IN THE

UNITED STATES COURT OF APPEALS

for the

NINTH CIRCUIT

Case No. 11-35162

In the Matter of: BELLINGHAM INSURANCE AGENCY, INC., *Debtor,*

EXECUTIVE BENEFITS INSURANCE AGENCY,

Appellant,

-v.-

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

Appellee.

ON APPEAL FROM THE UNITED STATES WESTERN DISTRICT COURT OF WASHINGTON, SEATTLE
CASE NO. 10-00929-MJP

BRIEF OF AMICI CURIAE (i) NEW CH YMC ACQUISITION LLC, (ii) YELLOWSTONE MOUNTAIN CLUB, LLC AND (iii) YELLOWSTONE DEVELOPMENT, LLC IN SUPPORT OF NEITHER PARTY AND IN RESPONSE TO THE COURT'S QUESTIONS

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CORPORATE DISCLOSURE STATEMENT

New CH YMC Acquisition LLC, a Delaware limited liability company, is owned 100% by CrossHarbor Institutional Partners, L.P., a Delaware limited partnership. No publicly traded corporation owns any interest in New CH YMC Acquisition LLC.

Yellowstone Mountain Club, LLC, a Montana limited liability company, is owned 100% by YC Holdings LLC, a Delaware limited liability company. No publicly traded corporation owns any interest in Yellowstone Mountain Club, LLC.

Yellowstone Development, LLC, a Montana limited liability company, is owned 100% by YC Holdings LLC, a Delaware limited liability company. No publicly traded corporation owns any interest in Yellowstone Development, LLC.

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INTRODUCTION

The two questions presented by the Court's Order of November 4, 2011, address the extent to which bankruptcy courts may enter orders in fraudulent transfer actions. The first question is whether a "final" order may be entered by bankruptcy courts in those actions. The second is whether, if those actions may not be heard as "core" matters in which a bankruptcy court may enter a final order, bankruptcy courts may nonetheless submit proposed findings of fact and conclusions of law subject to *de novo* review by the district courts.

Amici herein will address only the second question in this brief. *Amici* submit that bankruptcy courts have authority to submit proposed findings of fact and conclusions of law in fraudulent transfer actions even if those actions are non-core.

INTERESTS OF AMICI[1]

Amici are parties to the Yellowstone Mountain Club, LLC bankruptcy proceedings pending in the United States Bankruptcy Court for the District of Montana, Chapter 11 Case No. 08-61570-11-RBK. In proceedings related to the Yellowstone Mountain Club bankruptcy case, the bankruptcy court considered the very same procedural issues raised by the Court in its November 4, 2011 order.

[1] Neither the parties to this matter, nor their respective counsel, have authored this brief in whole or in part, nor have they funded its preparation.

Amici submit this brief in an effort to clarify the law and provide clarity in an area that has created confusion and uncertainty in bankruptcy practice. *Amici* are authorized to file this brief pursuant to the Court's November 4, 2011, order inviting supplemental briefs by *amicus curiae*.

LEGAL ARGUMENT

A. Judicial Power and Article I Judges.

(i) The Statutory Framework

Article III of the Constitution provides that "[t]he judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as Congress may from time to time ordain and establish," and that the judges of those courts must have life tenure (assuming "good Behavior") and receive undiminished compensation during that tenure. U.S. CONST. art. III, § 1. These protections ensure independence of the judiciary, which is an "inseparable element of the constitutional system of checks and balances." *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 58 (1982).

Nevertheless, Congress may, pursuant to Article I of the Constitution, vest decision-making authority over certain disputes in tribunals that lack the attributes of Article III courts. *Thomas v. Union Carbide Agric. Prods., Inc.*, 473 U.S. 568, 583 (1986). Bankruptcy Courts are Article I tribunals. Whether a congressional delegation of adjudicative functions to an Article I tribunal is constitutionally

permissible "must be assessed by reference to the purposes underlying the requirements of Article III." *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 847-48 (1986).

The question of the extent to which Congress may delegate the judicial power of the United States to Article I bankruptcy courts, consistent with constitutional limitations, is not new. In 1978, Congress re-wrote the nation's bankruptcy laws, replacing the Bankruptcy Act of 1898 with the Code. The 1978 Code gave district courts broad jurisdiction over "all civil proceedings arising under title 11 [the Code] or arising in or related to cases under title 11." 28 U.S.C. § 1471 (repealed 1984). The 1978 Code also established bankruptcy courts in each judicial district and empowered them to exercise the full judicial power of the United States in all matters within the scope of bankruptcy jurisdiction. *See* 28 U.S.C. § 1471(c) (repealed) (bankruptcy courts "exercise all of the jurisdiction conferred by this section on the district courts."); *Marshall v. Stern (In re Marshall)*, 600 F.3d 1037, 1040, 1051 (9th Cir. 2010) ("*Marshall*").

The Supreme Court answered the question of whether the 1978 Code's complete transfer of judicial power from the district courts to Article I bankruptcy courts violated Article III in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.,* 458 U.S. 50 (1982). After Northern Pipeline filed for bankruptcy, it brought suit in the bankruptcy court against Marathon on a state-law breach-of-

contract claim. *Marathon*, 458 U.S. at 56. The state-law claim did not "arise under" the Code or "arise in" the bankruptcy case, but was "related to" the bankruptcy case because any recovery on the claim would have augmented the bankruptcy estate. *Id*. at 54, 71-72. Under the 1978 Code, bankruptcy courts could enter final orders in proceedings "related to" the bankruptcy case. *Id*. at 54. The Supreme Court held that permitting non-Article III bankruptcy courts to enter final orders on state-law contract claims merely because those claims were "related to" a bankruptcy case contravened Article III because doing so removed "the essential attributes of the judicial power from the Article III district court and vested those attributes in a non-Article III adjunct." *Id*. at 87 (plurality opinion); *id*. at 91-92 (Rehnquist, J., concurring).

It is important to note that, in *Marathon*, a plurality of four Justices concluded that there was a constitutionally significant difference between "public rights" matters "arising between the Government and persons subject to its authority" that historically could have been determined by Congress or the executive branch, on the one hand, and "private rights" matters, which include disputes between individuals arising under common law, on the other. *Id*. at 67-70. "Public rights" matters could, under certain circumstances, be constitutionally adjudicated by entry of a final order by non-Article III tribunals. *Id*. at 69. By contrast, "private rights" matters, generally, could not. *Id*. at 70-71, 83-87.

In response to the constitutional concern articulated in *Marathon*, Congress amended title 28 of the United Sates Code in 1984.

The amended statute remains in place today, and gives federal district courts original and exclusive jurisdiction over "all cases under title 11," and original but not exclusive jurisdiction over "all civil proceedings arising under" the Code and all matters "arising in" or "related to" bankruptcy cases under the Code. 28 U.S.C. § 1334. Where the scope of bankruptcy *jurisdiction* is concerned, the Code today is substantially similar to that which existed pre-*Marathon*, (*i.e.*, the 1978 Code). *Marshall*, 600 F.3d at 1052.

However, "the manner in which the bankruptcy court may exercise its delegated jurisdiction differs." *Id*. at 1053. Through the 1984 revisions, Congress revised the Code provisions governing the extent to which bankruptcy courts may exercise the judicial power of the United States through the entry of final orders. The revised statutes were designed to limit the power of bankruptcy courts to enter final orders to the "public rights" matters that *Marathon* suggested may be constitutionally adjudicated in an Article I court. The statute achieves this by distinguishing between "core" bankruptcy proceedings that "aris[e] under" the Code or "aris[e] in a case under" the Code, on the one hand, and "non-core" proceedings that are "otherwise related to" a case under the bankruptcy laws, on the other, and by providing different degrees of authority to bankruptcy courts

depending upon which category of matter is involved. *See* 28 U.S.C. §§ 157(b), (c).

The distinction is set out in 28 U.S.C. § 157. For "core" matters arising under the Code or arising in a bankruptcy case, bankruptcy courts are authorized to exercise the full range of judicial power of the United States and may enter final orders reviewable only by appeal. 28 U.S.C. § 157(b). For "non-core" matters that are merely "related to" a bankruptcy case, bankruptcy courts may not exercise the full extent of that power without the parties' express written consent, and may instead only enter proposed findings of fact and conclusions of law that are reviewable, *de novo*, by an Article III district court. 28 U.S.C. § 157(c)(1). In either case, *jurisdiction* is present and the matter may be *heard* by the bankruptcy court. The revised statute complies with *Marathon* by distinguishing between *the type of order that may be entered by the bankruptcy court* in "core" or "non-core" proceedings. Today, any interpretation of 28 U.S.C. § 157 must be consistent with *Marathon*.

In the revised statute, Congress identified representative "core" matters in which bankruptcy courts may enter final orders subject only to review on appeal. See 28 U.S.C. § 157(b)(2). "Core" matters identified in the statute include: the allowance and disallowance of claims against the estate; counterclaims by the estate against persons filing claims; turnover of estate property; preference

recovery; matters relating to the automatic stay; the dischargeability of debt and discharge of the debtor; and broad categories of matters such as the administration of the estate, the liquidation of assets of the estate or the adjustment of the debtor-creditor relationship. 28 U.S.C. § 157(b)(2).

However, Congress's designation of a matter as "core" does not necessarily mean that the matter may, consistent with the constitutional limitations noted in *Marathon*, be properly considered a "core" matter that may be adjudicated by an Article I court exercising the full extent of the judicial power of the United States. In other words: even though Congress tried to fix the statute, it may not have gotten the fix right. The Supreme Court explored this issue in *Granfinanciera* where the Court considered whether a defendant in a fraudulent transfer action was entitled to a jury trial pursuant to the Seventh Amendment, even though fraudulent transfer actions are "core" matters to be adjudicated by bankruptcy courts. *Granfinanciera, S.A. v. Nordberg,* 492 U.S. 33, 36 (1989). In finding that the defendant was entitled to a jury trial, the Court *in Granfinanciera* relied upon the public/private rights distinction articulated in *Marathon,* noting that because the defendant had not filed a claim against the bankruptcy estate, the matter was *not* a case in which "public rights" were to be adjudicated. *Id.* at 63-64. The Court reasoned that the fraudulent transfer action was "more accurately characterized as a private rather than a public right" because it involved "state-law contract claims

brought by a bankrupt corporation to augment the bankruptcy estate," and not a determination of "creditors' hierarchically ordered claims to a *pro rata* share" of the bankruptcy estate. *Id.* at 56. Thus, the Court held that the defendant was entitled to a jury trial because Congress's power to override the Seventh Amendment's right to a jury trial is implicated only in cases where "public rights" are litigated. *Id.* at 64-65.

Even though *Granfinanciera* was a Seventh Amendment jury trial right case, the Court's comments on the practical effect of a congressional determination that a matter was "core" (and, thus, a matter of public right) should have sounded the alarm that other problems may exist with the congressional fix for the problems identified in *Marathon*.

(ii) *Stern v. Marshall*, 131 S. Ct. 2594 (2011)

In many ways, *Marathon*, the revised statute and *Granfinanciera* set the stage for *Stern v. Marshall*, 131 S. Ct. 2594 (2011 ("*Stern*"). Boiled down its basics, the primary issue before the Supreme Court in *Stern* was whether Congress's designation of estate counterclaims as "core" matters was permissible when judged alongside the Supreme Court's Article I jurisprudence, including *Marathon*. Specifically, the Court considered whether a state law counterclaim that was not resolved as part of the allowance or disallowance of the underlying claim to which it related, could properly be considered a "core" matter. The statute

specifically identifies all counterclaims by the estate as being "core" matters. *See* 28 U.S.C. §157(b)(2)(c). However, the Court found that, on the facts presented, the counterclaim could not, consistent with the Constitution, be considered a "core" matter for which an Article I bankruptcy court could enter a final order.

In reaching that conclusion, the Supreme Court did not specifically address the procedural question which *amici* raise herein. However, Supreme Court's majority opinion in *Stern* noted two points that bear upon the issue. Indeed, a careful review of *Stern* reveals the Court's view as to the operation of the statute as it relates to the question addressed herein.

First, the procedural background of *Stern* must be kept in focus. After the bankruptcy court entered a final judgment on the counterclaim, an appeal was brought to the district court. The district court, however, found that the counterclaim could not be considered a core matter under *Marathon*, treated the bankruptcy court's findings of fact and conclusions of law as proposed findings and conclusions, and then subjected them to *de novo* review. In other words, although the counterclaim could not be considered a "core" matter, the district court found that it *was* properly considered a matter that was "related to" the bankruptcy case. Both this Court and the Supreme Court noted the procedure utilized by the district court. Despite the opportunity, neither court criticized the procedure. *See Stern*, 131 S.Ct. at 2602; *Marshall*, 600 F.3d at 1039-40.

Admittedly, absence of criticism is not an affirmative endorsement. However, this lack of any criticism, or even the inclusion of a footnote by either court stating that they expressed no view as to the procedure, is worthy of note.

Second, the Supreme Court's analysis of the statutory framework is important. The Court first noted the extent to which bankruptcy courts may act in "core" matters, discussing 28 U.S.C. § 157(b). *Stern*, 131 S.Ct. at 2603-04. Then, the Court went directly to 28 U.S.C. § 157(c)(1), and stated:

> When a bankruptcy judge determines that a referred "proceeding . . . is not a core proceeding but . . . is otherwise related to a case under title 11," the judge may only "submit proposed findings of fact and conclusions of law to the district court."

Stern, 131 S. Ct. at 2604. This manner of reading the statute is important. The bankruptcy court must first decide whether a matter is core. *If it is not core*, but *is* related to a bankruptcy case, the bankruptcy court must proceed by entry of proposed findings and conclusions only. This is important because the Court's analysis also indicates that where something was designated as "core" by Congress, but cannot be "core" on a given set of facts, it should be "removed" from the "core" category and handled as non-core. *See Stern*, 131 S. Ct. at 2620 ("We do not think the *removal of counterclaims such as [this] from core bankruptcy jurisdiction* meaningfully changes the division of labor . . . .") (emphasis supplied). Thus, although the Court did not expressly rule on the

procedural issue raised in the case at bar, the analytical framework within which the Court discussed the statutory landscape in *Stern* is important.

(iii) Recent Decisions Analyzing *Stern*

Several courts have grappled with the question of whether bankruptcy courts may enter proposed findings of fact and conclusions of law when a matter is identified in 28 U.S.C. § 157 as being a "core" matter, but cannot be adjudicated as such consistent with constitutional limitations. There is no consensus.

In *In re Blixseth*, No. 10-00088, 2011 WL 3274042 (Bankr. D. Mont. Aug. 1, 2011), the United States Bankruptcy Court for the District of Montana considered a defendant's motion seeking dismissal or, in the alternative, mandatory or permissive abstention, of an adversary proceeding seeking, *inter alia,* the avoidance and recovery of fraudulent transfers. *Id.* at *1. The defendant argued that the bankruptcy court lacked subject matter jurisdiction. *Id.*

The *Blixseth* court rejected the defendants' arguments for dismissal or abstention. *Id.* at *2-9. However, the *Blixseth* court, *sua sponte*, considered the impact of *Stern v. Marshall* on the constitutionality of the bankruptcy court's subject matter jurisdiction over the equitable subordination, fraudulent transfer and preferential transfer claims asserted against the defendant. The court noted that, under *Stern v. Marshall*, although the court had core jurisdiction over those claims "pursuant to its statutory authority, that authority may not be exercised unless it is

also constitutional." *Id.* at *10. The *Blixseth* court reasoned that, in order for a bankruptcy court to adjudicate a claim, such claim had to be a matter of "public rights" as described by the Supreme Court in *Marathon*. *Id.* at *11.

The Blixseth court found that although some of the matters before it were labeled "core" proceedings, they were not matters of "public rights". *Id.* The court then reasoned that "unlike in non-core proceedings, a bankruptcy court has no statutory authority to render findings of fact and conclusions of law for core proceedings that it may not constitutionally hear." *Id.* at *12. The *Blixseth* court accordingly concluded that because: (i) it could not constitutionally hear the fraudulent conveyance claim as a core proceeding; and (ii) it had no statutory authority to hear the case as a non-core proceeding, it lacked subject matter jurisdiction to adjudicate the fraudulent conveyance claims. *Id.*[2]

[2] The court initially ruled that under *Stern*, jurisdiction was lacking over certain claims. *In re Blixseth*, 2011 WL 3274042, at *12. However, the court subsequently reconsidered whether jurisdiction was present and found that it was, indeed, present. *See* Case No. 10-00094, Order entered Dec. 14, 2011 and Case No. 09-00014, Order entered Dec. 13, 2011, both in the United States Bankruptcy Court for the District of Montana. Although it is reasonable to infer from the court's ultimate rulings on jurisdiction that the *Blixseth* court would agree with the procedural analysis herein, the procedural question has not been expressly revisited by the *Blixseth* court. It is reasonable to infer that the *Blixseth* court would agree with the analysis herein because in reversing course on the jurisdictional question, it kept the cases before it. Presumably, the court would not have done so if it believed it had no power to adjudicate the matter by entry of some form of order.

The United States Bankruptcy Court for the Southern District of New York recently considered the same issues with different results. *See In re Refco,* No. 07-3060, 2011 WL 5984532 (Bankr. S.D.N.Y. Nov. 30, 2011). In *Refco*, a litigation trustee commenced litigation seeking, *inter alia*, to avoid and recover fraudulent transfers. The *Refco* court observed that the Supreme Court's holding in *Stern* raised two questions with respect to the bankruptcy court's power to rule on the fraudulent transfer claims: (a) whether the "core" fraudulent transfer and related unjust enrichment claim "so resemble[d] the state law tortious interference counterclaim . . . at issue in *Stern*, as to preclude [the bankruptcy court's] ability to issue a final judgment," and (b) whether, if the bankruptcy court indeed lacks the constitutional power to issue a final judgment, it would nevertheless have statutory or other authority to submit proposed findings of fact and conclusions of law to the district court. *Id.* at *2.

The *Refco* court held that the adjudication of fraudulent transfer actions has "repeated[ly] and emphatic[ally]" been found to fall within the authority of the bankruptcy court, a result that has helped ensure a "coordinated response overseen by one judge on behalf of a host of creditor-victims." *Id.* The *Refco* court further held that even if it was later determined that the bankruptcy court lacked authority to enter a final judgment on the fraudulent transfer claims, *Stern* and other case law suggests that the matter would become "non-core" and that a bankruptcy court may

still enter proposed findings of fact and conclusions of law for *de novo* review by the district court. *Id.*

Written decisions finding that *no orders* may be entered by bankruptcy courts in these matters – the "dead zone" decisions – contain little, if any, substantive analysis to support this result.[3] Those decisions simply look at the statute and state a position. The *Stern* analysis, together with the application of principles of statutory construction and other well-settled principles of federal law, support the *Refco* holding. An expansion of the *Refco* analysis is set forth below.

B. WHETHER BANKRUPTCY COURTS CAN SUBMIT PROPOSED FINDINGS OF FACT AND CONCLUSIONS OF LAW IN CONSTITUTIONALLY SUSPECT OR CONSTITUTIONALLY IMPERMISSIBLE "CORE" MATTERS

The cases discussed above set the stage for the analysis set out below by *amici* herein. A simplistic restatement of the issue is: "When Congress mistakenly designates a matter as 'core,' what, if anything, may a bankruptcy court do to determine the matter?" Are bankruptcy courts precluded from entering *any* order, even though it is beyond dispute that jurisdiction exists? *Amici* submit that bankruptcy courts are, in such circumstances, able to enter proposed findings of fact and conclusions of law because that is the extent of judicial power granted to

[3] *See*, *e.q.*, *Ortiz v. Aurera Health Care, Inc. (In re Ortiz)*, Case No. 10-3465, 2011 WL 6880651, at *7 (7th Cir. Dec. 30, 2011) (stating conclusion, but offering no analysis supporting conclusion beyond cursory review of statutory text); *In re Blixseth*, 2011 WL 3274042, at *11-12.

bankruptcy courts for matters that are merely "related to" a bankruptcy case. Simply put, if a matter *cannot* be "core," *it is not* "core," regardless of any statutory designation. If not "core," the question is whether the matter fits within the scope of matters that are "non-core," and then handled accordingly. *Amici* submit that this result is (i) proper as a matter of statutory construction, and (ii) appropriate as an exercise in the creation of federal common law to fill a procedural gap in a federal statutory scheme.

(i) <u>Analysis of the Statute</u>

Two bedrock principles of statutory construction and one general principle of federal jurisdiction must be kept in focus when analyzing whether bankruptcy courts may enter proposed findings of fact and conclusions of law in matters identified in the statute as being "core," but which cannot be heard as "core" matters because doing so violates Article III of the Constitution. These principles demonstrate that the approach advocated by *amici* herein is properly grounded in the statutory text.

Statutory construction is a "holistic endeavor." *United Sav. Ass'n of Texas v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 371 (1988). In other words, statutes must be read in context and alongside other related provisions in order to interpret their meaning. The "overall statutory scheme often clarifies a seemingly ambiguous provision because 'only one of the permissible meanings . . .

produces a substantive effect that is compatible with the rest of the law.'" *In re Ransom*, 380 B.R. 799, 807 (9th Cir. BAP 2007) (quoting *Timbers of Inwood*, *supra*); *see also Davis v. Michigan Dept. of Treasury*, 489 U.S. 803, 809 (1989) ("[S]tatutory language cannot be construed in a vacuum. It is a fundamental canon of statutory construction that the words of a statute must be read in their context and with a view to their place in the overall statutory scheme.") (internal citations omitted). Moreover, statutes should be applied as written except when literal construction leads to an absurd result. *Lamie v. U.S. Trustee*, 540 U.S. 526, 534 (2004); *Green v. Bock Laundry Mach. Co*., 490 U.S. 504, 527 (1989) (rejecting literal interpretation of federal rule that would produce an absurd result); C*entral States, S.E. & S.W. Areas Pension Fund v. Lady Baltimore Foods*, 960 F.2d 1339, 1345 (7th Cir. 1992) ("even interpretative literalists" recognize that if strict interpretation is absurd, "interpreter is free (we would say compelled) to depart in the direction of sense"), *cert. denied*, 113 S. Ct. 179 (1992).

In analyzing the grant of judicial power to bankruptcy courts in matters over which they have jurisdiction, courts should also bear in mind a basic tenet of federal jurisdiction: "[l]ike all federal courts, [a bankruptcy court has] a 'virtually unflagging obligation . . . to exercise the jurisdiction given it.'" *In re Gucci,* 309 B.R. 679, 683 (S.D.N.Y. 2004) (quoting *Colorado River Conserv. Dist. v. U.S.*, 424 U.S. 800, 817 (1976)). "Once presented with a valid basis for jurisdiction, it is

the general rule that courts are to exercise that grant of jurisdictional authority." *In re Weldon F. Stump & Co.*, 373 B.R. 823, 827 (Bankr. N.D. Ohio 2007) (citing *Colorado River*, *supra*). *Amici* recognize that this principle is most frequently applied in cases addressing whether a federal court should abstain in a given case, but contend that there is no reason why the principle is not more broadly applicable.

Bankruptcy jurisdiction arises under 28 U.S.C. § 1334, and provides for jurisdiction over a broad range of matters, extending as far as all matters that are "related to" a bankruptcy case, and 28 U.S.C. § 157 "refers" bankruptcy matters to bankruptcy courts. In response to *Marathon*, Congress created a two-tiered structure for the delegation of the judicial power of the United States to Article I bankruptcy judges: (i) a full delegation of judicial power for "core" matters, permitting bankruptcy courts to enter final orders in such matters; and (ii) a lesser delegation, permitting bankruptcy courts only to enter proposed findings of fact and conclusions of law, subject to *de novo* review, for non-core matters that are "related to" a bankruptcy case. *Compare* 28 U.S.C. §§157(b) and (c). Viewed alongside one another, it becomes clear that the jurisdictional grant in 28 U.S.C. § 1334 and procedures outlined in 28 U.S.C. § 157 not only work together but are also co-extensive – out to the very boundaries of bankruptcy jurisdiction.

Congress delegated judicial power to bankruptcy courts so that they may enter orders in all matters properly before them.

Courts which have held that bankruptcy courts are unable to enter *any* orders in matters identified by Congress as "core" matters, but which cannot, consistent with *Stern* and *Marathon*, be heard and ruled upon as "core" matters, rely on a perceived "dead zone" in the statute. *See In re Blixseth*, 2011 WL 3274042, at *11-12; *see also In re Ortiz*, 2011 WL 6880651, at *7. Those courts hold that when Congress has designated a matter as "core," Congress has only authorized them to enter a final order, which they may not do under *Stern* and *Marathon*. In other words, they refuse to characterize those matters as non-core because they have not been authorized by the statute to "move" something that is on the "core" list into the "non-core" category. This is a flawed approach.

Matters expressly designated as "core" by 28 U.S.C. § 157 include all "matters concerning the administration of the estate" and all "other proceedings affecting the liquidation of the assets of the estate or the adjustment of the debtor-creditor or the equity security holder relationship[.]" *See* 28 U.S.C. § 157(b)(2)(A), (O). From the scope of this statutory language, it is hard to conceive of a matter that isn't "core."

However, courts analyzing the bankruptcy statutes have construed the statutory text as limited by *Marathon*. *See*, *e.g.*, *Orion Pictures Corp. v. Showtime*

Networks, Inc. (In re Orion Pictures Corp.), 4 F.3d 1095, 1102-03 (2d Cir. 1993) (construing 28 U.S.C. § 157(b)(2)(A) as limited by *Marathon*); *Ben Cooper, Inc. v. Ins. Co. of Pennsylvania (In re Ben Cooper, Inc.)*, 896 F.2d 1394, 1397-99 (2d Cir. 1990) (same). Applying that rule, when matters are within the scope of 28 U.S.C. § 157(b)(2), but treating them as core matters would violate *Marathon* (and now, *Stern*), courts have determined that those matters *are* "non-core" "related-to" disputes. In other words, it is appropriate for bankruptcy courts to interpret the statutory text of 28 U.S.C. § 157 to see whether a matter may be treated as "core" on a given set of facts. *See Stern*, 131 S. Ct. at 2618. If it *cannot* be a core matter, the correct approach is to recognize that it *is non-core* and to proceed accordingly (regardless of the congressional designation in 28 U.S.C. § 157(b)(2)(B)).

This approach is consistent with *Stern*. The Court in *Stern* noted that 28 U.S.C. § 157(b)(1) is descriptive in nature. *Stern*, 131 S. Ct. at 2604. Subsection (b)(2) expands upon (b)(1), but again, is illustrative in nature. The Court then described the operation of the statute: for "core" matters, a final order may be entered but for non-core, "related to" matters, bankruptcy courts may only enter proposed findings and conclusions. There was no discussion in *Stern* of whether a matter that was improperly designated as core by Congress rendered bankruptcy courts powerless to enter any order. Indeed, the Supreme Court recognized that this argument could have been made, *see Stern*, at 2620 ("Pierce has not argued

that the bankruptcy courts 'are barred from 'hearing' all counterclaims' or proposing findings of fact and conclusions of law on those matters . . . ."), but ruled only that a final judgment could not be entered. If the Supreme Court believes that absolutely *no orders* may be entered by bankruptcy courts on matters impermissibly designated as core, it is reasonable to infer that the Court would have said so.

In fact, it is reasonable to infer from *Stern* that the Court approved of the manner in which the district court proceeded. In addressing *Stern's* impact on bankruptcy practice, the Court noted that "the *removal of counterclaims such as [this] from core bankruptcy jurisdiction* [would not] meaningfully change[] the *division of labor* in the current statute[.]" The Court discussed "*removal*" of the "core" counterclaim from the list of "core" matters, and *placing it* in the "non-core" category.[4] *See In re Refco Inc.*, No. 07-3060, 2011 WL 5974532, at *9-10; *see also RES-GA Four LLC v. Avalon Bldrs of Ga LLC*, No. 10-463, 2012 WL 13544, at *8-10 (M.D. Ga. Jan. 4, 2012); *In re The Mortgage Store, Inc.*, No. 11-00439, 2011 WL 5056990, at *5-6 (D. Haw. Oct. 5, 2011); *In re Coudert Bros.*

[4] This is implicit in the Court's division of labor discussion, which relates to which court – the bankruptcy or district court – may enter a final order in a matter. It is also important to note that the Court did not hold that all counterclaims may *never* be "core" matters. To the contrary, the Court stated that there will be times when a counterclaim *may* be core, and times when it may not. This supports the statutory construction advocated by *amici*.

LLP, No. 11-2785, 2011 WL 5593147, at *13-14 (S.D.N.Y. Sept. 23, 2011); *In re Canopy Fin., Inc*., No. 11-581, 2011 WL 3911082, at *3-5 (N.D. Ill. Sept 1, 2011); *In re Soporex, Inc*., No. 11-3306, 2011 WL 5911674, at *3-5 (Bankr. N.D. Tx. Nov. 28, 2011); *In re Univ. Marketing, Inc*., No. 09-15404, 2011 WL 5553280, at *3-6 (Bankr. E.D. Pa. Nov. 15, 2011); *In re Emerald Casino, Inc.*, 459 B.R. 298, 300 (Bankr. N.D. Ill. 2011). This is the correct approach and is contrary to the analysis in the "dead zone" cases. Those cases are based on the premise that once something is designated as "core," it cannot be "removed" and placed into the non-core category. A close reading of *Stern* reveals that the Court implicitly rejected that reasoning.

The foregoing demonstrates that the most plausible, reasonable reading of the statutory text, as construed by the Supreme Court, is that matters designated "core" by Congress, but which are beyond the scope of what can permissibly be handled as "core" matters, *are* non-core matters for which bankruptcy courts may enter proposed findings of fact and conclusions of law. Those matters are, when circumstances dictate, "removed" from the "core" category and placed in the "non-core" category, and handled accordingly. As construed by the Supreme Court, the statutory text requires what *amici* contend.

Moreover, this reading of the statute is supported by the principles of statutory construction and federal jurisdiction noted at the outset of this discussion.

The overall statutory scheme supports this interpretation. "Core" matters are a subset of all matters that fall within broad scope of bankruptcy jurisdiction – they can be viewed as a small circle within a larger circle. If something cannot be core (regardless of whether it is listed in 28 U.S.C. § 157(b)(2)), but fits within the scope of non-core, "related to" matters, it fits within the larger circle and 28 U.S.C. § 157(c) provides authority for the bankruptcy court to hear the matter and enter proposed findings of fact and conclusions of law. *See In re Refco Inc*., No. 07-3060, 2011 WL 5974532, at *10 (reviewing statute); *In re Univ. Marketing, Inc*., 2011 WL 5553280, at * 5 ("every core proceeding necessarily is also 'related to' the bankruptcy case for purposes of 28 U.S.C. § 1334(b). One might say that every core proceeding is related, but not every related proceeding is core and that a matter must at least be related to the bankruptcy for the bankruptcy court to exercise any type of subject matter jurisdiction."); *see also RES-GA Four LLC*, 2012 WL 13544, at *9 (quoting *Univ. Marketing*, *supra*). Viewed in this manner, the delegation of authority contained in 28 U.S.C. § 157 is both consistent and coterminous with the full scope of bankruptcy jurisdiction set out in 28 U.S.C. § 1334. Construing the statute as providing authority to enter some form of an order (final or proposed findings and conclusions) for all matters within the jurisdictional grant, makes good sense; construing the statute as providing for a "dead zone" does not. *See RES-GA Four LLC*, 2012 WL 13544, at *9 ("The rule that a

bankruptcy court has the power to hear a referred case whether it is core or non-core is logical . . . ."). Viewing the statutory scheme holistically, the reading of the statute advocated by *amici* herein is the most supportable.

This reading of the statute is bolstered by the principle that federal courts have a virtually unflagging obligation to exercise the jurisdiction given to them. The "dead zone" reading of the statutory text violates this principle. It creates a situation where, although *jurisdiction* is present under 28 U.S.C. § 1334, other provisions of the same statutory scheme are being construed in a manner that precludes bankruptcy courts from entering *any orders* in those matters. A correct reading of the statute cannot lead to the conclusion that there are instances where jurisdiction is present without authority to enter any order at all. *In re The Mortgage Store, Inc*., 2011 WL 5056990, at *6; *In re Universal Marketing, Inc*., 2011 WL 5553280, at *5.

The "dead zone" approach also leads to an absurd result that should be avoided. *See In re Soporex, Inc*., 2011 WL 5911674, at *4 (noting "absurd" result); *In re Refco Inc*., No. 07-3060, 2011 WL 5974532, at *10 (noting "absurd" result); *In re Emerald Casino, Inc*., 459 B.R. at 300, n.1 (noting "bizarre" result). To construe a statute as conferring jurisdiction, but precluding the exercise of any judicial power, simply cannot be correct. To construe a statute as providing no authority for bankruptcy courts to enter orders in matters that technically fit within

the exceedingly broad text of 28 U.S.C. § 157(b)(2)(A) and (O) but which are beyond what is permissible under *Stern* and *Marathon*, simply cannot be correct. This Court should reject a reading of the statute that leads to an absurd result in favor of a more straightforward, holistic and supportable reading of the statute that provides for the seamless exercise of judicial power to the full extent of the statutory grant of jurisdiction.

Where matters cannot be considered as "core" consistent with *Stern* or *Marathon* and where 28 U.S.C. § 157 nonetheless characterizes those matters as "core," this Court should construe the Bankruptcy Code as permitting bankruptcy courts to treat these matters as non-core, "related to" matters in which bankruptcy courts may enter proposed findings of fact and conclusions of law subject to *de novo* review by the district courts. In other words, matters that cannot be "core," but which were listed by Congress in 28 U.S.C. § 157(b)(2), should be "removed" from the "core" list and addressed as non-core matters.

(ii) Federal Courts Have Inherent Authority to Fill Procedural Gaps in Federal Statutory Schemes

Even if the Court disagrees with the analysis set forth above and concludes that there is, in fact, a "dead zone" in the statute that is resolved neither by *Stern* nor principles of statutory construction, there is ample authority for federal courts to create a federal common law rule to fill in any procedural gaps that may exist in a federal statutory framework. A*mici* urge the creation of a federal common law

rule providing that, in the event a statutorily designated "core" matter cannot, consistent with the Constitution, be heard and ruled upon by a bankruptcy court as a "core" matter, it should be heard and ruled upon as a "non-core" matter.

In *Erie Railroad Company v. Tompkins*, 304 U.S. 64 (1938), the Supreme Court declared that "[t]here is no federal general common law." *Id*. at 78; *see also* 19 Wright, Miller, Cooper, Federal Practice and Procedure § 4514, p. 451 (2 ed. 1996) (hereinafter, "Wright"). Since then, however, "it has become clear that this statement is not completely accurate[.]" Wright, § 4514.

Federal courts are competent to formulate federal common law rules of decision in several areas, including instances where it is necessary "to fill the interstices of a pervasively federal framework." Wright, § 4516, p. 500.

> The need for interstitial lawmaking arises as a consequence of the practical reality that it is impossible for Congress to draft any statute in sufficient detail so that it is completely comprehensive and comprehensible. Legislators, being human, are not capable of anticipating and providing the rules for every conceivable situation in which the statute subsequently will be applied in terms that are sufficiently well-defined to leave no need for judicial interpretation and elaboration. The power to generate federal common law under these circumstances thus "follows from the recognized futility of attempting all-complete statutory codes, and is apparent from the terms of the Constitution itself."

Wright, § 4516, pp. 500-01 (citations omitted).

The creation of a federal common law rule to fill gaps in a federal statutory framework reflects an effort to ascertain and implement congressional intent. This remedy has been used to fill in gaps in statutes where statutory terms are vague or where procedural rules were not provided. *See* Wright, § 4516, pp. 502-04 ("At one end of the continuum there is the simple necessity of filling in the interstices in a reasonably detailed federal statutory scheme – for example, by construing and applying vague statutory terms [and] supplying procedural rules that have been omitted from the statute[.]"); *In re KAR Development Assoc.*, 180 B.R. 597, 615-16 (Bankr. D. Kan. 1994) ("This category [of judicial decision] embraces situations in which Congress or the Constitution has not provided a rule of decision for the resolution of a federal question case that is properly within the subject matter jurisdiction of the federal courts. Concomitantly, congressional or constitutional intent can be inferred that the federal courts should supply the necessary rule of decision by pronouncing common law to fill the interstices of a pervasively federal framework.") (citing Wright et. al., *Federal Practice and Procedure*, § 4514, p. 223 (1982)); *Ellenbogen v. Rider Maintenance Corp.*, 794 F.2d 768 (2d Cir. 1986) (filling in a gap regarding statute of limitations); *Dunich v. Becton Dickinson & Co.*, 486 U.S. 196 (1988) (defining "final decision" for purposes of appeal).

To identify the appropriate remedy, a court should determine which of any potential remedial approaches is most compatible with the legislature's intent as

embodied in the statute being construed. *United States v. Booker*, 543 U.S. 220, 245 (2005) (finding two sections of statute unconstitutional and excising those two sections from statute as remedy rather than invalidating entire act because doing so was more consistent with what "Congress would have intended"); *see In re The Mortgage Store, Inc.*, 2011 WL 5056990, at *5-6 (considering congressional intent, consistent with *Booker* rule); *In re Coudert Bros. LLP*, 2011 WL 5593147, at *13 (considering congressional intent); *In re Refco Inc.*, No. 07-3060, 2011 WL 5974532, at *10 (finding analysis set out above consistent with *Booker* rule); *In re Soporex, Inc.*, 2011 WL 5911674, at *4 (inferring congressional intent in light of *Stern* ruling); *In re Univ. Marketing, Inc.*, 2011 WL 5553280, at *5 (analyzing congressional intent).

When confronted with a situation where a matter identified in 28 U.S.C. § 157(b)(2) cannot, consistent with constitutional limitations, be heard by a bankruptcy court as a "core" matter, bankruptcy courts can look to their authority to fashion a federal common law remedy to fill in any gaps in the statute. Admittedly, the statutory framework does not include a "savings clause" providing that, if a matter is improperly identified as "core," it should then be handled as a "non-core" matter so long as it fits within the scope of matters that are "related to" the bankruptcy case. Such provisions are uncommon in statutes.

The issue is whether the remedy proposed by *amici* herein is consistent with congressional intent. The answer to this question is a clear and resounding "Yes." The necessary breadth of bankruptcy *jurisdiction* is well-established. It is reasonable to infer that Congress intended for bankruptcy courts to be able to enter orders in all matters properly before them. Indeed, that is the *only* plausible inference. It is also reasonable to infer that Congress intended for "core" matters to be viewed as a subset of all matters permissibly before bankruptcy courts. Thus, it is reasonable to infer that Congress intended that all matters that cannot be permissibly heard as "core" matters be heard and ruled upon as "non-core," "related to" matters. Fashioning a limited federal common law procedural rule permitting bankruptcy courts to do so is consistent with congressional intent.

The Supreme Court recognized this result in *Stern*. By commenting that matters designated as "core" by Congress but which cannot be heard as "core" matters should be "removed" from core status and handled as non-core matters, the Court was both construing the statute and effectively creating a federal common law procedure or rule to fill in the gap perceived by the "dead zone" cases.

CONCLUSION

When viewed in context, alongside settled principles of statutory construction and federal jurisdiction, and in light of the Supreme Court's analysis in Stern, *amici* respectfully submit that the Bankruptcy Code requires matters that are identified in 28 U.S.C. § 157(b)(2) as "core" matters, but which cannot be heard and ruled upon as "core" matters consistent with constitutional limitations, are "non-core" matters for which bankruptcy courts may enter proposed findings of fact and conclusions of law subject to *de novo* review by the district courts. Alternatively, *amici* respectfully submit that federal common law provides a basis for implementing such a rule.

Respectfully submitted,

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CERTIFICATION OF COMPLIANCE

I hereby certify that the foregoing brief complies with the type-volume limitation provided in Rule 32(a)(7)(C)(i) of the Federal Rules of Appellate Procedure. The foregoing brief contains 6,993 words of Times New Roman (14 pt) proportional type. Microsoft Word is the word-processing software that was used to prepare the brief.

/s/ Paul D. Moore
Paul D. Moore