Bankruptcy Venue Reform Bill Needs Amending

By **Kenneth Rosen and Philip Gross** (October 12, 2021, 3:29 PM EDT)

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The issue of venue reform has been debated for many years and is again being revisited in light of the expected surge in bankruptcy cases in the wake of the COVID-19 pandemic and certain recent large Chapter 11 filings, including Purdue Pharma LP and Mallinckrodt in the pharmaceutical space, Boy Scouts of America and USA Gymnastics in abuse-related cases, and Neiman Marcus Group, J.C. Penney Co. Inc., J. Crew Group Inc., Brooks Brothers, Century 21 and Modell's Sporting Goods in the retail space.

While some of these cases were filed in varied districts around the country, most of these cases — and, indeed, a large majority of large business bankruptcy cases[1] — were filed in so-called magnet bankruptcy districts, namely the District of Delaware, the Southern District of New York, the Eastern District of Virginia and the Southern District of Texas.

Indeed, particularly in connection with the recent Purdue Pharma case and third-party releases approved in that case by the bankruptcy court in New York, the issue of bankruptcy venue and forum shopping has again become a hot topic.

Members of Congress have called for investigations of Stamford, Connecticut-based Purdue Pharma's decision to file its bankruptcy case in White Plains, New York.[2]

Increased concerns that debtors are cherry-picking bankruptcy venues and judges to the detriment of the bankruptcy system have also prompted certain members of Congress to propose the Bankruptcy Venue Reform Act, preventing debtors from doing this by limiting them to filing only in places where debtor's headquarters or principal assets are located.

However, that proposed legislation is not a panacea. The act and a recent article supporting it and criticizing the current venue rules ignore (1) the current ability of parties to seek to change venue; (2) the often complex corporate structure of large companies with scores of entities located in multiple jurisdictions around the U.S., or even the globe; and (3) the fact that many bankruptcy cases are unique in our legal system as most cases are not just a typical two-party dispute where regular nonbankruptcy venue rules make sense.

Below, we propose a compromise solution that seeks to balance the concerns of the proponents and opponents of the current bankruptcy venue law. Specifically, while recognizing that there are certain types of debtor companies where the current bankruptcy venue rules are appropriate, the proposed compromise suggests situations, including those based on the nature or character of certain companies and the particularly strong effect of a bankruptcy filing on the local community, where changes to the current bankruptcy venue rules make sense.

The Bankruptcy Venue Reform Act of 2021

On June 28, the Bankruptcy Venue Reform Act was introduced on a bipartisan basis by Rep. Zoe Lofgren, D-Calif., and Rep. Ken Buck, R-Colo.[3] The act proposes that a potential debtor commence its bankruptcy case only in a venue where the debtor's headquarters or principal assets are located. This is in contrast to the current bankruptcy venue statute,[4] which also allows for bankruptcy venue in a jurisdiction where the debtor is domiciled, i.e. the state of incorporation for a corporate debtor.

The act was introduced in the Senate by Sen. Elizabeth Warren, D-Mass.

In an article entitled "Now Is The Time For Bankruptcy Venue Reform" published on The Hill on Aug. 6 in support of the act, retired bankruptcy judges Joan Feeney and Steven Rhodes and professors Jay Westbrook and Adam Levitin argue that a frequently used bankruptcy law loophole enables companies to pick the court, the applicable case law, and sometimes even the judge who will hear their Chapter 11 cases.[5]

They further argue said that these "runaway cases" create opportunities for unjust results allegedly "tucked away" from the careful scrutiny of those most concerned and that bankruptcy judges around the country can and should handle all types of bankruptcy cases.[6]

Additionally, they claim that debtors and their advisers often choose bankruptcy filing locations far away from a company's corporate headquarters, making it difficult for creditors, employees, retirees and the local media to observe and participate in the case. They conclude that debtors should be required to file cases where their headquarters or principal assets are located.[7]

Concerns With Proposed Venue Reform

The bases for venue reform offered by the professors and former bankruptcy judges can be challenged for several reasons.

First, large creditors, particularly unions and creditors' committees, have the express ability to seek to change venue if they believe another venue is more appropriate or in the interests of justice.[8]

Second, while the Hill article claims that filing bankruptcy in a venue far away from headquarters makes it difficult for certain creditors, employees, retirees and the home-town media to be involved in a case, the truth about large national and multinational corporations in many situations belies this assertion, particularly with regard to mega Chapter 11 cases. The companies typically commencing such so-called mega cases often have highly complex corporate structures with scores of entities located in multiple jurisdictions around the U.S. or even globally.

To give one example: the article mentions that while the Chicago Tribune "proudly bear[s] the name" of the city where it is based, this newspaper somehow improperly filed for Chapter 11 bankruptcy in Delaware, thereby "taking advantage of a loophole in bankruptcy law."[9]

However, this does not take into account that the Chicago Tribune was part of a media conglomerate, the Tribune Co., consisting of 111 debtor entities, including publishing, broadcast and entertainment segments that operated, among other things, eight major-market daily newspapers — in cities such as Los Angeles, Orlando, Hartford and London — and 23 television stations in 19 markets.[10] The Tribune Co. was incorporated in Delaware,

and had creditors, employees and operations around the country and world. Why is Wilmington, Delaware, any less fair a jurisdiction for such a filing than Chicago?

Third, companies incorporate in places like New York and Delaware to take advantage of a large body of established corporate law in these jurisdictions, and courts in those jurisdictions are well-versed in applying the laws in the jurisdiction in which they sit. Moreover, creditors doing business with these large corporations very often are not located in the same locale as corporate headquarters and bankruptcy lawyers involved in the case choose these specific jurisdictions not necessarily because the judges are more debtor- or creditor-friendly but because these jurisdictions have local rules in place for complex Chapter 11 bankruptcy proceedings.

Finally, the bankruptcy venue statute recognizes that bankruptcy is unique in the litigation world. While at times, a bankruptcy filing is precipitated by a two-party dispute, more often, it is not about a two-party dispute that cleanly or neatly follow venue rules. Rather, a company facing cash-flow issues or other industry headwinds is looking to clean up its balance sheet and restructure obligations owed to its noteholders; secured lenders — who reside around the world and whose agent is based in Delaware or New York; union employees — who often reside in different states, even for smaller or middle-market corporations; governmental entities in multiple jurisdictions; landlords — typically around the country; and other parties.

Like prior efforts at venue reform, the act will inevitably be met with strong opposition.[11] The chair of the House Judiciary Committee is Rep. Jerrold Nadler, D-N.Y.,[12] and any bill would need to be signed by President Joe Biden, previously the senator from Delaware and, historically, a strong supporter of the current bankruptcy venue rules that authorize a corporate debtor to file in the jurisdiction of incorporation.[13]

We disagree with the frequent argument made against venue reform that keeping mega cases in certain districts is justified because the judges in those districts are experienced in managing large cases.[14] That argument incorrectly assumes that the judges in other districts cannot navigate a large case — they certainly can and do.

Furthermore, any bankruptcy judge is going to be capable of navigating mega cases after getting experience in such matters. In fact, even in the popular districts, newly appointed judges learn how to manage mega cases and become seasoned in such cases after handling one or two.

Proposed Compromise on Bankruptcy Venue Reform

With the prospect of a rewrite of the venue statute highly charged and frequently debated and challenged, is a compromise on bankruptcy venue possible?

We believe that there are certain cases and situations where it is appropriate that venue should be specific to a location. Further, even ardent opponents of the act should agree that the following represents a reasonable compromise. For supporters of the act, the following suggestions cure many problems with the current venue rules but also recognize that we live in a very different economy than in the past and there are certain situations where the current bankruptcy venue rules should remain in place.

Venue of Chapter 9 cases is already covered in the current venue rules. In other cases, the instances where venue is to be limited may be in the form of an amendment to the proposed act setting forth criteria for a judge to weigh when considering a venue transfer,

including the following.

Single-asset real estate cases must be commenced in the jurisdiction where the property is located.

In cases where collective bargaining agreements or retiree benefit obligations are anticipated to be rejected or modified by order of the bankruptcy court pursuant to Sections 1113 or 1114 of the Bankruptcy Code, the case must be commenced in a jurisdiction where the debtor has its principal headquarters or where the debtor or its affiliates has a place of business at which its unionized employees are — or were, in the case of retirees — employed.

Where the debtor has commenced a Chapter 11 case within the previous four years, the case has been closed and thereafter the debtor commences a new Chapter 11 case, the new case must be commenced in the jurisdiction where the previous case was commenced.

If more than two-thirds of the debtor's employees are employed by the debtor in a single location, the debtor must commence its Chapter 11 case in the jurisdiction of its principal headquarters or else in the jurisdiction where more than two-thirds of its employees are employed by the debtor. If the debtor and its affiliates do not have one location where more than two-thirds of employees are employed, then the debtor can file based on the current venue rules — including based on state of incorporation.

Where more than two-thirds of a debtor's or its affiliates' revenues derive from manufacturing, refining, rendering services, assembly of goods or distribution of goods at a single facility operated by the debtor, the debtor's Chapter 11 case must be commenced in the jurisdiction in which that facility is located or else the jurisdiction where the debtor's principal headquarters are located.

Not-for-profit firms must commence Chapter 11 cases in the jurisdiction where the debtor's principal headquarters are located.

Chapter 11 cases for the following types of debtor companies — because the bulk of the debtor's employees are local, the effect of the debtor's business on the local economy is substantial or the debtor is an especially important part of the local community — must be commenced in the jurisdiction of the debtor's principal place of business — i.e. where the relevant operating facility or business is located — provided that if the debtor owns or operates more than one operating facility or operating business location, then the case may be commenced in any jurisdiction in which any facility or operating business is located, or the jurisdiction in which the debtor's headquarters are located, as proposed in the act:

- Health care facilities;
- Mining, farming operation or family fisherman companies;
- Railroad companies;
- Hospitality facilities, i.e. hotels, amusement parks, ski areas, water parks, clubs and other recreational centers; and
- Casinos.

Our goal is to solve as many of the alleged problems that currently exist with choice of venue in a way that is sufficiently politically palatable to become law. While our proposals may not be perfect, we believe that they are a good starting point at providing a compromise framework for those on both sides of the venue dispute.

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[1] According to Bloomberg Law, three bankruptcy judges heard 57% of all large public company Chapter 11 cases in 2020. See Alex Wolf, Purdue Pharma Bankruptcy Spotlights Venue Shopping Battle, Bloomberg Law, https://news.bloomberglaw.com/bankruptcy-law/purdue-pharma-bankruptcy-spotlights-court-venue-shopping-battle.

[2] See Katie Adams, Senator Raises Concerns about Purdue Pharma's Bankruptcy Court Location, Becker's Hospital Review, https://www.beckershospitalreview.com/opioids/senator-raises-concerns-about-purdue-pharma-s-bankruptcy-court-location.html.

[3] H.R. 4193.

[4] 28 U.S.C. § 1408.

[5] See Joan Feeney, Adam Levitin, Steven Rhodes and Jay Westbrook, Now is the Time for Bankruptcy Venue Reform, The Hill (Aug. 6, 2021), available at https://thehill.com/blogs/congress-blog/judicial/566729-now-is-the-time-for-bankruptcy-venue-reform.

[6] Id.

[7] Id.

[8] See, e.g., In re Patriot Coal Corporation, Case No. 12-12900 (SCC), 2012 WL 5934334 (Bankr. S.D.N.Y. Nov. 27, 2012) (transferring venue of chapter 11 cases of Patriot Coal and affiliated debtors from New York to Missouri, the state in which Patriot's corporate headquarters was located; venue was only proper in New York based on the formation of two subsidiaries of Patriot Coal in New York on the eve of the bankruptcy filing); Nick Brown, Patriot Coal Bankruptcy Moved to Court in Missouri, Reuters, available at https://www.reuters.com/article/us-patriot/patriot-coal-bankruptcy-moved-to-court-in-missouri-idUSBRE8AQ1BV20121127; In re Municipal Corrections LLC, Case No. 12-12253-mkn (Bankr. D. Nev. Dec. 28, 2012) (transferring venue from Nevada, state of incorporation of debtor, to Georgia, based on the location of the business and primary creditors), available at https://www.ianb.uscourts.gov/sites/ianb/files/opinions/MunicipalCorrections.pdf.

[9] See Hill Article.

[10] See In re Tribune Company, et al., Case No. 08-13141, Affidavit of Chandler Bigelow, III, Senior Vice President and Chief Financial Officer of Tribune Company in Support of First Day Motions (Bankr. D. Del. Dec. 8, 2008), available at https://document.epiq11.com/document/getdocumentsbydocket/?docketId=163464&projectCode=TRB&docketNumber=3&source=DM.

[11] See, e.g., Governor Carney, Congressional Delegation Respond to Bill that would Hurt U.S. Economy, Change Bankruptcy Venue Laws, available at https://news.delaware.gov/2018/01/08/venue-options-bill/ (opposing the Bankruptcy Venue Reform Act of 2018 introduced by Sen. John Cornyn (R) and Sen. Elizabeth Warren (D)).

[12] The New York legal community has historically opposed bankruptcy venue reform. See, e.g., New York City Bar, Report Opposing the Bankruptcy Venue Reform Act of 2018, available at https://www.nycbar.org/member-and-career-services/committees/reports-listing/reports/detail/report-opposing-the-bankruptcy-venue-reform-act-of-2018.

[13] See Gary M. Freedman, Bankruptcy Venue — Between a Rock and a Hard Place, available at https://www.nelsonmullins.com/idea_exchange/blogs/the_bankruptcy_protector/other-issues-affecting-bankruptcy-cases/bankruptcy-venue-between-a-rock-and-a-hard-place.

[14] See, e.g., Governor Carney, Congressional Delegation Respond to Bill that would Hurt U.S. Economy, Change Bankruptcy Venue Laws, available at https://news.delaware.gov/2018/01/08/venue-options-bill/ (arguing that "the bankruptcy judges in Delaware are experienced in handling these difficult restructuring cases.").