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H.R. 2533
CHAPTER 11 BANKRUPTCY VENUE REFORM ACT

Written Statement

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STATEMENT OF THE COMMERCIAL LAW LEAGUE OF AMERICA AND ITS BANKRUPTCY SECTION SUBMITTED AT THE HEARING ON THE SUBCOMMITTEE ON COURTS, COMMERCIAL AND ADMINISTRATIVE LAW OF THE COMMITTEE ON THE JUDICIARY OF THE UNITED STATES HOUSE OF REPRESENTATIVES

"Chapter 11 Bankruptcy Venue Reform Act of 2011"

September 8, 2011

I. INTRODUCTION

The Commercial Law League of America (the "CLLA"), has been in favor of venue reform for over 10 years. The CLLA, founded in 1895, is the nation's oldest organization of attorneys and other experts engaged in the field of commercial law, bankruptcy and reorganization. The CLLA's bankruptcy membership, which numbers over 500 professionals, includes attorneys from mid-size and small firms and bankruptcy judges representing virtually every state, and consists of representatives of divergent interests in bankruptcy cases. Although the CLLA has been traditionally associated with the representation of creditor interests, many of its attorneys represent debtors, trustees, and other parties in the bankruptcy process. Most importantly, its primary goal, when opining of legislative and related matters, is the fair, equitable and efficient administration of bankruptcy cases.

II. SUMMARY OF THE CLLA'S POSITION

The CLLA supports the "Chapter 11 Bankruptcy Venue Reform Act of 2011", recently introduced by Representatives Lamar Smith and John Conyers, Jr. (HR 2533) because it constructively attempts to rebalance the interests of all parties in bankruptcy by making sure that the bankruptcy reorganization process remains within the regions and communities that have the most significant vested interest in the outcome. This is achieved by proposing that a corporate debtor file only in districts where its principal place of business or principal assets has been located for at least one year prior to the commencement of the case, as well as placing other restrictions on "pending affiliate case" filings. The CLLA believes that if enacted, HR 2533 will significantly assist in the administration of bankruptcy cases throughout the country.

III. ANALYSIS

A. Statutory background.

28 U.S.C. §1408 provides:

> Except as provided in section 1410 of this title, a case under title 11 may be commenced in the district court for the district—
>
> **(1)** in which the domicile, residence, principal place of business in the United States, or principal assets in the United States, of the person or entity that is the subject of such case have been located for the one hundred and eighty days immediately preceding such commencement, or for a longer portion of such one-hundred-and-eighty-day period than the domicile, residence, or principal place of business, in the United States, or principal assets in the United States, of such person were located in any other district; or
>
> **(2)** in which there is pending a case under title 11 concerning such person's affiliate, general partner, or partnership.

It is generally accepted that the domicile for a corporation is its state of incorporation. *In re B.L. of Miami, Inc.*, 294 B.R. 325 (Bankr. D. Nev. 2003); *In re FRG, Inc.*, 107 B.R. 461, 471 (Bankr. S.D.N.Y. 1989), *citing Fourco Glass Co. v. Transmirra Products Corp.*, 353 U.S. 222, 226 (1957); *In re Segno Communications, Inc.*, 264 B.R. 501, 506 (Bankr. N.D. Ill. 2001) ("To determine the domicile of a corporation we look to the state of its incorporation.").

The initial choice of venue can be changed pursuant to 28 U.S.C. Section 1412 provides that: "A district court may transfer a case or proceeding under title 11 to a district court for another district, in the interest of justice or for the convenience of the parties." Unfortunately, this remedy is rarely used, and, even if attempted, it is not usually successful. The burden of proof for the change of venue is on the party seeking transfer and the "remote" jurisdiction has almost total discretion to decide whether or not to deny the motion. In the context of a large bankruptcy filing where the court is quickly deciding many important threshold issues at the commencement of a case and other actions that must be taken promptly (for example, cash collateral orders and the appointment of committees) it is extremely difficult to change venue. Accordingly, it has been reported that:

> The power to transfer a case or proceeding should be exercised cautiously." *Toxic Control Tech.*, 84 B.R. at 143; see Enron, 274 B.R. at 342 ("Transferring venue of

> a bankruptcy case is not to be taken lightly.") (*citing*, in turn, *Commonwealth of Puerto Rico v. Commonwealth Oil Ref. Co. (In re Commonwealth Oil Ref. Co.)*, 596 F.2d 1239, 1241 (5th Cir. 1979) ("CORCO ") ("the court should exercise its power to transfer cautiously"); In re Pavilion Place Assocs., 88 B.R. 32 (Bankr. S.D.N.Y. 1988) ("Transfer is a cumbersome disruption of the Chapter 11 process.")). Whether or not to grant a section 1412 motion to transfer venue of a case or proceeding under title 11 lies within the sound discretion of a bankruptcy court based on an "individualized, case-by-case analysis of convenience and fairness" factors. *Gulf States Exploration Co. v. Manville Forest Prod. Corp. (In re Manville Forest Prod. Corp.*), 896 F.2d 1384, 1391 (2d Cir.1990) (*quoting Stewart Org., Inc. v. Ricoh Corp.*, 487 U.S. 22, 29, 108 S.Ct. 2239, 101 L.Ed.2d 22 (1988) (quoting, in turn, *Van Dusen v. Barrack*, 376 U.S. 612, 622, 84 S.Ct. 805, 11 L.Ed.2d 945 (1964)). "A bankruptcy court's decision denying or transferring venue will only be reversed if the court's decision constitutes an abuse of discretion. *Enron*, 274 B.R. at 343.

(footnote omitted). *In re Enron*, 317 B.R. 629, 638 (Bankr. S.D.N.Y. 2004).

B. HR 2533 and local interests

The consequences of a corporate bankruptcy are most profound in the region and community in which the debtor's principal place of business or principal assets are located. ***Simply stated, bankruptcy is local***. Not only are there jobs involved, but also the local economy might depend to a large extent on business from that debtor. Many critical issues of local importance arise. The debtor may be, for example, one of the community's larger employers or it may sustain many small businesses that provide various goods and services. The consequences could extend even further, affecting the number of hospital beds that are available, the quality of elder care, or even waste removal. These are just a few of the countless local issues that might be engaged, and of course will require local subject matter expertise for example in real property, local taxes, environmental or health and safety issues, along with the treatment of real and personal security interests.

It has been our members' experience that bankruptcies filed in remote jurisdictions draw cases away from the parties with the most familiarity with the debtor's operations and who have an important stake in the case's outcome. For example, employees, local vendors and retirees will be unable to attend hearings without incurring insurmountable tome and travel expenses. There will also be little or no local media coverage on the progress of the debtor's efforts to reorganize and the development and interest in local groups and unofficial/official committees

will wane. Practitioners know that quite often, these interested parties will go down to the local bankruptcy court and meet other similarly-situated parties, share information and develop alliances and informal groups to protect their interests. Ultimately, these efforts might impact official or unofficial committees in the case, whether claims are successfully bought by third parties, or even have a direct impact on the provisions of the plan of reorganization. However, if the bankruptcy is pending in a remote location, these parties would not be able to take advantage of this type of informal networking and their contribution will be lost or minimized.

In summary, requiring that a corporate bankruptcy take place locally ensures that the distinct needs of the community are not overlooked or, worse, ignored by other groups residing hundreds, if not thousands, of miles away. HR 2533 insures the participation, input and information that local parties can provide to the debtor, other creditors and the courts, and enhances the overall bankruptcy process.

C. Examples of how bankruptcy venue impacts local interests.

(1) In re Pacific Gas and Electric Company, United States Bankruptcy Court, Northern District of California, Case No. 01-30923 – This bankruptcy, one of the largest utility bankruptcy cases ever to be filed ($35 billion in assets and approximately 20,000 employees), commenced in April 2001. Immediately, a small group of homebuilders began meeting and formed an informal committee ("MLX Committee") to address the treatment of claims, deposits and the assumption/rejection of main line extension contracts ("MLX Contracts") needed for the building of new subdivisions. The MLX Contracts were subject to a complicated set of state tariffs on file with the California Public Utilities Commission. The MLX Committee exchanged information, negotiated with the Debtor and cooperated in law and motion practice that resulted in the assumption of all MLX Contracts (50,000 contracts worth approximately $90 million) by December 2001. Without the local connections between the homebuilders, local lawyers and the Debtor, assumption and payment on the MLX Contracts would have been substantially delayed and possibly jeopardized. Please also note that this case, with the Honorable Dennis Montali presiding, resulted in a confirmed plan and a successful reorganized debtor after efficiently administered proceedings. This indicates that there are courts around the country who have jurists and staffs with the understanding, ability and skill to handle "mega-bankruptcy" cases.

(2) In re Astropower, Inc., United States Bankruptcy Court, District of Delaware, Case No. 04-10322. Plaintiff filed a preference action against one of its freight shippers for approximately $463,000. The Shipper had worked extensively with the Debtor for several years and continued working with them during the preference period (90 days preceding the filing) providing services during this time. In addition, by continuing to provide services to the Shipper, the Shipper had accrued substantial "new value" offsets against amounts claimed as preferential payments. At the time (and to some extent, this still is the case) Delaware law was more restrictive than most jurisdictions in how new value was calculated and therefore reduced the effect of the new value provided by the Shipper. The Shipper ultimately decided to settle the matter for $116,000 and avoid having to litigate the matter in Delaware. This situation is very common and an often repeated scenario for creditors, wherever a remote jurisdiction is involved.

(3) In re Integrated Telecom Express, Inc., 384 F.3d 108 (3d Cir. 2004). The Debtor elected to go out of business, even though it was highly solvent, solely to use the Bankruptcy Code (11 U.S.C. Section 502 (b)(6)) to reduce the landlord's rent claim by about $20 million, which would result in a surplus distribution to shareholders ($100 million instead of approximately $80 million). The Debtor had no contacts with Delaware except that was the state of incorporation. The Debtor developed equipment and software for broadband communications and was headquartered in San Jose, California. Most of its shareholders resided in Taiwan. The Debtor chose to file in Delaware because of favorable legal precedent sustaining debtors' filing in the face of a motion to dismiss for bad faith filing holding that a filing meets the good faith filing standard if the debtor files to take advantage of a particular provision of the Bankruptcy Code notwithstanding other circumstances. See, In re PPI Enteprises, Inc., 228 B.R. 339 (Bankr. D. Del. 1998, aff'd by, In re PPI Enteprises, Inc., 324 F.3d 197 (3rd Cir. 2003). The bankruptcy court in Delaware declined to dismiss the Debtor's case as a bad faith filing and refused to transfer venue to the Northern District of California. The District Court upheld the Court's decision but the Third Circuit reversed. The Third Circuit found that the case was not filed in good faith in that the Debtor was not in financial distress and did not preserve any special value for the creditors with the filing of the petition. Given the circumstances, taking advantage of the cap on the landlord's rent claim was not justification enough to establish "good faith" for the

bankruptcy, so the case was order dismissed. Had the landlord lacked the resources to persevere in the remote district, the dispute would have ended earlier in the Debtor's favor.

(4) In re Franklin Park Development I, Inc., United States Bankruptcy Court, District of Massachusetts, Case No. 86-10721. Bankruptcy Judge Lavien, presided over a housing project, primarily for lower income renters, comprising hundreds of units and perhaps over a thousand residents. The judge, along with the trustee, visited the property, and received significant local press coverage. His personal attention helped defuse a seriously emotionally charged situation. The delicate consideration of a local judge provided invaluable comfort to those affected and led Bankruptcy Judge Lavien to observe:

> So far, I've said nothing explicit about the conditions that I saw on the View of August 5th, because I still have trouble believing that as a nation, in 1986, we are concerned with an assortment of sophisticated national and international issues and, yet, still allow our fellow human beings to live in filth and substandard housing. Had the conditions of the Franklin Park Development been viewed in a third world country, they would have raised sympathetic outcries. *In re Franklin Park Development I, Inc.*, 64 B.R. 253, 255-256 (Bankr. D. Mass 1986).

(5) In re Solyndra LLC, United States Bankruptcy Court, District of Delaware, Case No. 11-12799. Recently filed bankruptcy case of a high profile solar-panel maker. Upon filing the California-based company suspended its manufacturing operations and laid off 1100 employees triggering both Federal and California Worker Adjustment and Retraining Notification Act ("WARN") issues. In addition, California Labor Code places significant duties on employers when its employees are laid off, especially with respect to salary and accrued benefits. Penalties for violations of these obligations may provide a basis for nondischargeability according to case law in the 9th Circuit. It is currently unclear how the Debtor's employees will fair in the remote jurisdiction on these issues.

(6) In re Perkins & Marie Callender's Inc., United States Bankruptcy Court, District of Delaware, Case No. 11-11795. At the commencement of the case the Debtor filed a motion to reject *nunc pro tunc* various nonresidential real property leases back to the petition date and in effect, eliminate any basis to claim administrative rent. One of the landlords involved in this group leases is a retiree who owns property in Colorado and leases restaurant space to the Debtor (the "Landlord"). The motion also allowed the Debtor to abandon all personal property and

surrender with no further conditions, leaving the landlord with the task to clean up the premises. If the bankruptcy case had been filed in a local bankruptcy court, the Landlord might have worked together with other landlords and negotiated better surrender terms with the Debtor. But due to the distance of the remote court and the time and expense involved in pursuing the matter, the Landlord had no choice but to accept the Debtor's terms.

D. Response to possible objections to HR 2533.

Opponents may advance various arguments for the status quo for bankruptcy venue. We have already addressed above the difficulties in presenting and prevailing on a motion for venue transfer under 28 U.S.C. Section 1412 and courts' ability to properly handle mega-cases.

In addition, others claim that special provisions contained in the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), first day orders, telephonic hearings and arrangements for *pro hac vice* counsel all together provide adequate protection for trade creditors' and employees' interests. To the contrary, these protections fall considerably short when addressing the bigger overall issue of bankruptcies filed in a remote venue located far away from local concerns. One example showing how these protections fall short is in the area of preference litigation. Contrary to the majority view found in decisions from other jurisdictions throughout the country, the new value exception provided for in 11 U.S.C. Section 547 (c)(4) must remain unpaid to qualify as a defense in some jurisdictions. This immediately puts preference defendants in these districts at a distinct disadvantage. Additionally, while employees are certainly interested in being paid on their priority wage claims, their input in negotiations concerning the long term survival of the debtor is even more important. Our point is that none of these technical protections adequately replace the benefits in having a local bankruptcy court reorganize a local company.

IV. CONCLUSION

Bankruptcy venue with its forum-shopping and judge-shopping implications has been the subject of much legal scholarship and debate. Reasonable minds can differ greatly on the subject. However, HR 2533 remedies the overly permissive venue provisions of 28 U.S.C.

Section 1408 and brings bankruptcy cases back to the communities most affected by the outcome, enhancing success, and providing effective administration.

Respectfully submitted,

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