Case No. 11-35162

IN THE UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

IN RE: BELLINGHAM INSURANCE AGENCY, INC., Debtor

EXECUTIVE BENEFITS INSURANCE AGENCY,

Appellant,

v.

PETER H. ARKINSON, TRUSTEE, solely in his capacity as Chapter 7 Trustee of the estate of Bellingham Insurance Agency, Inc.,

Appellee.

On Appeal from the United States District Court
for the Western District of Washington
Case No. 2:10-cv-00929, Adversary Proceeding No. 08-1132

BRIEF OF *AMICUS CURIAE* MARCIA M. TINGLEY IN SUPPORT OF APPELLANT

ROPES & GRAY LLP
D. Ross Martin
Prudential Tower
800 Boylston Street
Boston, MA 02199-3600
Phone: (617) 951-7000
Facsimile: (617) 951-7050

ROPES & GRAY LLP
Douglas H. Hallward-Driemeier
One Metro Center
700 12th Street, NW, Suite 900
Washington, DC 20005-3948
Phone: (202) 508-4600
Facsimile: (202) 508-4650

Attorneys for Marcia M. Tingley

TABLE OF CONTENTS

Page

TABLE OF AUTHORITIES

Page(s)

CASES

STATUTES

OTHER AUTHORITIES

INTEREST OF AMICUS[1]

Amicus curiae Marcia Tingley is one of thousands of named defendants in a set of fraudulent conveyance actions arising out of the *Tribune Newspapers* bankruptcies. In one those actions, a bankruptcy creditors committee has sued almost all public shareholders of the Tribune Companies, many of whom did no more than receive cash-out consideration when the Tribune was taken over in a leveraged buyout. That suit is pending in bankruptcy court. Ms. Tingley is individually named as a defendant in that action, although she was never a creditor of the Tribune Companies. She inherited Tribune Company stock from her father, a long-time *Tribune Newspapers* employee.

Additionally, the bankruptcy court has permitted bond trustees who are creditors of the Tribune Companies to bring fraudulent conveyance actions in over thirty states, all of which are now pending in federal district courts. Ms. Tingley has been named in one of those lawsuits (in the District of Massachusetts), where the plaintiff bond trustees have purported to make Ms. Tingley an involuntary defendant class representative.

Accordingly, Ms. Tingley has an interest in seeing that the law regarding whether, and to what extent, fraudulent conveyance actions can be heard by

[1] No counsel for any party authored this brief in whole or in part, and no person or entity other than amicus curiae and her counsel made a monetary contribution intended to fund the preparation or submission of this brief.

bankruptcy courts is developed properly. She submits this brief in response to this Court's Order inviting the views of amicus curiae.

SUMMARY OF ARGUMENT

In *Stern v. Marshall*, the Supreme Court made clear that a bankruptcy court's exercise of authority must comport with both statutory and constitutional grants of authority. In particular, the Court held that entry of final judgment on a cause of action designated as "core" by the Judicial Code may nevertheless violate Article III. Rather than relying on a proceeding's statutory label as "core" or "non-core," a court must independently analyze the requirements of Article III in every case to ensure that, in addition to statutory authority, bankruptcy courts have constitutional authority to act.

This Court's request for further briefing identifies two of the most significant questions that have arisen in *Stern*'s wake: Whether an action to avoid a fraudulent conveyance is one that a bankruptcy court can finally determine? And what authority do bankruptcy courts retain in "core" proceedings in which they may no longer enter final judgments? Amicus submits that, under the logic of *Stern*, bankruptcy courts lack constitutional authority to enter final judgment on a cause of action for fraudulent conveyance, at least where affirmative recovery is demanded from a non-creditor. Moreover, because the authority to issue proposed findings of fact and conclusions of law is confined by statute to non-core

proceedings, and fraudulent conveyance actions are clearly designated as "core" proceedings, the bankruptcy courts lack statutory authority to submit a report and recommendation to the district court in lieu of entering a final judgment.

Stern holds that bankruptcy courts may not enter final judgment on matters of private right. The Supreme Court has twice recognized that a fraudulent conveyance action, like the state law counterclaim at issue in *Stern*, is a matter of private right. The entry of final judgment on a fraudulent conveyance action against a non-creditor is therefore an exercise of judicial power subject to Article III and cannot be performed by bankruptcy judges.

Even where a fraudulent conveyance action is brought in response to a creditor's proof of claim, the bankruptcy courts' authority to award affirmative relief against the creditor is limited. Because the bankruptcy court below entered final judgment on a fraudulent conveyance action against a non-creditor, the judgment below must be vacated and this Court need not consider when, if ever, the bankruptcy courts may in effect rule on a fraudulent conveyance action via a ruling in a claim allowance process.

Where a bankruptcy court lacks constitutional authority to enter final judgment on a so-called "core" proceeding, it also lacks statutory authority to submit a report and recommendation. The bankruptcy courts' statutory authority to submit a report and recommendation is expressly limited to non-core

proceedings. Contrary to the suggestion of some amici, the principle of "severability" does not permit the Court to redesignate a fraudulent conveyance action as a non-core proceeding. A bankruptcy court's inability to enter final judgment in a core proceeding does not render the proceeding non-core. That result could be obtained only through rewriting the statute. Nor does the authority to "hear" a core proceeding include the authority to issue a statutory report and recommendation. Because fraudulent conveyance actions are plainly designated as "core" by statute, bankruptcy courts lack statutory authority to submit a report and recommendation with respect to such actions in lieu of entering a final judgment.

Finally, permitting bankruptcy judges to conduct, and submit a report and recommendation on, the final hearing on the merits would raise additional constitutional concerns. Because the question can be resolved on narrow statutory grounds, however, this Court need not address the constitutionality of the report-and-recommendation scheme with respect to final evidentiary merits hearings.

ARGUMENT

I. Article III Precludes Bankruptcy Courts From Entering Final Judgment On Causes Of Action For Fraudulent Conveyance At Least Against Non-Creditors

A cause of action by one private individual against another, historically resolved by judicial officers, is a matter of private right. Entering final judgment on a private right is an exercise of "judicial power" reserved for Article III courts.

The Supreme Court has identified fraudulent conveyance actions as private rights. Where, as here, such an action is asserted against a non-creditor, the entry of final judgment by a bankruptcy court violates Article III.

A. Article III Protection Attaches to Private Rights of Action Resembling Those Traditionally Heard by Judicial Officers

1. *Stern v. Marshall* holds that entering final judgment on causes of action historically existing independent of legislative grace or any agency regulatory regime is an exercise of "judicial power" committed to Article III courts

In *Stern v. Marshall*, 131 S. Ct. 2594 (2011), the Supreme Court drew a clear distinction between matters of "public right" subject to determination by non-Article III courts, and matters of "private right" that must be decided by Article III judges. Public rights originally included only certain cases "arising 'between the Government and persons subject to its authority.'" *Id.* at 2612 (quoting *Crowell v. Benson*, 285 U.S. 22, 50 (1932)). Where the federal government waives its right to sovereign immunity, or similarly delegates to a non-Article III court "'matters that historically could have been determined exclusively by'" the Legislative or Executive Branches, it creates rights of action "that can be pursued only by grace of" those branches. *Id.* at 2612, 2614 (quoting *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 68 (1982) (plurality opinion)). Congress may, therefore, assign the adjudication of such matters to non-Article III courts. *Id.* at 2612.

Although several cases extended the public rights doctrine beyond suits to which the government is a party, *Stern* confirmed that the exception remains narrow. Where the government is not a party, *Stern* explained, the Supreme Court has "limit[ed] the exception to cases in which the claim at issue derives from a federal regulatory scheme, or in which resolution of the claim by an expert government agency is deemed essential to a limited regulatory objective within the agency's authority." *Id.* at 2613. Certain matters adjudicated by administrative agencies have thus been treated as public rights. *Id.* at 2613-14 (discussing *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833 (1986)). But "it is still the case," *Stern* declared, "that what makes a right 'public' rather than private is that the right is integrally related to a particular federal government action." *Id.* at 2613.

Matters of private right, by contrast, involve "'the liability of one individual to another under the law as defined,'" *id.* at 2612 (quoting *Crowell*, 285 U.S. at 51), and include suits "made of the stuff of the traditional actions at common law tried by the courts at Westminster in 1789," *id.* at 2609 (internal quotation marks omitted). In *Stern*, the Court held that a common law counterclaim was a private right. *See id.* at 2614-15.

Full Article III protection attaches to private rights, as their resolution requires the exercise of "judicial power" reserved to judges who enjoy tenure

during good behavior and salary protection. Unlike public rights, "Congress cannot withdraw from judicial cognizance any matter which, from its nature, is the subject of a suit at the common law, or in equity, or admiralty." *Id.* at 2612 (internal quotation marks omitted). In *Stern*, the Court declared that "entry of a final, binding judgment *by a court* with broad substantive jurisdiction, on a common law cause of action, when the action neither derives from nor depends upon any agency regulatory regime" – *i.e.*, entry of judgment on a private right – is "the most prototypical exercise of judicial power." *Id.* at 2615. The Court thus held that, by entering final judgment on a common law counterclaim, the bankruptcy court exercised the judicial power of the United States in violation of Article III. *Id.* at 2620.

2. Article III applies even if a cause of action is properly characterized as a "core" bankruptcy proceeding by statute

The Judicial Code vests the bankruptcy courts with authority to "hear and determine" certain proceedings designated as "core proceedings arising under title 11, or arising in a case under title 11." 28 U.S.C. § 157(b)(1)-(2). In non-core proceedings, the bankruptcy court's authority is limited to submitting proposed findings of fact and conclusions of law to the district court, which retains ultimate authority to decided the matter. *Id.* § 157(c).

The statute's division of authority between the bankruptcy courts and the district courts is a direct consequence of the Supreme Court's decision in *Northern*

Pipeline, which held unconstitutional the Bankruptcy Act of 1978. 458 U.S. at 87 (plurality opinion); *id.* at 92 (Rehnquist, J., concurring in judgment). The *Northern Pipeline* plurality distinguished between the "restructuring of the debtor-creditor relations, which is *at the core* of the federal bankruptcy power," and adjudicating private right actions that merely seek to augment the bankruptcy estate. *Id.* at 71 (plurality opinion) (emphasis added). Congress responded by revising the Judicial Code to permit bankruptcy courts to enter final judgments only in "core" proceedings as defined by the statute. *See* 28 U.S.C. § 157(b); *Stern*, 131 S. Ct. at 2610.

In *Stern*, the Court for the first time held that entry of a final judgment in a "core" proceeding nevertheless violated Article III. 131 S. Ct. at 2608. The Court held that the common law counterclaim at issue was "core" under 28 U.S.C. § 157(b)(2)(C), and that the bankruptcy court had statutory authority to enter final judgment on that counterclaim. *Id.* By exercising that statutory authority, however, the bankruptcy court violated Article III of the Constitution. *Id.* *Stern* thus demonstrates that, in revising bankruptcy courts' authority, Congress failed to cure all of the constitutional deficiencies identified in *Northern Pipeline*.

B. A Cause of Action for Fraudulent Conveyance Is a "Private Right" Entitled to the Full Protections of Article III

The Supreme Court has recognized that a cause of action for fraudulent conveyance is a matter of private right. After *Stern*, it is clear that entering final

judgment on such an action – at least where it is not resolved in ruling on a creditor's proof of claim – is an exercise of judicial power committed to Article III courts. Because the bankruptcy court, and not an Article III court, entered judgment on the trustee's fraudulent conveyance action, the judgment below must be vacated.[2]

This Court's decision in *In re Mankin*, 823 F.2d 1296 (9th Cir. 1987), which held that the bankruptcy courts have authority to decide fraudulent conveyance actions, has been overruled by the Supreme Court's intervening decisions in *Stern* and *Granfinanciera v. Nordberg*, 492 U.S. 33 (1989). In *Mankin*, this Court concluded that Article III was satisfied because "the rationale underlying the public rights doctrine has at least some applicability" to fraudulent conveyance proceedings, *id.* at 1307-08, and, "to the extent that the right at issue here might not be considered a congressionally created public right," the appointment of

[2] The trustee brought claims for fraudulent conveyance under 11 U.S.C. §§ 548(a) and 544. Although the trustee also asserted fraudulent preference claims under 11 U.S.C. § 547, he did not seek, and the bankruptcy court did not grant, summary judgment on those claims. *See* Pl.'s Mem. in Supp. of Mot. for Summ. J. at 13, Adversary No. 08-1132 (Bankr. W.D. Wash. Mar. 17, 2010); Appellant's Excerpts of Record 28-29.

The trustee's state law claim for successor liability cannot provide an independent basis for upholding the bankruptcy court's entry of final judgment. Even before *Stern*, courts routinely held that such claims are not "core." *See, e.g.*, *In re Freeway Foods of Greensboro, Inc.*, 449 B.R. 860, 876 (Bankr. M.D.N.C. 2011); *In re H. King & Assocs.*, 295 B.R. 246, 259 (Bankr. N.D. Ill. 2003).

bankruptcy judges by Article III judges was sufficient to "ensure[] compliance with Article III." *Id.* at 1309-10.

The Supreme Court has since rejected each prong of *Mankin*'s reasoning. The Supreme Court has held that bankruptcy courts may enter final judgment only on matters of public right, *see* Section I.A.1, *supra*, and further concluded that fraudulent conveyance actions are matters of private right. Finally, the Court has made clear that the appointment and supervision of bankruptcy judges by Article III courts does not satisfy the demands of Article III. Because *Mankin* cannot be reconciled with the Supreme Court's intervening decisions in *Stern* and *Granfinanciera*, this Court should reject *Mankin* as having been effectively overruled. *See Miller v. Gammie*, 335 F.3d 889, 893 (9th Cir. 2003) (en banc).

1. The Supreme Court's decisions in *Stern* and *Granfinanciera* establish that fraudulent conveyance actions are matters of "private right"

The Supreme Court has already concluded, in both *Stern* and *Granfinanciera*, that a fraudulent conveyance action is a private right. Moreover, both decisions recognized that, as a private right, such an action can be determined only by Article III courts.

Although the question in *Granfinanciera* was whether a Seventh Amendment right to a jury trial attaches to fraudulent conveyance actions, the Court relied on the same distinction between public and private rights that it

applies in its Article III jurisprudence. *See* 492 U.S. at 53. The Court observed that "[t]here can be little doubt that fraudulent conveyance actions by bankruptcy trustees … are quintessentially suits at common law that more nearly resemble state-law contract claims brought by a bankrupt corporation to augment the bankruptcy estate than they do creditors' hierarchically ordered claims to a pro rata share of the bankruptcy res." *Id.* at 56. The Court thus concluded that "a bankruptcy trustee's right to recover a fraudulent conveyance under 11 U.S.C. § 548(a)(2) seems to us more accurately characterized as a private right rather than a public right as we have used those terms in our Article III decisions." *Id.* at 55.

In *Stern*, the Court relied on *Granfinanciera*'s analysis to conclude that a state law counterclaim was a matter of private right. In doing so, the Court likened the counterclaim to the fraudulent conveyance claim at issue in *Granfinanciera*, observing that neither fell "within any of the varied formulations of the public rights exception in this Court's cases." *Stern*, 131 S. Ct. at 2614. In fact, *Stern* construed *Granfinanciera* as having already decided that full Article III protection attaches to fraudulent conveyance actions: "Our conclusion [in *Granfinanciera*] was that … Congress could not constitutionally assign resolution of the fraudulent conveyance action to a non-Article III court." *Id.* at 2614 n.7.

2. The relationship between bankruptcy judges and Article III courts does not permit bankruptcy judges to enter final judgment on all fraudulent conveyance actions

Stern squarely rejected the argument that bankruptcy judges act as mere adjuncts of Article III courts when entering final judgments on matters of private right. Rather, by entering such final judgments, a bankruptcy court "exercises the essential attributes of judicial power." *Stern*, 131 S. Ct. at 2618. As a result, "a bankruptcy court can no more be deemed a mere 'adjunct' of the district court than a district court can be deemed such an 'adjunct' of the court of appeals." *Id.* at 2619.[3]

Stern similarly rejected the argument, endorsed by this Court in *Mankin*, that the appointment of bankruptcy judges by Article III judges is somehow sufficient to satisfy the requirements of Article III. *See Mankin*, 823 F.2d at 1309 (finding "significant" that Congress placed "control over the employment of bankruptcy judges exclusively in the hands of Article III judges"). Instead, *Stern* unequivocally declared that "[i]t does not affect our analysis that … bankruptcy judges under the current Act are appointed by the Article III courts, rather than the President." 131 S. Ct. at 2619. When bankruptcy judges exercise the judicial

[3] It makes no difference that the bankruptcy court's order granting summary judgment was reviewed *de novo* rather than under a more deferential standard applicable to factual findings. By entering a final, binding judgment, "subject to review only if a party chooses to appeal," the bankruptcy court exercised "the essential attributes of judicial power that are reserved to Article III courts." *Stern*, 131 S. Ct. at 2619 (brackets omitted).

power reserved to Article III courts, "it does not matter who appointed the bankruptcy judge or authorized the judge to render final judgments in such proceedings. The constitutional bar remains." *Id.*

C. Even Where a Defendant Has Filed a Creditor's Proof of Claim, Bankruptcy Courts May Lack Authority to Award Affirmative Relief

The defendant in this case is a non-creditor that did not file a proof of claim against the bankruptcy estate. Accordingly, this Court need not decide potentially difficult questions concerning the bankruptcy courts' authority in fraudulent conveyance actions against a creditor who has asserted a proof of claim, or the effect of *Stern* and *Granfinanciera* on § 502(d) of the Bankruptcy Code.[4] It remains uncertain the extent to which a bankruptcy court may, under the guise of merely disallowing a proof of claim, effectively award affirmative relief against a creditor in a fraudulent conveyance action because of the preclusive effect of the claim allowance ruling.

The Supreme Court has provided little guidance on this question. In *Stern*, the Court observed that, despite some overlap between the creditor's counterclaim and the debtor's proof of claim, "there was never any reason to believe that the process of adjudicating [the] proof of claim would *necessarily resolve* [the]

[4] Section 502(d) requires bankruptcy courts to disallow *any* proof of claim by a creditor that received a fraudulent transfer until the amount of the fraudulent transfer is repaid. *See* 11 U.S.C. § 502(d).

counterclaim." *Id.* at 2617 (emphasis added). The Court thus held that the bankruptcy court's authority to decide the proof of claim did not include authority to resolve the counterclaim. *Id.* at 2620. Although the Supreme Court's preference decisions have approved of awards of affirmative relief against a creditor in some circumstances, those decisions, as the Court emphasized in *Stern*, "'intimated no opinion concerning whether'" the bankruptcy referee could decide "'a demand by the bankruptcy trustee for affirmative relief, all of the substantial factual and legal bases for which had not been disposed of in passing on objections to the creditor's proof of claim.'" *Id.* 2616-17 (brackets omitted) (quoting *Katchen v. Landy*, 382 U.S. 323, 333 n.9 (1966)).

In sum, even where a defendant files a proof of claim, the bankruptcy court's authority to consider a fraudulent conveyance claim may be limited. Congress certainly could not, for example, enact a statute that eviscerates *Stern* by incorporating adjudication of the bankruptcy estate's affirmative causes of action into the process of allowing or disallowing creditors' claims. In all events, because the defendant here was a non-creditor, the bankruptcy court plainly lacked authority to enter judgment on the trustee's fraudulent conveyance claim. This Court can (and should) specifically reserve resolution of more difficult questions.

II. Bankruptcy Courts Lack Statutory Authority To Propose Findings Of Fact And Conclusions Of Law In Lieu Of Entering Final Judgment In "Core" Proceedings

Because fraudulent conveyance actions are designated as "core" proceedings, bankruptcy courts have statutory authority to enter final judgments in such proceedings, but, for the reasons just explained, Article III prohibits bankruptcy courts from exercising that statutory authority in most cases. That constitutional limitation does not, however, eliminate Congress's designation of fraudulent conveyance actions as "core" proceedings. Because bankruptcy courts lack *statutory authority* to propose findings of fact and conclusions of law in actions denominated as "core" by statute, a bankruptcy court may not issue a report and recommendation in lieu of entering final judgment in a fraudulent conveyance action.

A. The Judicial Code Is Unambiguous and Does Not Permit the Use of Report and Recommendation in Proceedings that Are Denominated as "Core"

The bankruptcy courts' authority to propose findings of fact and conclusions of law – that is, to issue a report and recommendation to the district court – is confined by statute to actions that are "not a core proceeding." 28 U.S.C. § 157(c)(1). Notwithstanding that, after *Stern*, bankruptcy courts will often lack constitutional authority to enter final judgments on fraudulent conveyance actions, Congress has clearly denominated such actions as "core" proceedings. *Id.*

§ 157(b)(2)(H). Accordingly, as the Seventh Circuit – the only court of appeals to address the question – recently concluded, where a bankruptcy court can no longer decide a "core" proceeding after *Stern*, the statute does not permit the bankruptcy judge to issue a report and recommendation in lieu of entering final judgment. *See In re Ortiz*, Nos. 10-3465, 10-3466, 2011 WL 6880651, at *7 (7th Cir. Dec. 30, 2011) (refusing to construe final judgments as proposed findings of fact and conclusions of law because "the debtors' claims qualify as core proceedings and therefore do not fit under § 157(c)(1)").

The bankruptcy courts' statutory authority is governed by 28 U.S.C. § 157, which provides:

> (b)(1) Bankruptcy judges may hear and determine all cases under title 11 and all core proceedings arising under title 11, or arising in a case under title 11 … and may enter appropriate orders and judgments, subject to review under section 158 of this title.
>
> (2) Core proceedings include, but are not limited to –
>
> ….
>
> (H) proceedings to determine, avoid, or recover fraudulent conveyances;
>
> ….
>
> (c)(1) 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.

28 U.S.C. § 157. The statute clearly distinguishes between core and non-core proceedings, and a particular cause of action must fall within one category or the other. No claim may be in both categories. *See Stern*, 131 S. Ct. at 2605 (holding that "core" proceedings cannot also be "related to" proceedings).

The bankruptcy courts' authority to act in each category of proceeding is clearly delineated by statute. Bankruptcy courts may "hear and determine" and enter "appropriate orders and judgments" in core proceedings. 28 U.S.C. § 157(b)(1). In "a proceeding that is not a core proceeding," by contrast, bankruptcy courts are authorized to issue a report and recommendation, acting much like magistrate judges. *Id.* § 157(c). District courts are required to consider any such report and recommendation and review *de novo* matters to which a party objects. *Id.*

In *Stern*, the Supreme Court held that that 28 U.S.C. § 157(b) is unconstitutional as applied in certain circumstances to causes of action designated as "core" by statute. Bankruptcy courts may thus no longer "determine" (enter final judgment on) such actions without the parties' consent. *Stern* did not address, however, what authority bankruptcy courts retain over those "core" proceedings that they can no longer "determine."

Certain amici urge that the Supreme Court, in dicta, implicitly endorsed the view that bankruptcy courts may issue reports and recommendations in "core" proceedings that the courts lack constitutional authority to determine. *See* Br. of Professor S. Todd Brown et al. as *Amici Curiae* at 24 (Jan. 13, 2012); Br. of G. Eric Brunstad, Jr. as *Amicus Curiae* at 27 (Jan. 3, 2012). But these amici read too much into the Court's mere acknowledgement that the respondent had "not argued that the bankruptcy courts are barred from 'hearing' all counterclaims or proposing findings of fact and conclusions of law on those matters." *Stern*, 131 S. Ct. at 2620 (some internal quotation marks omitted). In fact, the question was not even relevant in *Stern* because of the case's peculiar procedural posture. Once it was determined that the bankruptcy court lacked authority to enter final judgment, a separate final judgment of a Texas state court acquired preclusive effect in any further bankruptcy proceedings, thus rendering moot the question whether the bankruptcy court might have exercised authority short of determining the case. *See id.* at 2602.

While *Stern* does not answer the question, the Supreme Court has, in other cases, provided substantial guidance that makes clear this Court may not rewrite the statute to designate fraudulent conveyance actions as non-core. "[W]hen confronting a constitutional flaw in a statute" courts should "limit the solution to the problem." *Ayotte v. Planned Parenthood of N. New England*, 546 U.S. 320,

328 (2006). Courts should not "nullify more of a legislature's work than is necessary." *Id.* at 329. Furthermore, although legislative intent should guide the inquiry, courts are not "free to rewrite the statutory scheme in order to approximate what [they] think Congress might have wanted had it known that [a particular provision] was beyond its authority." *Seminole Tribe of Fla. v. Florida*, 517 U.S. 44, 76 (1996); *see Ayotte*, 546 U.S. at 329 ("[M]indful that our constitutional mandate and institutional competence are limited, we restrain ourselves from rewriting state law to conform it to constitutional requirements, even as we strive to salvage it." (brackets and internal quotation marks omitted)). To the extent a provision is unaffected by the constitutional infirmity, it must be sustained unless it is evident that Congress would have preferred that the entire law be stricken. *See Ayotte*, 546 U.S. at 330 ("After finding an application or portion of a statute unconstitutional, we must next ask: Would the legislature have preferred what is left of its statute to no statute at all?").

Applied to the Judicial Code's bankruptcy provisions, the foregoing principles require holding only that bankruptcy courts may no longer "determine" and enter final judgments in certain "core" proceedings where doing so would violate Article III. A bankruptcy court may thus no longer "determine" this fraudulent conveyance action without the consent of the parties. Notably, however, the action remains designated as "core" under the statute. Congress did

not violate Article III by selecting that label. And as a core proceeding, it is excluded from the category of case in which the bankruptcy court may issue a report and recommendation. *See* 28 U.S.C. § 157(c)(1) (report and recommendation authorized in proceeding "that is not a core proceeding").

For that reason, the Seventh Circuit recently concluded that a bankruptcy court's final orders could not be construed as reports and recommendations. In *In re Ortiz*, the court of appeals held that state law counterclaims were "core" proceedings under 28 U.S.C. § 157 that the bankruptcy court nevertheless lacked authority to decide after *Stern*. 2011 WL 6880651, at *4. To determine its own appellate jurisdiction, the court then considered, among other possibilities, whether the bankruptcy court's final "orders should be considered … proposed findings of fact and conclusions of law under 28 U.S.C. § 157(c)(1)." *Id.* at *3. The Seventh Circuit concluded that they could not. "For the bankruptcy judge's orders to function as proposed findings of fact or conclusions of law," the court explained, "we would have to hold that the debtors' complaints were 'not a core proceeding' but are 'otherwise related to a case under title 11.'" *Id.* at *7. Yet, as the court of appeals had "just concluded, the debtors' claims qualify as core proceedings and therefore do not fit under § 157(c)(1)." *Id.* Like the Seventh Circuit, this Court should adhere to the straightforward language of § 157.

Until Congress revisits § 157 in light of *Stern*, it is inappropriate for courts to attempt to rewrite the statute. Significantly, even after *Stern*, the subparagraph designating fraudulent conveyance actions as "core," is not a dead letter. *See* 28 U.S.C. § 157(b)(2)(H). Although the bankruptcy court may no longer finally "determine" fraudulent conveyance actions or enter "judgments" absent the parties' consent, it may still "hear" the case and "enter appropriate orders." *See* § 157(b)(1). The "core" designation thus empowers the bankruptcy court to enter pretrial orders on discovery issues and resolve other non-dispositive matters. There is no constitutional obstacle to bankruptcy judges exercising such authority, as demonstrated by similar provisions in the Federal Magistrates Act. *See* 28 U.S.C. § 636(b)(1)(A) (authorizing magistrate judges to "hear and determine" non-dispositive pretrial matters and permitting reconsideration by district court only "where it has been shown that the magistrate judge's order is clearly erroneous or contrary to law"); *Bhan v. NME Hosps., Inc.*, 929 F.2d 1404, 1414-15 (9th Cir. 1991) (rejecting Article III challenge to magistrate judges' authority to hear and determine discovery matters). Because § 157(b)(2)(H) retains significance after *Stern*, the court cannot excise the provision; Congress's designation of fraudulent conveyance actions among enumerated "core" proceedings remains effective.

For this Court to remove fraudulent conveyance actions from the list of enumerated "core" proceedings merely because bankruptcy courts lack authority to

finally "determine" them over the parties' objection would impermissibly nullify more of the statute than is necessary. *See Ayotte*, 546 U.S. at 329. Several bankruptcy and district courts that have purported to remove fraudulent conveyance actions from "core" proceedings have done so in an impermissible attempt to effectuate their best guess of what Congress would have intended. *See In re Refco*, No. 05-60006, 2011 WL 5974532, at *9-10 (Bankr. S.D.N.Y. Nov. 30, 2011); *In re Mortgage Store, Inc.*, No. 11-00439, 2011 WL 5056990, at *6 (D. Haw. Oct. 5, 2011); *see also* Br. of G. Eric Brunstad, Jr. at 27-28 (arguing same). Although recognizing that "the Judicial Code and Bankruptcy Rules do not specifically contemplate bankruptcy courts issuing proposed finding of fact and conclusions of law in core matters," those courts take the view that Congress would have intended that offending actions be "removed" altogether from "core jurisdiction." *See Refco*, 2011 WL 5974532, at *9-10.[5]

[5] *Refco* and several amici, *see* Br. of S. Todd Brown et al. at 24; Br. of G. Eric Brunstad, Jr. at 27-28, also rely on dicta from *Stern* in which the Supreme Court observed that it did "not think the removal of counterclaims such as Vickie's from core bankruptcy jurisdiction meaningfully changes the division of labor in the current statute." 131 S. Ct. at 2620. Considered in context, it is apparent that the Court was referring to *removing the authority* of bankruptcy courts to "determine" certain "core" matters, not removing a category of cases from one subsection of the statute and placing it within another. Not surprisingly, the Court elsewhere in its opinion declared unequivocally that "Vickie's counterclaim against Pierce for tortious interference is a 'core proceeding' under the plain text of [the statute]." *Id.* at 2604.

While legislative intent is relevant to the determination whether to strike down an *entire statute* or only that part that must be excised in order to prevent its unconstitutional application, *see Ayotte*, 546 U.S. at 330, courts may not rewrite a statute in an effort to make it read the way Congress would have written it had it known that some application of the statute would be found invalid. *See id.* at 330; *Seminole Tribe*, 517 U.S. at 76. Congress has every ability to alter the bankruptcy courts' statutory authority (subject to constitutional constraints), and it is not the place of the courts to revise the statute to achieve a result that Congress might have wanted but for which it did not provide. *See Ayotte*, 546 U.S. at 329-30.

Nor can the statute be read to somehow confer, as a lesser-included-power, the authority to issue reports and recommendations in core proceedings. Although bankruptcy courts might retain authority to "hear" core proceedings, that power does not include the authority to issue the sort of report and recommendation contemplated by 28 U.S.C. § 157(c)(1). If it did, the second sentence of § 157(c)(1) would be superfluous, as there would be no need to grant bankruptcy courts authority to both hear, *and* issue reports and recommendations in, non-core proceedings. *See* 28 U.S.C. § 157(c)(1). Furthermore, unlike the mere opinions or musings of a bankruptcy judge, a statutory report and recommendation carries important legal consequences. The district court is required to consider a report and recommendation, and it reviews *de novo* only those portions to which a party

objects. *Id.* Issuing a report and recommendation thus requires a specific grant of authority that is not inherent in the power to "hear" a proceeding. In sum, there simply is no statutory authority for bankruptcy judges to issue a reports and recommendations in core proceedings.

Bankruptcy courts could nevertheless retain important authority in fraudulent conveyance actions. Where the parties consent, the bankruptcy court retains authority to "hear and determine" the proceeding. *See* 28 U.S.C. § 157(c)(2). Even where the bankruptcy court cannot enter final judgment, it might still enter appropriate orders on non-dispositive pretrial matters if this Court so construes § 157(b). And, if Congress so chooses, it may amend the statute to confer bankruptcy judges in core proceedings with the same authority exercised by magistrate judges. It is not, however, within the power of this Court to amend the statute itself, as some lower courts have done.

B. This Court Need Not Address the Constitutional Questions that Would Arise from an Expansive Report-and-Recommendation Scheme

Because bankruptcy judges lack statutory authority to issue a report and recommendation in lieu of entering final judgment in a core proceeding, this Court need not, and should not, address the constitutional questions that may arise in connection with such a practice. The text of the statute is unambiguous, and this Court need not resort to the canon of constitutional avoidance to conclude that

bankruptcy courts lack authority to issue a report and recommendation in connection with a core proceeding. *See Stern*, 131 S. Ct. at 2605. Nevertheless, the serious constitutional questions that would arise from an expansive report-and-recommendation scheme lend further support to this conclusion.

Congress may, within limits, authorize the appointment of subordinate officers to assist federal district courts with decisionmaking in civil and criminal cases that otherwise require an Article III tribunal. The Supreme Court has set forth boundaries for use of non-Article III judges, specifically with respect to magistrate judges.

Most notably, in *United States v. Raddatz*, 447 U.S. 667 (1980), the Court concluded that magistrate judges without Article III protections can conduct evidentiary hearings on the voluntariness of confessions and issue proposed findings of fact and a recommendation. In *Raddatz*, the Court reviewed the Federal Magistrates Act, which grants magistrate judges authority to "hear and determine" certain pretrial matters, such as in discovery disputes, and authority to propose "findings of fact and recommendations for the disposition" in other "dispositive" pretrial matters, including suppression hearings. *Id.* at 673; 28 U.S.C. § 636(b)(1). And we can presume that Congress may constitutionally empower bankruptcy judges to act to the same extent as magistrates.

Notably, however, the Federal Magistrates Act does not authorize a magistrate judge to conduct the final merits evidentiary hearing – a jury or non-jury trial – in a civil action and issue proposed findings and a recommendation unless the parties consent. *See* 28 U.S.C. § 636(c) (magistrates may preside over final merits hearing only with consent of the parties). Indeed, *Raddatz* suggests that considerations of due process may impose some outer boundaries on the constitutionality of a report-and-recommendation scheme. *See* 447 U.S. at 681 n.7. In *Raddatz*, the magistrate found a criminal defendant's confession voluntary based on live testimony and credibility determinations by the magistrate. *Id.* at 669-72. The magistrate thus recommended denial of the defendant's motion to suppress. *Id.* at 671. The district court, without taking further evidence or hearing live testimony, adopted the magistrate's findings and recommendation. *Id.* at 672. Although the Supreme Court concluded that this procedure neither deprived the defendant of due process of law nor violated Article III, it observed that it could give rise to "serious questions" in other circumstances. *Id.* at 681 n.7. Specifically, the Court noted that more difficult questions would arise if a magistrate made credibility determinations that the district court then *rejected* without a live rehearing of the witnesses. *Id.*[6] Furthermore, in upholding the procedure permitted by the Federal Magistrates Act, the Court specifically

[6] Because the district court in *Raddatz* adopted the credibility findings of the magistrate, the Court did not reach this issue. *See id.*

observed that the magistrate was not conducting the final merits hearing on guilt or innocence. *Id.* at 678-79.

Raddatz leaves unresolved the question how far Congress may go in assigning a non-Article III tribunal responsibility over a final merits hearing. Section 157 of the Judicial Code does purport to give bankruptcy judges just such authority. *See* 28 U.S.C. § 157(c). Although § 157 in many ways parallels the Federal Magistrates Act, it also specifically empowers bankruptcy judges to use the report-and-recommendation scheme at *all phases* of a civil action, including the final trial on the merits in civil actions brought by a bankruptcy trustee. *See id.*[7] It enables bankruptcy judges to do so even in simple common law actions against non-creditor defendants with no connection to the bankruptcy estate other than as defendants. In assigning bankruptcy judges this authority, Congress may have assumed that bankruptcy judges' role in overseeing the broader bankruptcy process provided a basis for giving bankruptcy courts greater latitude than magistrate judges. But *Stern* makes clear that even suits seeking to augment the bankruptcy estate are subject to constitutional limits on Congress's authority to assign them to bankruptcy judges. *Stern*, 131 S. Ct. 2615.

[7] Any action brought by the trustee will seek to enlarge the estate and, therefore, they are all at least "related-to" actions. *See In re Am. Hardwoods, Inc.*, 885 F.2d 621, 623 (9th Cir. 1989) (describing scope of "related-to" jurisdiction).

The breadth of the potential use of the report-and-recommendation procedure by bankruptcy judges thus raises significant constitutional concerns following *Stern*. Although *Stern* did not address the issue directly, together with the Court's earlier decisions, *Stern* at least raises serious questions about the constitutionality of bankruptcy courts offering reports and recommendations following a final evidentiary hearing on the merits.

Notably, in many cases governed by *Stern*, the bankruptcy judge would never have the opportunity to issue a report and recommendation in connection with a final hearing. Following *Granfinanciera*, a defendant in such cases has a right to a jury trial. *See* 492 U.S. at 36. If the defendant invokes that right, and does not consent to jury trial in the bankruptcy court, the district court will conduct the entire merits hearing in any event. *In re Cinematronics*, 916 F.2d 1444, 1451 (9th Cir. 1990) ("[B]ankruptcy courts cannot conduct jury trials on noncore matters, where the parties have not consented.").

The additional circumstances in which the bankruptcy courts' constitutional authority to issue reports and recommendations is in doubt are therefore narrow, but not therefore unimportant. The authority of bankruptcy judges to issue a report and recommendation after a final hearing on the merits would arise only in either (i) a non-jury action (an action historically lying in equity) or (ii) a case in which the defendant prefers a bench trial and thus waives his jury right. The question,

then, is whether a defendant who is entitled to a final judgment by an Article III judge is always therefore entitled to a merits hearing in front an Article III judge or only if there is a jury? Put differently, absent a jury right, may Congress grant report-and-recommendation power as to the final merits hearings to a non-Article-III judge?

The concern evident in *Raddatz* suggests that the answer may well be no. Where the bankruptcy estate seeks affirmative recovery from a defendant, the scope of Article III's protection should not depend on other factors such as jury availability and desirability. Whether a case would have been tried before a jury in 1789 does not affect whether the presiding judge must enjoy Article III protections. Article III, unlike the Seventh Amendment, draws no distinction between actions sounding in law and in equity. *See Stern*, 131 S. Ct. at 2609 ("Congress may not withdraw from judicial cognizance any matter which from its nature, is the subject of a suit at the common law, *or in equity*, or admiralty." (emphasis added) (internal quotation marks omitted)).

In sum, to the extent that bankruptcy judges are authorized to propose findings of fact and conclusions of law on matters over which magistrate judges exercise similar authority, the Constitution presents no obstacle, so long as Congress, and not the courts, rewrite the statute to confer such authority. But to the extent that bankruptcy judges have the additional authority to issue a report and

recommendation after a final hearing on the merits, serious constitutional questions could arise. Because this case does not involve a final hearing on the merits, and because it should be resolved on narrower statutory grounds, this Court need not, and should not, decide all of the circumstances in which the report-and-recommendation procedure is constitutionally permitted.

CONCLUSION

For the foregoing reasons, this Court should vacate the judgment below and remand this matter for further proceedings.

Respectfully submitted,

s/ Douglas H. Hallward-Driemeier
ROPES & GRAY LLP
Douglas H. Hallward-Driemeier
One Metro Center
700 12th Street, NW, Suite 900
Washington, DC 20005-3948
Phone: (202) 508-4600
Facsimile: (202) 508-4650

ROPES & GRAY LLP
D. Ross Martin
Prudential Tower
800 Boylston Street
Boston, MA 02199-3600
Phone: (617) 951-7000
Facsimile: (617) 951-7050

Attorneys for Marcia M. Tingley

CERTIFICATE OF SERVICE

I hereby certify that I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system on January 19, 2012.

I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

s/ Douglas H. Hallward-Driemeier

ROPES & GRAY LLP
Douglas H. Hallward-Driemeier
One Metro Center
700 12th Street, NW, Suite 900
Washington, DC 20005-3948
Phone: (202) 508-4600
Facsimile: (202) 508-4650

Attorney for Marcia M. Tingley

CERTIFICATE OF COMPLIANCE WITH RULE 32(a)

1. This brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because this brief contains 6,991 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

2. This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in a proportionally spaced typeface using Microsoft Word 2007 in 14-point Times New Roman type style.

s/ Douglas H. Hallward-Driemeier

ROPES & GRAY LLP
Douglas H. Hallward-Driemeier
One Metro Center
700 12th Street, NW, Suite 900
Washington, DC 20005-3948
Phone: (202) 508-4600
Facsimile: (202) 508-4650

Attorney for Marcia M. Tingley

Dated: January 19, 2012