supp. 1996).

[1890] 28 U.S.C. § 158(a) (1994).

immediate appeal of the order may materially advance resolution of the litigation; and the court of appeals, in its discretion, grants leave to appeal.[1891]

Bankruptcy is different than civil litigation. Numerous substantive orders are entered during the course of a bankruptcy case, though technically the "final" order is the order confirming the plan in a Chapter 9, 11, or 12 case or discharging the debtor in a Chapter 7 or a Chapter 13 case. It would be procedurally and substantively unworkable for the order confirming the plan or discharging the debtor to be the only appealable order. The solution is to permit the appeal of certain interlocutory orders. Due to the nature of bankruptcy matters, however, appealable interlocutory orders are difficult to define with any precision. A list of appealable interlocutory orders would be at once over- and under-inclusive. A recent commentator proposed that an interlocutory bankruptcy order should be appealable if it is "both procedurally complete and determinative of substantive rights."[1892] This approach is consistent with the Commission's Recommendation to define only a few appealable interlocutory orders and leave all other determinations up to the court of appeals.

The Recommendation is an amalgamation of the current interlocutory appeal provisions contained in section 158(a) and section 1292(a) and (b). An appeal as of right is provided for certain specific interlocutory orders consistent with the current appellate practices of both the district courts and the courts of appeals. In addition, the Recommendation gives the courts of appeals discretion to grant an appeal of both certified and uncertified interlocutory orders. By giving discretion to the courts of appeals, the Recommendation avoids the problems inherent in attempting to codify all of the interlocutory orders that may be appealed. The parties to a dispute are in the best position to persuade or dissuade the court of appeals to grant appeal of an interlocutory order.

*Competing Considerations.* It may be argued that the latitude granted by the Recommendation to the courts of appeals is too broad to assure review of important interlocutory bankruptcy orders. If so, the Recommendation would diminish the stare decisis benefits of direct appeals. The Recommendation is not too broad. It essentially codifies the interlocutory appeal provisions between the bankruptcy court and the district court and the district court and the court of appeals.

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[1891] 28 U.S.C. §§ 1292(a) & (b) (1996).

[1892] John P. Hennigan, *Toward Regularizing Appealability in Bankruptcy*, 12 BANKR. DEV. J. 583, 587-88 (1996) ("Procedural completeness is achieved upon the resolution of all non-ministerial litigation within a unit. An order determines substantive rights when it decides the sorts of entitlements at issue in civil litigation outside bankruptcy, that is, rights to money damages, property, or injunctions.").

**Sample of Draft Statutory Provision**

28 U.S.C. § 1293. Bankruptcy court decisions

(a) The courts of appeals shall have jurisdiction of final judgments, orders and decrees of bankruptcy judges entered in cases and proceedings under section 157 of this title. An appeal under this subsection or under subsection (b) shall be taken only to the court of appeals for the judicial circuit in which the order or decree is entered;

(b) The courts of appeals shall have jurisdiction of the following orders:

(1) Interlocutory orders and decrees of bankruptcy judges,

(A) granting, continuing, modifying, refusing, or dissolving injunctions, or refusing to dissolve or modify injunctions;

(B) modifying or refusing to modify the automatic stay created by section 362 of title 11;

(C) appointing a trustee or refusing to appoint a trustee, authorizing a sale or other disposition of property of the estate; and

(D) increasing or reducing the time periods referred to in section 1121(b) and (c) of title 11; and

(E) with leave of the court from other interlocutory orders and decrees.

(2) When a bankruptcy judge, in making an order not otherwise appealable under this section, shall be of the opinion that such order involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate resolution of the proceeding, the bankruptcy judge shall so state in writing in such order. The Court of Appeals which would have jurisdiction of an appeal of such action may thereupon, in its discretion, permit an appeal to be taken from such order, if application is made within ten days after the entry of the order; *provided, however,* that application for an appeal hereunder shall not stay proceedings in the bankruptcy court unless the bankruptcy judge or the Court of Appeals or a judge thereof shall so order.

### 3.1.5 *Venue Provisions under 28 U.S.C. § 1408*

**28 U.S.C. § 1408(1) should be amended to prohibit corporate debtors from filing for relief in a district based solely on the debtor's incorporation in the state where that district is located.**

**The affiliate rule contained in 28 U.S.C. § 1408(2) should be amended to prohibit a corporate filing in an improper venue unless such debtor's**

**corporate parent is a debtor in a case under the Bankruptcy Code in that forum. Section 1408(2) should be amended as follows:**

> **(2) in which there is pending a case under title 11 concerning such person's affiliate, as defined in section 101(2)(A) of title 11, general partner, partnership, or a partnership controlled by the same general partner.**

**The court's discretionary power to transfer venue in the interest of justice and for the convenience of the parties should not be restricted.**

Current bankruptcy venue options for corporations and partnerships permit filings in the (1) place of incorporation or organization; (2) location of principal assets; or (3) location of principal place of business.[1893] For the majority of business debtors, these options afford a choice of only one or two bankruptcy venues. For large corporations, however, the current venue provisions afford a wide range of geographic options for filing bankruptcy. Frequently, large corporations are organized in one state, have their headquarters in another, and arguably have their principal assets in yet a third (and sometimes more) locales. In a Chapter 11 reorganization case, these choices can make the choice of a bankruptcy venue a strategic one, where a debtor may be able to shape the course of its reorganization depending on its choice of venue. To the extent the creditors' interests are aligned with the debtor's interests, this choice can be a mutually beneficial one. The other side of venue choice, however, is when these interests are not aligned, and the debtor's choice of venue has the effect of disenfranchising its creditors and may prevent them from actively participating in the case and defending their claims. Smaller creditors are the ones who are disenfranchised by a bankruptcy filing in a distant forum; enough money will always be at stake for larger creditors to defend their interests no matter where the bankruptcy case is filed.

The Commission's Recommendation is designed to prevent this type of forum-shopping by large Chapter 11 debtors and their affiliates by limiting venue options to the debtor's principal place of business or location of principal assets.

A. Venue Under the Bankruptcy Act of 1898

Under the Bankruptcy Act of 1898, Section 2a(1) did not distinguish between natural persons and fictitious entities, using the generic term "persons" that was

[1893] 28 U.S.C. § 1408(1) (1994).

defined to include fictitious entities, such as corporations and partnerships.[1894] The specific enumeration of each term in the statute maintained a legal distinction between the terms "residence" and "domicile." For natural persons, that distinction was more readily drawn: "domicile" was defined as an individual's actual residence coupled with a present intention to remain there. It "is the place where one has his true, fixed, permanent home, and principal establishment, and to which, when he is absent, he has the intention of returning, and where he exercises his political rights."[1895] "Residence," by contrast, does not require the intention to remain and may be nothing more than a place of "sojourn."[1896] The clear distinction between "residence" and "domicile" did not work for corporations. It was argued that despite the statute's delineation, the terms "residence" and "domicile" had to be identical for a corporation unless a corporation could be said to reside wherever it did *some* business. In order to ameliorate the interpretive difficulties and bring the venue provision in line with the interpretation in ordinary civil cases, the "residence" and "domicile" of a corporation were treated identically, as the state of incorporation.[1897]

In 1973, Bankruptcy Rule 116(a) revised Section 2a(1) in order to resolve the domicile/residence ambiguity. Rule 116(a) eliminated the place of incorporation (residence/domicile) option for purposes of establishing venue. The venue

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[1894] Section 2a(1) provided in pertinent part that:

**§2. Creation of Courts of Bankruptcy and Their Jurisdiction.** a. The courts of the United States hereinbefore defined as courts of bankruptcy are hereby created courts of bankruptcy and are hereby invested, within their respective territorial limits as now established or as they may be hereafter changed, with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in proceedings under this Act, in vacation, in chambers, and during their respective terms, as they are now or may be hereafter held, to--

(1) Adjudge *persons* bankrupt who have had their principal place of business, resided, or had their domicile within their respective territorial jurisdictions for the preceding six months, or for a longer portion of the preceding six months than in any other jurisdiction.

[1895] 1 COLLIER ON BANKRUPTCY ¶ 2.16, at 207 (Lawrence P. King et al., eds., 14th ed. 1988).

[1896] *Id.* at 208.

[1897] *See* Shaw v. Quincy Mining Co., 145 U.S. 444, 450 (1892) ("the legal existence, the home, the domicile, the habitat, the residence, the citizenship of the corporation can only be in the state in which it was created, although it may do business in other states whose laws permit it."); *In re* Triton Chem. Corp., 46 F. Supp. 326, 328 n.1 (D. Del. 1942); *In re* R.C. Stanley Shoe Co., 8 F. Supp. 681, 633 (D.N.H. 1934).

determination under Rule 116(a) was determined by the district where the corporation had its "principal place of business or principal assets."[1898]

## B. Venue Under the 1978 Reform Act

The 1978 Reform Act changed the venue provisions.[1899] Title 28 now provides that the proper place to file a petition under the Bankruptcy Code is in the district where the debtor's domicile, residence, principal place of business is located, or principal U.S. assets were located for the greater part of the preceding 180 days.[1900]

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[1898] Bankruptcy Rule 116(a) provided:

(a) Proper Venue

> (1) *Natural Person.* A petition by or against a natural person may be filed in the district where the bankrupt has had his principal place of business, residence, or domicile for the preceding six months or for a longer portion thereof than in any other district. A petition by or against a natural person who has had no principal place of business, residence, or domicile within the United States during the preceding six months may be filed in a district wherein he has property.
>
> (2) *Corporation or Partnership*. A petition by or against a corporation or partnership may e filed in the district (A) where the bankrupt has had its principal place of business or principal assets for the preceding six months or for a longer portion thereof than in any other district; or, (B) if there is no such district, in any district where the bankrupt has property.
>
> (3) *Partner with Partnership or Copartner.* Notwithstanding the foregoing: (A) a petition commencing a bankruptcy case may be filed by or against any general partner in a district where a petition under the Act by or against a general partner is pending; (B) a petition commencing a bankruptcy case may be filed by or against a partnership or by or against any other general partner or by or against any combination of the partnership and the general partners in a district where a petition under the Act by or against a general partner is pending.
>
> (4) *Affiliate*. Notwithstanding the foregoing, a petition commencing a bankruptcy case may be filed by or against and affiliate of the bankrupt in a district where a petition under the Act by or against the bankrupt is pending.

FED. R. BANKR. P. 116(a) (abrogated). The commentary to section 2a(1) provided: "Rule 116 dealing with venue primarily revises the statutory language for clarification. Rule 116(a)(2) eliminates the notion of residence or domicile as a useful basis to determine venue of a corporation or partnership."

[1899] The predecessor provision under the Bankruptcy Reform Act of 1978 was 28 U.S.C. § 1472. Section 1472 was repealed and replaced by section 1408 by the Bankruptcy Amendments and Federal Judgeship Act of 1984. Section 1472 was reenacted verbatim as section 1408.

[1900] 28 U.S.C. § 1408(1) (1994).

The affiliate rule provides that a case under title 11 may be commenced in the district court for the district where a case concerning such person's affiliate, general partner, or partnership is pending.[1901]

Debtors file for bankruptcy where they are located. Most cases involving consumer debtors or small businesses present no question about where to file. In some jurisdictions, however, near state borders, for example, some problems arise when debtors attempt to choose a more convenient courthouse or a more debtor-friendly forum. In general, however, venue issues do not arise in small cases.

In a global economy the determination of venue is not so obvious. For multi-state corporations, venue options can be broad and this is where the opportunity for abuse can begin. Section 1408(1) permits a corporation to file a bankruptcy petition in its state of incorporation, the location of its "principal place of business," or the location of its "principal assets."[1902] For the multi-state corporation, the ability to manipulate the state of incorporation, the location of the "principal place of business" or the "principal assets" provides a choice of a number of different jurisdictions. As more businesses incorporate in a state that is not the principal place of business, the magnitude of this opportunity, and its effect on the bankruptcy system, increases.

C. Affiliate Venue under the Bankruptcy Code

The affiliate rule contained in section 1408(2) raises a companion issue to the venue provisions in section 1408(1). The current affiliate rule permits a debtor's affiliate(s) to file a bankruptcy petition in the same venue as the debtor's case regardless of whether that court would be a proper venue for the affiliated entity.[1903] The affiliate rule thus provides a broader range of venue alternatives than those provided in section 1408(1). Under the current rule, a multiple entity corporate structure may file petitions for all of the related entities in the same forum as long as a case of one of the affiliated entities is already pending. By permitting a coordinated filing of multiple entities in one venue, the affiliate rule prevents the problem of multiple professionals and conflicting rulings if affiliated cases are filed in separate

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[1901] 28 U.S.C. § 1408(2) (1994).

[1902] 28 U.S.C. § 1408(1) (1994).

[1903] Section 1408(2) provides

> Except as provided in section 1410 of this title, a case under title 11 may be commenced in the district court for the district--
>
> (2) in which there is pending a case under title 11 concerning such person's affiliate, general partner, or partnership.

venues and, importantly, allows a reorganization of an entire business enterprise as may be necessary.

While the current affiliate rule saves valuable time and expense by permitting a single venue filing for multiple related entities, it has also been subject to criticism. Under the rule, a parent corporation can follow a subsidiary into a venue that would otherwise be unavailable to the parent under section 1408(1). A corporation may thus follow its corporate affiliate into bankruptcy in the same venue, even if it has no other ties to that forum. For example, a corporation with an affiliate in bankruptcy in court "A" can file for bankruptcy in court "A" even if it meets none of the other criteria for filing in that court. As a result, the affiliate rule multiplies the already diverse venue choices of large, multi-entity corporate families. Given the interests at stake in a large Chapter 11 case, the risk of a "sacrificial debtor" *(i.e.*, a subsidiary or affiliate who files for Chapter 11 relief solely for the purpose of gaining entree´ to a particular venue) is high.[1904]

Well-known examples of "affiliate venue" method of forum selection are Eastern Airlines and LTV Corporation. Eastern first filed a Chapter 11 petition for its frequent flier club, Ionosphere, Inc., in the Southern District of New York. At the time of Ionosphere, Inc.'s filing, there was no indication that Ionosphere was in need of bankruptcy protection or a financial restructuring.[1905] The parent corporation, Eastern Airlines, followed its affiliate into the New York bankruptcy court soon after. Similarly, LTV Corporation followed a small subsidiary, Chateaugay Corporation, into the bankruptcy court in the Southern District of New York. At the time of LTV's filing, there was no indication that Chateaugay Corporation was in need of bankruptcy protection. Nonetheless, its filing determined the geographic location of one of the country's largest bankruptcies.

While invocation of affiliate venue rules have not been a common practice and has been employed in a limited number of cases, these types of venue stratagems discredit the fairness of the entire bankruptcy process by placing too much discretion in the hands of the debtor. The delicate balance of power between debtors and creditors must be maintained by the Bankruptcy Code and related statutory provisions. Venue should not be an exception.

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[1904] Use of an affiliate for venue purposes has been referred to as the "venue hook." Lynn M. LoPucki & William C. Whitford, *Venue Choice and Forum Shopping in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 1991 WIS. L. REV. 11, 20-21. (hereinafter the *LoPucki & Whitford Study*).

[1905] *Id.*, at 21 ("The subsidiary, Ionosphere, had assets of less than two million dollars and was solvent at the time of filing. It ran hospitality clubs at airports served by Eastern. For a discussion of the venue choice in this case, see *Eastern's Bankruptcy Strategy: Go North*, MIAMI REVIEW, March 20, 1989, at 4 col. 1.").

## D. Strategic Use of Venue Choice

Does forum shopping occur frequently? In their landmark study of the bankruptcies of publicly traded companies in the 1980s, Professors Lynn LoPucki and William Whitford documented the companies' choices for filing locations.[1906] They concluded that venue could be explained *only* by forum shopping in about 16% of the cases, and another 63% of the cases showed some signs of forum shopping.[1907] In large cases, the widespread perception is that companies can—and frequently do—choose their fora based on a number of criteria other than those listed in the statute. When the researchers considered whether forum shopping was part of the filing decision, along with other listed factors, such as experience of the judge, another 63% of the cases were affected, for a total of 78 %—or about four out of five—of the venue choices of large businesses were influenced by forum shopping.[1908]

Reasons for forum shopping vary among debtors and their attorneys. Some debtors claim they choose a forum because of its well-developed case law or proximity to large, knowledgeable law firms. They argue that such advantages actually decrease the total cost of the bankruptcy. Respect for a local judiciary with demonstrated abilities to handle large cases may account for the disproportionate migration of large cases to one or two cities.

Other reasons for forum shopping are less benign. Commentators identify the desire among debtors' counsel to go to fora that permit high attorney's fees and do not pro-actively review fee applications.[1909] Higher administrative costs for professional fees are borne by unsecured creditors. High professional fees also discredit the reputation of the bankruptcy system. When the professionals are able to choose the fee-friendly forum, the reputation of the bankruptcy system suffers even further.

Gaining strategic advantage over other litigants, such as choosing a forum where a harmful ruling is not applicable, is another frequently cited reason to select one forum over another. Sometimes a venue is chosen for its inaccessibility for certain litigants, driving up the costs of their pursuit of their claims and making it

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[1906] *LoPucki & Whitford Study, supra* note 1904 at 26.

[1907] *Id*. at 26-27.

[1908] *Id.* at Appendix.

[1909] *Id.* at 45-46.

difficult for them to serve on committees.[1910] For example, when a debtor with thousands of small local unsecured creditors is able to file for bankruptcy at the other end of the country, it is impossible for these parties to represent their interests in the debtor's case. Such strategies can affect the outcome of cases.

Obtaining a debtor-friendly judge can also have an impact on the reorganization case. In a large Chapter 11 case, judges have a great deal of discretion in applying the Bankruptcy Code. For example, debtor in possession financing terms, lift stay motions, cash collateral and valuation disputes are examples of areas where the bankruptcy judge has broad discretion interpreting and applying the Bankruptcy Code.[1911] Debtors will naturally choose the bankruptcy forum that appears the most favorable. Sometimes that choice will benefit the majority of creditors and sometimes it will not. The Recommendation does not prevent a debtor from choosing a favorable forum, it only limits those choices to principle place of business and location of principle assets.

Choosing a distant forum also has the effect of reducing local press coverage of the debtor's case. Forum shopping, as stated earlier, is limited to large corporations and the bankruptcy filing is of great local interest where the debtor's headquarters and usually the greatest number of employees are located. Dampening local press interest in the case is a side-effect of filing for bankruptcy relief in a distant location and may be beneficial to the debtor in possession. Creditors may also benefit by less negative press coverage if the debtor's business is preserved as a result.

If creditors could easily transfer venue to a more convenient or more appropriate venue, the initial rules on venue would not be as important. Judges might be counted on to exercise sound judgment in seeing to it that a case ended up in the

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[1910] *See In re* Abacus Broad. Corp., 154 B.R. 682, 686 (Bankr. W.D. Tex. 1993) ("the court writes to underscore the danger of forum shopping (or, more insidiously, judge shopping) in the placement of venue in reorganization proceedings .... How much deference should be given to a forum selected primarily by the lawyers, for their own convenience or concern for remuneration? How much deference should be given to a debtor's concern that it get what it perceives to be a "debtor's judge?" Whenever a creditor raises the venue question, none at all. Forum shopping has never been favored by federal courts, and courts are quick to discern the evil in all its disguises .... In bankruptcy, too often the tactic is masked by pious pronouncements about the debtor's "right" to select the most advantageous of several possible forums, in order to advance the prospects for reorganization.")

[1911] Whether bankruptcy judges would be able to "compete" effectively for bankruptcy cases is one of the bases for a proposal to allow corporations to choose a bankruptcy venue well before financial distress occurs. Professors Rasmussen and Thomas conclude that permitting corporations to choose a bankruptcy venue ahead of any financial problems will, among other things, improve the application of the Bankruptcy Code by encouraging judges to rule in a way that promotes efficiency. *See* Robert K. Rasmussen & Randall S. Thomas, Improving Corporate Bankruptcy Law Through Venue Reform, 6, Unpublished Manuscript (1997).

appropriate forum. For a number of reasons, however, transfer is problematic. A bankruptcy case is not like ordinary, two-party litigation. Because a reorganization case is about the survival of a live (but struggling) business, the first day of the filing is critical.

The debtor nearly always makes the initial forum selection by choosing its filing location. For creditors to protest, often they need local counsel and they need to mount an expensive suit at the inception of the case.[1912] Because bankruptcy cases often have a number of issues decided in the first few days, judges often feel that by the end of a week, the case is already theirs, and they are understandably reluctant to transfer venue elsewhere.

In assessing the effectiveness of transfer motions, one cannot lose sight of the dynamic at work in a bankruptcy courtroom on the first day of a large Chapter 11 case. The courtroom is packed with the debtor's attorneys (both "foreign" counsel and local counsel, if necessary), as well as attorneys (and presumably local counsel) for all of the large creditors. Even before the judge makes the first ruling, the debtor and the creditors have incurred a great deal of expense in getting prepared and familiarizing their various professionals with the relevant facts.

Big bankruptcy cases often equate to big business for the local bankruptcy bar. The cost and time of educating all of the debtor's and the creditors' "local" professionals prior to and during the first few weeks of the case is often significant. Big bankruptcy cases further educate the local professionals and provide an opportunity to develop an expertise over the course of the case. Bankruptcy judges, who generally emerge from the local bar, are usually very cognizant of these factors and weigh them along with the other interests in deciding whether to transfer the case.

Some of the costs of forum shopping, when it exists, are obvious. Forum selection becomes a strategic tool, available for clever parties to manipulate outcomes to the disadvantage of smaller creditors who are cut out of the bankruptcy process. Because forum shopping is available in its extreme forms only for large companies, it also involves an element of discrimination against smaller businesses and consumers who have no such choices.

The real costs of forum shopping, if it is widespread, might be even greater. The damning charge that forum shopping is used to select fora that are fee-friendly, combined with the allegation that judges want to keep high visibility cases, raises a

[1912] Indeed, LoPucki and Whitford studied thirty-seven voluntary Chapter 11 cases which only two had transfer motions. Both motions were unsuccessful. *LoPucki & Whitford Study*, *supra* note 1904, at 24.

troubling specter of courts competing for big-case bankruptcy business.[1913] If they do compete, they would do so by making lawyer-friendly, debtor-friendly rulings. Of course, the application of these rulings is not limited to the mega-cases they attract; these rulings also affect every other business case before the courts. Given the complex appellate structure currently in existence and the extraordinary discretionary decision-making vested in the bankruptcy courts, the impact of forum shopping is compounded. Court competition for cases could distort analysis of legal problems and undermine the fairness—real or perceived—of the bankruptcy system.[1914]

This Recommendation is not directed at the bankruptcy courts in the Southern District of New York, those in Delaware, or in any other specific bankruptcy venue. Rather it is directed at ameliorating the problems that arise as a result of the broad venue choices available to corporate and partnership debtors. The National Bankruptcy Review Commission received numerous letters on the problem of the disenfranchisement of creditors due to forum shopping.[1915] One letter recounted how a Chicago retailer with extensive operations in Chicago could file for bankruptcy relief in Delaware or New York.[1916] As a result, it is uneconomical for a landlord who may have as much as $50,000-$60,000 at stake to litigate in the distant forum and enforce her statutory rights.[1917] The Recommendation does not eliminate the problem of creditor disenfranchisement, but rather attempts to limit a debtor's venue choices to places most relevant to the ongoing business: the principal place of business or location of the principal assets.

These Recommendations for change in forum selection criteria are not novel. In large part, they reflect the state of the law on forum selection for cases under the Bankruptcy Act between 1973 and the 1978 Reform Act.

*Competing Considerations.* Restricting forum choices may increase litigation over the appropriateness of forum choices. A debtor's desire to choose an

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[1913] *But see* Rasmussen & Thomas, *supra* note 1911 (arguing that competition among bankruptcy judges for cases will produce interpretations of the law that will lead to efficient uses of resources).

[1914] *See* GORDON BERMANT *ET AL.*, CHAPTER 11 VENUE CHOICE BY LARGE PUBLIC COMPANIES, REPORT TO THE COMMITTEE ON THE ADMINISTRATION OF THE BANKRUPTCY SYSTEM (1997).

[1915] *See* NBRC Database Reports on Venue.

[1916] Letter from Steven B. Towbin, D'Ancona & Pflaum to National Bankruptcy Review Commission, (Sept. 12, 1996).

[1917] *Id.*

advantageous forum, regardless of the venue rule, would not go away. While some debtors could be expected to comply with the more restricted provisions, undoubtedly there would be other debtors who would challenge the statute at the margins by selecting a friendly forum, prompting their creditors to challenge the forum choice.

"Principal place of business" is not an entirely rigid criterion. The main debates under this approach, however, would likely be over whether the "principal place of business" was at the location of corporate headquarters or the location of most of the assets. Some forum choices would still exist under the Recommendation. The difference between the Recommendation and the current system is that the Recommendation will focus a debtor's choice of venue on places that bear a tangible relationship to the ongoing business. Recognizing that no single venue will make all the interested parties happy all the time, the Recommendation would ensure that whatever venue was selected would bear a significant relationship to the operation of the business. Place of incorporation, alone, will no longer be a valid basis for venue of a bankruptcy case.

For some businesses, "principal place of business" would remain an elusive concept. As companies do more work by computer, the "virtual headquarters" may be located anywhere. Moreover, as more businesses consist of intangible assets, questions about where the assets are located or where the business transactions take place become ephemeral. The courts would be called on to develop new guidelines for new kinds of corporations.[1918]

It is important to note that not all commentators believe that forum shopping is an inappropriate practice. Professors LoPucki and Whitford documented the forum shopping practices of the publicly traded companies in the decisions about where to file for bankruptcy. They did not conclude, however, that such practices be curtailed.[1919] The reason they cited for maintaining the current system is that it permits examination of the more pernicious reasons behind forum shopping. What factors a debtor (or its professionals) considers in choosing a particular forum and whether those underlying reasons jeopardize the effectiveness of other bankruptcy policies. The current system also encourages competition among courts to develop methods to maximize a debtor's value. In addition, forum shopping permits a few

[1918] *See, e.g., In re* Bell Tower Assoc., 86 B.R. 795, 800 (Bankr. S.D.N.Y. 1988) (holding that principal place of business was where debtor made overall management decisions); *In re* Dock of the Bay, Inc., 24 B.R. 811 (Bankr. E.D.N.Y. 1982) (utilizing the "nerve center" test to determine where a multi-jurisdiction corporation has its principal place of business); *In re* Holiday Towers, 18 B.R. 183 (Bankr. S.D. Ohio 1982) (location of general executive offices dictated proper venue).

[1919] *LoPucki & Whitford Study, supra* note 1904, at 163.

courts to develop expertise in dealing with large bankruptcy cases. These may be positive, rather than negative implications of the current system.[1920]

A great deal of debate has been generated by the Commission's Recommendation to amend the venue provisions of section 1408. In response to the initial Commission Recommendation at the June 20-21, 1996 meeting, an extensive study was undertaken by the Delaware State Bar Association to support maintaining the existing venue choices under section 1408.[1921] The Commission was fortunate to have been provided with this exhaustive study and thorough discussion of the arguments against the Recommendation. The Delaware Venue Report raises a number of important arguments.

A. Substantive Reforms Cloaked by Procedural Reform

The Delaware Venue Report argues that the Commission is attempting to effect substantive reforms with its procedural Recommendation to eliminate place of incorporation as a valid venue option.[1922] Venue choice has been blamed for access to routine exclusivity extensions, favorable fee rulings, and disenfranchising small creditors.[1923] The Delaware Venue Report argues that these problems, "if they are in fact systemic problems, as opposed to isolated, albeit notorious instances" are substantive issues that cannot, and should not, be remedied through a procedural venue reform.[1924]

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[1920] *Id.* On the subject of amending the current venue provisions, LoPucki and Whitford conclude:

> Even though elimination of forum shopping is a practical alternative, we favor the approach of retaining the present system for selecting venue and addressing in other ways the deleterious consequences that flow from extensive venue choice and forum shopping. The primary benefit we anticipate from maintaining venue choice and forum shopping is continued competition among districts in improving their methods and techniques for maximizing the aggregate value of the enterprise undergoing reorganization. The development of such methods and techniques is in the interest of all parties.

*LoPucki & Whitford Study*, *supra* note 1904, at 163.

[1921] Report of the Delaware State Bar Association to the National Bankruptcy Review Commission in Support of Maintaining Existing Venue Choices, dated October 3, 1996 [hereinafter the *Delaware Venue Report*). The Delaware Venue Report is included in the Appendix.

[1922] *Id.* at 9-18.

[1923] *Id.*

[1924] *Id.* at 9-10.

There is no doubt that uniformity of legal interpretation and application are desirable. More importantly, a cornerstone of our judicial system is that the law be subject to a variety of interpretations at the trial level and made uniformly applicable by the courts of appeals and the Supreme Court. But when a few judges, by virtue of sitting in desirable venues, are the only judges to review certain issues, the system breaks down. There may be no need to make substantive law reform; there may be a need to prevent one or two judges from making national law. Deleting state of incorporation as a venue option increases the number of courts that can decide important issues, and the number of appellate courts that can eventually exercise review over those decisions. Ultimately, this approach is more likely to yield thoughtful decision making and policy applicable to big cases.

B. Validity of Venue Based on State of Incorporation

The Delaware Venue Report notes that despite the focus on disenfranchisement of smaller creditors in the current venue statute, "no one has seriously suggested premising venue on creditor location."[1925] Premising bankruptcy venue on creditor location would result in an unworkable rule that would be the source of a great deal of litigation.[1926] The Report argues that place of incorporation is a valid venue under numerous federal venue provisions, including the general federal venue statute;[1927] the patent venue statute;[1928] antitrust action venue provisions;[1929] venue for actions commenced under CERCLA;[1930] venue for actions

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[1925] *Id.* at 22 (emphasis added) (citing *LoPucki & Whitford Study*, *supra* note 1881, at 49, and Robert J. Rosenberg and Marla S. Becker, *The Perils of Forum Shopping and the Need for Statutory Reform of the Venue Selection Process*, printed in "The Biased Business of Venue Shopping" 75, 81 (ABI Northeast Bankruptcy Conference, July 21, 1995).

[1926] *Delaware Venue Report*, *supra* note 1921, at 22.

[1927] Section 1391(c) provides in pertinent part that "[f]or purposes of venue under this chapter, a defendant that is a corporation shall be deemed to reside in any judicial district in which it is subject to personal jurisdiction at the time the action is commenced." 28 U.S.C. § 1391(c) (1996).

[1928] Section 1400(b) provides in pertinent part that "[a]ny civil action for patent infringement may be brought in the judicial district where the defendant resides,...." 28 U.S.C. § 1400(b) (1996).

[1929] 15 U.S.C. § 22 provides that an antitrust action may be commenced in any judicial district where the defendant is an "inhabitant." "Under this provision, '[t]he word "inhabitant" is synonymous with "resident" and "a corporation is a resident of the state in which it is incorporated." *Delaware Venue Report*, *supra* note 1921, at 24 *citing* Aro Manuf. Co., Inc. v. Automobile Body Research Corp., 352 F.2d 400, 404 (1st Cir. 1965).

[1930] 42 U.S.C. § 9613(b) (1993).

commenced under the Securities Act of 1933;[1931] venue for actions commenced under the Securities and Exchange Act of 1934;[1932] and venue for actions commenced under the Investment Advisors Act.[1933] The Delaware Venue Report concludes that if the Commission's venue Recommendation were adopted, it would "eliminate state of incorporation as a venue predicate for corporate debtors, thereby singling out bankruptcy as the one significant federal statute where a company's state of incorporation will not support venue."[1934]

This argument fails to observe how a bankruptcy case is different from the two-party actions with which it is compared. Bankruptcy is essentially an *in rem* proceeding involving a multitude of parties involving creditors of all types: it is not the typical two-party civil litigation. A multitude of parties that are not necessarily adverse to each other are brought into the bankruptcy court by the debtor to determine the claims and interests in the property of the estate. Over the course of a case it is not unusual for different parties to have allied interests on some issues and adverse interests on others. The shifting sands in a bankruptcy case thus make it much different than straight two-party litigation where the parties interests are adverse throughout the case.

In addition, no plaintiff anywhere else in the system may commence a lawsuit based on its *own* state of incorporation. Plaintiffs are limited to fora based on where the defendants are subject to suit. An interpleader action is the closest civil action analogue to the bankruptcy case. It is commenced by the holder of a fund that is subject to competing claims, similar to a bankruptcy estate. Unlike bankruptcy, however, an interpleader action may only be filed "where one or more of the claimants reside."[1935] Thus, the creditors (or claimants) in an interpleader action dictate the venue of the action.

Retaining place of incorporation as a venue choice is contrary to the spirit of all the federal venue provisions. It lets the initiating party look at factors most convenient to itself and pick the jurisdiction it wants without regard to the other parties to the action. Principal place of business generally demonstrates a willingness

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[1931] 15 U.S.C. § 77v (1995).

[1932] 15 U.S.C. § 78aa (1995)

[1933] 15 U.S.C. § 80b-14 (1995).

[1934] *Delaware Venue Report, supra* note 1921, at 22.

[1935] An interpleader action that is commenced by the holder of a "fund" to which one or more claimants seek recovery must be commenced "in the judicial district where one or more of the claimants reside." 28 U.S.C. § 1397.

of both parties to do business in that location. Location of principal assets similarly bears more of a relationship to the ongoing operations of the debtor than the place of incorporation.

C. Increased Litigation

The Delaware Venue Report argues that adoption of the Commission's venue Recommendation will lead to increased litigation over where the debtor's principal assets or principal place of business is located.[1936] Place of incorporation is the only bright line venue rule that "is clear, easily ascertainable by everyone in advance, and not subject to litigation."[1937] Moreover, as technology progresses, it will become more difficult to fix a single place where the principal place of business is located or where the principal assets are located.[1938] In addition, technological advances will enable creditors to participate in bankruptcy court proceedings by telephonic and video-conferencing, as well as monitoring a case via electronic docket information, thus diminishing any risk of disenfranchisement by a debtor filing in a distant forum.[1939]

Interestingly, however, from 1973 to 1979, there did not appear to be great difficulty in deciding appropriate venue. The interpretive guidelines for principal place of business and principal assets are already the subject of judge-made law.[1940] The parties to a venue dispute as well as the judges presiding over those proceedings are in the best position to argue and formulate clear standards for what constitutes principal place of business and what constitutes location of principal assets.

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[1936] *Id.* at 27-30.

[1937] *Id.* at 27.

[1938] This issue was raised by Commissioner Alix during the plenary session of the Commission in San Diego, CA on October 19, 1996. *See* Transcript of National Bankruptcy Review Commision Meeting, San Diego, CA (Oct. 19, 1996). *See Delaware Venue Report, supra* note 1921, at 27.

[1939] *Delaware Venue Report, supra* note 1921, at 28.

[1940] *See, e.g., In re* Bell Tower Assoc., 86 B.R. 795, 800 (Bankr. S.D.N.Y. 1988) (site of overall management decisions was proper venue); *In re* Holiday Towers, 18 B.R. 183 (Bankr. S.D. Ohio 1982) (location of general executive offices determined proper venue); *In re* Dock of the Bay, Inc., 24 B.R. 811, 814-15 (Bankr. E.D.N.Y. 1982) (company's principal place of business not controlled by location of financing as well as president and sole shareholder); *In re* Lakeside Utils., 18 B.R. 115 (Bankr. D. Neb. 1982) (holding that the "nerve center" of the company was not the principal place of business).

The Delaware Venue Report asserts that "anyone who has ever been involved in a major Chapter 11 case knows that the 'principal place of business' and the 'place of principal assets,' even if readily ascertainable, bear little relationship to the 'location' of creditors."[1941] In support of this statement, the Report cites to a state by state analysis of creditor locations for a variety of debtors who filed for bankruptcy relief in Delaware.[1942] The Report concludes that virtually all of the debtors surveyed who filed for relief in Delaware did not have a significant percentage of their twenty largest creditors in the debtor's principal place of business.[1943]

The data on creditor location provided in the Delaware Venue Report tell a different story on *overall* creditor location. A comparison of the debtor's principal place of business with the bankruptcy venue chosen (all of the sample debtors filed in Delaware), revealed that more creditors were located in the state of the principal place of the debtor's business than in the State of Delaware, in all of the sample cases except one.[1944] In fact, out of the thirteen debtors studied, nine had more creditors in the state where their principal place of business was located than in any other state.[1945] In other words, if each of these debtors had filed for Chapter 11 relief in the district where their principal place of business was located, no other state-wide venue would have encompassed a greater number of creditors.[1946]

It is important to draw this distinction from the conclusions reached in the Delaware Venue Report, because in large Chapter 11 cases, the creditors holding the twenty largest claims have enough money at stake to defend their interests no matter what the choice of venue. The smaller creditors with the smaller claims are the ones

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[1941] *Delaware Venue Report, supra* note 1921, at 28-29.

[1942] *Id.* Exhibit C to the Delaware Venue Report is attached in the Appendix for ease of reference.

[1943] *Id.*

[1944] *See Delaware Venue Report, supra* note 1921, at Exh. C. The Venue Exhibit analyzes whether the principal place of business of the debtors listed in the Delaware Venue Report was more representative in terms of number of creditors from that state than from the bankruptcy venue state (all of the sample debtors filed for relief in Delaware). The Venue Exhibit concludes that nine out of thirteen debtors had more creditors located in the state of their principal place of business than in *any* other state. Moreover, only one debtor, Silo, Inc., had more creditors located in Delaware (the bankruptcy venue) than it did in the state where its principal place of business was located.

[1945] *See Delaware Venue Report, supra* note 1921, at Exh. C.

[1946] This conclusion was also reached in the *FJC Venue Report*, *supra*, note 1914, at 62. ("We concluded that the average creditor was usually inconvenienced by a Delaware filing in relation to a (hypothetical) filing at the principal place of business.").

who are more easily disenfranchised by the choice of a remote venue. Removing place of incorporation as a permissible venue will balance the reorganization process in favor of smaller creditors who cannot afford to participate in distant courts.[1947]

Critics of the Recommendation to amend affiliate venue argue that the system can sustain a few high profile abuses in order to prevent the multiple forum filing problems that may arise under the Recommendation. Under certain circumstances, the Recommendation will lead to a result opposite of its intention. An example is where a parent corporation's only asset is 100% of the stock of an operating subsidiary. Under the Recommendation, the operating subsidiary could file in the forum where the parent's bankruptcy case was pending despite the fact that the more appropriate venue would be where the operating subsidiary's principal place of business or principal assets were located; but the parent could not file where the subsidiary's case was pending. For the unusual case such as this, a motion to transfer venue of the parent's case under circumstances where the venue bears no relationship to the ongoing business of the debtor would be in order.

Other criticism of the Commission Recommendation includes the multiple fora filing risk of affiliated entities where no overlapping venue options exist and the parent does not file. Bankruptcy Rule 1014(b) addresses the multiple fora problem by enabling the court where the first petition was filed to determine (on motion) where the affiliated cases should be heard.[1948] The Recommendation is narrowly tailored to

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[1947] The Commission has a number of recommendations that help to tip the balance of equities more in favor of smaller creditors and other small parties in interest in bankruptcy cases. The proposal on National Admission, Recommendation 3.3.4 will reduce the costs associated with counsel appearing in a distant court. The proposals on preference amount and preference venue Recommendation 3.2.1-3.2.2 will help reduce noneconomical preference actions that cost more for the creditor to defend than to settle.

[1948] FED. R. BANKR. P. 1014(b) provides:

> (b) **Procedure When Petitions Involving the Same Debtor or Related Debtors are Filed in Different Courts.** If petitions commencing cases under the Code are filed in different districts by or against (1) the same debtor, or (2) a partnership and one or more of its general partners, or (3) two or more general partners, or (4) a debtor and an affiliate, on motion filed in the district in the petition filed first is pending and after hearing on notice to the petitioners, the United States trustee, and other entities as directed by the court, the court may determine, in the interest of justice or for the convenience of the parties, the district or districts in which the case or cases should proceed. Except as otherwise ordered by the court in the district in which the petition filed first is pending, the proceedings on the other petitions shall be stayed by the courts in which they have been filed until the determination is made.

FED. R. BANKR. P. 1014(b) (1994).

deter abuse of section 1408(2). Similarly, Rule 1014(b) provides a mechanism (in those admittedly rare instances) to prevent an uncoordinated multiple fora bankruptcy filing by related entities.

**Annex A**

**Legislative Response to Marathon:**
**Jurisdiction Provisions of the "Bankruptcy Amendments and Federal Judgeship Act of 1984" (as amended)**

| U.S. Code Section | Jurisdictional Effect |
|---|---|
| 28 U.S.C. § 1334(a) | Confers original and exclusive jurisdiction on the district courts of all cases under title 11. |
| 28 U.S.C. § 1334(b) | Confers original, but not exclusive, jurisdiction on the district courts over all civil proceedings arising under title 11, or arising in or related to cases under title 11. |
| 28 U.S.C. § 1334(c)(1) | Permits a district court to abstain from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11. |
| 28 U.S.C. § 1334(c)(2) | Upon timely motion of a party in a proceeding (a) based on state law; and (b) related to a case under title 11 (and one that could not have been brought in federal court absent this section), the district court must abstain from hearing such proceeding if the proceeding (x) is commenced; and (y) can be timely adjudicated in a state forum of appropriate jurisdiction. |
| 28 U.S.C. § 1334(d) | Provides that only a decision not to abstain is reviewable by the courts of appeal. |
| 28 U.S.C. § 1334(e) | Vests the district court in which a case under title 11 is commenced or pending with exclusive jurisdiction of property of the estate, wherever located. |
| 28 U.S.C. § 151 | Designates bankruptcy judges as units of the district court in the district where they preside. |
| 28 U.S.C. § 152(a)(1) | Authorizes the circuit courts of appeals to appoint bankruptcy judges for the judicial districts in its circuit. Grants bankruptcy judges 14 year terms and states that bankruptcy judges "shall serve as judicial officers of the United States district court established under Article III of the constitution." |
| 28 U.S.C. § 157(a) | Authorizes each district court to refer any or all title 11 cases and proceedings under, arising in, or related to a case under title 11 to the bankruptcy judges for the district. |
| 28 U.S.C. § 157(b)(1) | Authorizes bankruptcy judges to "hear and determine" all "core" proceedings and enter final orders. |
| 28 U.S.C. § 157(b)(2) | Core matters, include, but are not limited to, the following: |
| 28 U.S.C. § 157(b)(2)(A) | Matters concerning the administration of the estate; |
| 28 U.S.C. § 157(b)(2)(B) | Allowance or disallowance of claims against the estate; exemptions from property of the estate; estimation of claims or interest for confirmation purposes, but not the liquidation or estimation of contingent or unliquidated personal injury tort or wrongful death claims against the estate for purposes of distribution in a case under title 11; |
| 28 U.S.C. § 157(b)(2)(C) | Counterclaims by the estate against persons filing claims against the estate; |
| 28 U.S.C. § 157(b)(2)(E) | Orders to turn over property of the estate; |
| 28 U.S.C. § 157(b)(2)(F) | Proceedings to determine, avoid, or recover preferences; |

**Legislative Response to Marathon:**
**Jurisdiction Provisions of the "Bankruptcy Amendments and Federal Judgeship Act of 1984" (as amended)**

| U.S. Code Section | Jurisdictional Effect |
|---|---|
| 28 U.S.C. § 157(b)(2)(D) | Orders in respect to obtaining credit; |
| 28 U.S.C. § 157(b)(2)(G) | Motions to terminate, annul or modify the automatic stay; |
| 28 U.S.C. § 157(b)(2)(H) | Proceedings to determine, avoid, or recover fraudulent conveyances; |
| 28 U.S.C. § 157(b)(2)(I) | Determinations as to the dischargeability of particular debts; |
| 28 U.S.C. § 157(b)(2)(J) | Objections to discharges; |
| 28 U.S.C. § 157(b)(2)(K) | Determinations of the validity, extent or priority of liens; |
| 28 U.S.C. § 157(b)(2)(L) | Confirmation of plans; |
| 28 U.S.C. § 157(b)(2)(M) | Orders approving the use or lease of property, including the use of cash collateral; |
| 28 U.S.C. § 157(b)(2)(N) | Orders approving the sale of property other than property resulting from claims brought by the estate against persons who have not filed claims against the estate; |
| 28 U.S.C. § 157(b)(2)(O) | Other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship, except personal injury tort or wrongful death claims. |
| 28 U.S.C. § 157(b)(3) | Authorizing a bankruptcy judge to determine, on motion or sua sponte, whether a proceeding is core or noncore. A determination that a proceeding is noncore shall not be made solely on the basis that its resolution may be affected by state law. |
| 28 U.S.C. § 157(b)(4) | Provides that noncore proceedings under section 157(b)(2)(B) shall not be subject to the mandatory abstention provisions of section 1334(c)(2); |
| 28 U.S.C. § 157(b)(5) | Requiring the district court to try all personal injury and wrongful death actions either in the district court where the bankruptcy case is pending or in the district court where the claim arose, as determined by the district court in which the bankruptcy case is pending. |
| 28 U.S.C. § 157(c)(1) | Authorizing bankruptcy judges to hear noncore proceedings and submit proposed findings of fact and conclusions of law to the district court. The district court can "consider" the bankruptcy judge's findings and enter the appropriate order. The district court may review de novo only those specific portions to which any party has timely and specifically objected. |
| 28 U.S.C. § 157(c)(2) | With the consent of the parties, the district court can refer a proceeding to a bankruptcy judge to hear and determine and enter a final order. |
| 28 U.S.C. § 157(d) | Permits a district court to withdraw a proceeding, in whole or in part, from the bankruptcy judge for cause shown. The district court must withdraw a proceeding if resolution of the proceeding requires consideration of both title 11 and another law of the United States affecting interstate commerce. |

**Legislative Response to Marathon:**
**Jurisdiction Provisions of the "Bankruptcy Amendments and Federal Judgeship Act of 1984" (as amended)**

| U.S. Code Section | Jurisdictional Effect |
|---|---|
| 28 U.S.C. § 157(e) | Authorizing a bankruptcy judge to conduct a jury trial if the parties consent and the district court specially designates the exercise of such jurisdiction. |
| 28 U.S.C. § 158(a) | Authorizes district courts to hear appeals from (x) final orders of bankruptcy judges; (y) interlocutory orders and decrees increasing or reducing the time periods in 11 U.S.C. § 1121; and (z) with leave of the court from other interlocutory orders and decrees. |
| 28 U.S.C. § 158(b)(1)-(b)(6) | Authorizes the judicial council in each district to establish a bankruptcy appellate panel comprised of bankruptcy judges in that circuit to hear bankruptcy appeals (only in the absence of objection by the parties) instead of the district court. |
| 28 U.S.C. § 158(c) | Establishes that all appeals shall go to the BAP in the circuit unless an interested party opts out at the time of the filing of the appeal or within 30 days after service of the notice of appeal. |
| 28 U.S.C. § 158(d) | Provides that the courts of appeals shall have jurisdiction of all appeals of final decisions, judgments, orders and decrees entered under subsections (a) and (b) of section 158. |

## Annex B

| | Principal Place of Business Listed on Debtor's Petition | Number of Creditors Located in State of Principal Place of Business | Rank of Principal Business State for Creditor Location | Venue of Bankruptcy Case | Number of Creditors Located in State of Bankruptcy Venue | Rank of Bankruptcy Venue State for Creditor Location |
|---|---|---|---|---|---|---|
| **Morrison Knudsen Corp.** | Idaho | 4,111 | 1st out of 50 | Delaware | 112 | 45th out of 50 |
| **Rickel Home Centers** | New Jersey | 19,653 | 1st out of 50 | Delaware | 618 | 5th out of 50 |
| **Silo, Inc.** | Michigan | 130 | 18th out of 47 | Delaware | 265 | 14th out of 47 |
| **SLM Int'l** | New York | 492 | 4th out of 51* | Delaware | 12 | 37th out of 51* |
| **Smith Corona Corp.** | Connecticut | 484 | 3rd out of 51* | Delaware | 8 | 45th out of 51* |
| **Anacomp, Inc.** | Indiana | 2,158 | 1st out of 51* | Delaware | 49 | 33rd out of 51* |
| **Bill's Dollar Stores** | Mississippi | 3,122 | 1st out of 39 | Delaware | 7 | 28th out of 39 |
| **Spectra-vision, Inc.** | Texas | 1,634 | 1st out of 51* | Delaware | 65 | 28th out of 51* |
| **Burlington Motor Carriers, Inc.** | Indiana | 999 | 4th out of 49 | Delaware | 64 | 34th out of 49 |
| **DEP Corp.** | California | 722 | 1st out of 44 | Delaware | 4 | 32nd out of 44 |
| **Homeland Stores, Inc.** | Oklahoma | 10,106 | 1st out of 49 | Delaware | 19 | 23rd out of 49 |
| **Industrial General Corp.** | Ohio | 2,352 | 1st out of 45 | Delaware | 23 | 15th out of 45 |
| **Lomas Financial Corp.** | Texas | 12,755 | 1st out of 50 | Delaware | 85 | 44th out of 50 |

* Includes all foreign creditors as one creditor location.