



# CLLA LEGISLATIVE DAY

October 4, 2022

## **BANKRUPTCY VENUE REFORM** **H.R. 4193 and S. 2827**

### 1. **PROPOSAL**

In June, 2021, Representatives Zoe Lofgren (D-CA) and Ken Buck (R-CO) introduced HR 4193, followed by S 2827 in September, 2021, by Senators John Cornyn (R-TX) and Elizabeth Warren (D-MA) – bipartisan bills to amend the venue provisions in the US Bankruptcy Code. Both bills propose to eliminate the state of incorporation of the debtor as a basis for venue in commencing a business Chapter 11 case, providing instead for venue in the debtor's principal place of business, where its principal assets are located or where an affiliated entity had previously filed (as long as the parent entity filed first). We are looking for additional co-sponsors. Copies of both bills can be found at <https://www.congress.gov/117/bills/hr4193/BILLS-117hr4193ih.pdf> and <https://www.congress.gov/117/bills/s2827/BILLS-117s2827is.pdf>

### 2. **THE PROBLEM**

The root problem of the bankruptcy venue crisis stems from the growing concentration of large business cases being filed in a handful of courts by utilizing the current permissive venue provisions of 28 USC Section 1408. For example, in 2020, three bankruptcy judges, out of a total of 375 judges nationwide, heard 57% of all large commercial cases.<sup>1</sup> And even more troubling, is the growing trend of weaponizing Chapter 11 to limit claims and damages from mass tort victims. Cases like *Purdue Pharma* (opioids) and *LTL Management (Johnson & Johnson talc cases)* are "poster children" to this increasing use of the Chapter 11 bankruptcy process. The ability of debtors and their professionals to manipulate laws and choose their own venue to achieve a desired outcome directly threatens the integrity of the bankruptcy system and erodes public confidence. Attached is a *Bloomberg* on how forum shopping impacted the *Purdue Pharma* bankruptcy case.

The National Association of Attorneys General recognized this problem and in November

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<sup>1</sup> Oversight of the Bankruptcy Code, Part 1: Confronting Abuses of the Chapter 11 System: Hearings before the Subcommittee on Antitrust, Commercial, and Administrative Law, of the House Judiciary Committee, 117th Cong. (2021) (written testimony of Adam Levitin): <https://docs.house.gov/meetings/JU/JU05/20210728/113996/HHRG-117-JU05-Wstate-LevitinA-20210728.pdf>



2021, issued a comprehensive letter signed by 43 Attorneys General endorsing support for HR 4193 and S 2827. That letter notes that debtors have increasingly taken taking more and more advantage of the generous venue statute provided in the Bankruptcy Code, resulting in "unnatural" venue selections and limiting the development of bankruptcy jurisprudence to a handful of courts. The AGs, who are specifically charged with protecting their states' and citizens' financial interests, insuring the enforcement of consumer protection laws, and protecting the environment from pollution, believe that having bankruptcy cases resolved in distant forums away from where the debtor operates is not good public policy.<sup>2</sup>

### **3. THE HUMAN TOLL AND IMPACT OF FORUM SHOPPING**

On February 8, 2022 the Senate Judiciary's Subcommittee on Federal Courts, Oversight, Agency Action and Federal Rights held a hearing entitled "*Abusing Chapter 11: Corporate Efforts to Side-Step Accountability through Bankruptcy*".<sup>3</sup> The panel consisted of former bankruptcy judge, a law professor, practitioners and a single mother who had been diagnosed with terminal cancer caused by the use of *Johnson & Johnson's* talcum powder. The hearing focused on the novel bankruptcy development of using a divisive merger to separate the talc tort claims against *Johnson & Johnson* into a new corporation (*LTL Management*) apart from all the assets and business producing liabilities in another corporation (*Johnson & Johnson*) and then seek court approval of a plan of reorganization for *LTL Management* to the disadvantage of injured victims. The Senators at the hearing were clearly taken aback by debtor's counsel's aggressive tactics and the panelists noted how such an approach violated some fundamental principles of law: namely, that debts are typically discharged in bankruptcy because all assets of the debtor are available to pay creditors claims, that tort victims will get their day in court and will be fairly compensated for their injuries, and that forum shopping is not encouraged or awarded by the legal system. It was noted that the pending venue reform legislation (HR 4193 and S 2827) could provide solutions to these problems.

### **4. THE SOLUTION**

For the reasons stated above, the Commercial Law League of America supports venue reform and the passage of HR 4193 and S 2827 as a reasonable solution to ensuring that Chapter 11 bankruptcy cases are filed in the venue in which the debtor operates and its assets are located, and where the creditors most likely to have an interest in the bankruptcy case can actively participate without having to travel to or retain counsel in a distant venue.

For further information, please contact:  
Peter C. Califano, Esq., (415) 882-5300 or [pcalifano@nvlawllp.com](mailto:pcalifano@nvlawllp.com)

<sup>2</sup> See, a copy of the NAAG letter at <https://www.naag.org/policy-letter/naag-endorses-bankruptcy-venue-reform-act-of-2021/>

<sup>3</sup> See, <https://www.judiciary.senate.gov/meetings/abusing-chapter-11-corporate-efforts-to-side-step-accountability-through-bankruptcy>

Purdue Pharma Bankruptcy Spotlights Venue Shopping Battle (1)

Bankruptcy Law

# Purdue Pharma Bankruptcy Spotlights Venue Shopping Battle (1)

By Alex Wolf

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- Change advocates point to perception of preordained outcomes
  - OxyContin maker secured a perceived debtor-friendly judge
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Purdue Pharma LP's seeming ability to handpick its bankruptcy case judge has renewed discussions over a fight to stop large companies from forum shopping.

The issue recently has become harder to ignore, as Purdue, the National Rifle Association, the Boy Scouts of America, and other large organizations maneuver to get the court—and the judge—that they believe will most benefit them, without regard to their base of operations.

A recently introduced House bill (H.R. 4193) would require Chapter 11 proceedings to take place at the location of the debtor's principal place of business or main assets.

"The bankruptcy system is supposed to work for everyone, but in many cases it works only for the powerful," House Judiciary Committee Chairman Jerrold Nadler (D-N.Y.) said during a July 28 hearing on corporate abuse of bankruptcy law. "And too often it works best for big corporations and the very wealthy who have not even filed for bankruptcy."

Judges' predilections and where proceedings are held can have large ramifications for bankruptcy plan payouts. Once largely considered to be an esoteric legal strategy affecting deep-pocket creditors, the forum-shopping issue also has had profound effects on recent cases with large bases of working- and middle-class claimants, such as the Boy Scouts of America.

Three bankruptcy judges out of 375 heard 57% of all large public company Chapter 11 cases in 2020, David Lieberman of Webster, Chamberlain & Bean LLP said, citing research by Georgetown Law professor Adam Levitin.

The Boy Scouts, which filed in Delaware, is based in Texas. The NRA filed for bankruptcy in Texas despite being headquartered in Virginia and incorporated in New York.

"There are several high-profile cases that highlight the question in a way that's more salient to the public," said University of Chicago Law School professor Anthony Casey.

Distressed companies with savvy bankruptcy lawyers are steering cases to courts known for approving certain pro-debtor requests, and with little regard for the venues' proximity to creditors, forum shopping critics say. The process also alienates employees and consumers from the restructuring process, they say.

Others defend the practice as a way to ensure predictability and a judge with the right experience. Companies benefit from having their proceedings heard in sophisticated bankruptcy jurisdictions, Casey said.

Remote hearings that became pervasive during the Covid pandemic also have stirred conversations on whether court locations matter at all.

Forum shopping also avoids undue influence from local politicians in situations where a case affects their constituencies, Casey said.

### **Manufacturing Jurisdiction**

Nearly two decades of legislative efforts in both chambers of Congress have failed to gain much traction. Venue shopping became more pronounced after the 2008 recession pushed major companies to seek refuge in two of the busiest bankruptcy courts—the U.S. Bankruptcy Court for the Southern District of New York, and the U.S. Bankruptcy Court for the District of Delaware.

Both courts are known for efficient and predictable handling of major business reorganizations. More recently, the U.S. Bankruptcy Court for the Southern District of Texas and the U.S. Bankruptcy Court for the Eastern District of Virginia have developed similar reputations.

"You can sort of manufacture jurisdiction by making sure you have an entity in the district you want to file in," McGuireWoods LLP attorney Douglas Foley said. "Big firms that file cases have some certainty as to which judge they're going to get and what types of rulings they're going to get."

People had lots of "innocent explanations" for companies gravitating toward Delaware and Manhattan, said Lynn LoPucki, a bankruptcy scholar at UCLA School of Law.

But a recent shift of major cases to venues with only one or two judges—like Richmond, Va., Houston, and White Plains, N.Y.—has changed the debate, according to LoPucki, who manages a database of large, publicly traded companies' bankruptcies.

Those judges "are giving the people who bring them the cases whatever they want," he said.

### **White Plains Judge**

Stamford, Connecticut-based Purdue filed its case in the Southern District of New York's White Plains location, ensuring that proceedings ended up with Judge Robert Drain, the only jurist at the suburban courthouse who hears corporate bankruptcies.

The company filed bankruptcy just six months after changing the corporate address for one of its units to White Plains.

Purdue could have filed Chapter 11 in Connecticut, or even Manhattan, part of the same district as White Plains and featuring a much larger bench of experienced judges.

The company said in a statement that its White Plains entity, Purdue Pharma Inc., has been in New York state since it was incorporated in 1990. "White Plains is about 15 miles from our corporate headquarters and is the closest federal Bankruptcy courthouse," it said.

Drain has a debtor-friendly reputation, and the company and its owners are trying to protect their assets, Lieberman said.

"It's hard to sort of turn a blind eye and not realize what's happening to try to get Judge Drain," Foley said. "People file in White Plains because they know they're going to get him."

The OxyContin manufacturer now is on the verge of court approval for its plan to settle the legal claims of addiction victims, state governments, and municipal entities that have borne the brunt of the U.S. opioid crisis. The plan would release the controlling family—the Sacklers—from future opioid-related lawsuits in exchange for their contribution of roughly \$4.2 billion to a larger settlement fund.

"I just hope that these higher profile cases will get someone's attention," Elissa Miller of SulmeyerKupetz said, referring to legislative activity brewing on the issue.

### Changing Calculus

The House bill, if passed, could go a long way to appease venue-shopping critics and limit cases like Purdue's.

Reps. Zoe Lofgren (D-Calif.) and Ken Buck (R-Colo.), who introduced the bill, said it will "ensure the case is heard in a court familiar with all the affected stakeholders."

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Versions of the measure have been revived at various times since the early 2000s, but has never picked up enough steam to get a floor vote.

But Purdue's bankruptcy and the public outrage the case has generated "changed the calculus," Lieberman said.

—With assistance from Claire Hao

(July 30 story updated to include an additional source of bankruptcy case statistics.)

To contact the reporter on this story: Alex Wolf in New York at [awolf@bloomberglaw.com](mailto:awolf@bloomberglaw.com)

To contact the editors responsible for this story: Laura D. Francis at [lfrancis@bloomberglaw.com](mailto:lfrancis@bloomberglaw.com); Roger Yu at [ryu@bloomberglaw.com](mailto:ryu@bloomberglaw.com)

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Purdue Pharma LP

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