CLLA HILL DAY

March 2-3, 2015

THE BANKRUPTCY VENUE CRISIS

1) BACKGROUND

Forum shopping in bankruptcy has reached epidemic levels. A recent study shows that 70 percent of public companies have filed their chapter 11 cases in venues outside of the district where their principal place of business or principal assets are located. Eighty percent of those companies filed in the District of Delaware or the Southern District of New York. In total, between 2004 and 2012, research indicates that 559 Chapter 11 bankruptcy cases were filed in the District of Delaware and another 104 Chapter 11 bankruptcy cases were filed in the Southern District of New York involving business debtors headquartered in a different state. These cases involved approximately $2 trillion in debt, 4.5 million creditors and more than 2 million employees, all administered by courts having no meaningful connection with the subject debtors. This trend is not limited to large public companies. Almost half of the Delaware cases involved smaller businesses with less than $15 million in assets at the time of filing. The full report of the research and findings, along with other articles on venue reform can be found at:

http://www.clla.org/resources/venue_reform.cfm

2) CONSEQUENCES

The growing frequency of forum shopping by debtors and other interests are having a serious and debilitating impact on the practice of bankruptcy law. Indeed, Judge Rhodes recently published an opinion piece in the *Wall Street Journal* calling the current bankruptcy venue law "the single most significant source of injustice in chapter 11 bankruptcy cases."[1]

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[1] Judge Rhodes' article is attached as Exhibit A.

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a) Venue Manipulation Threatens the Legitimacy of the Bankruptcy System

Seven out of every ten public companies that file chapter 11 file outside of their home states. A disproportionate number of large and middle market companies file in Delaware or the SDNY in search of desired outcomes at the expense of trade creditors, employees and other constituents. By allowing debtors to choose where to reorganize, the system appears to be manipulable in favor or corporate and large-moneyed interests. In the *Patriot Coal* case it was noted by the press that "Lenders and lawyers who get the big cases like taking their troubles to courts in New York and Delaware, which are convenient to their homes and offices and attuned to their concerns". Rampant forum shopping directly threatens the integrity of the bankruptcy system by eroding public confidence and calling into question the fairness of a system that can be so easily manipulated.

b) Venue Shopping Disenfranchises Creditors, Employees and Others

In 1997 the *Bankruptcy Review Commission* issued findings for improving the practice of bankruptcy for the coming 20 years and noted that by allowing debtors the ability to file Chapter 11 cases in remote jurisdictions, local constituents were in effect being deprived of their due process. By concentrating cases in two districts smaller creditors, employees, retirees and other local parties with an interest in the bankruptcy case had no effective way to actively participate in the process. The situation has continued to deteriorate over time. The result is a growing level of indifference and distrust among creditor, employee and retiree constituents unable to participate actively in a process that directly affects their interests. The concentration of cases in two venues exacerbates the impact of forum shopping on these smaller constituents by tilting the playing field toward financially sophisticated parties who regularly appear in those courts.

c) Centralization of Cases Impairs the Balanced Development of Bankruptcy Law

The concentration of business filings in Delaware and SDNY has had the unintended consequences of creating two "super courts" with a duopoly on Chapter 11 jurisprudence. Other bankruptcy courts lose the ability to provide their input into the development of a rich body of experience and case law interpreting the Bankruptcy Code, with related federal appellate courts developing a consensus of controlling precedent. In addition, there is no assurance that the decisions by the duopoly are appropriate for all 94 federal districts or are even the proper interpretations. Absent the benefit of points of view from other courts, these decisions may be left unchallenged and are in fact strengthened by repeated application over time by cases filed in the same district before

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the same judges. This is not what the Framers intended when they contemplated the development of a uniform bankruptcy law.

3) SUGGESTED ACTION

a) First, the CLLA encourages that the United States Trustee's Office undertake a more active role in the forum selection of chapter 11 cases, especially those filed in Delaware and in the SDNY by out of state companies. When appropriate, the UST should initiate and/or support motions to transfer venue pursuant to 28 U.S.C. Section 1412.

b) Second, the CLLA requests that the UST assist in the development and enactment of appropriate bankruptcy venue reform legislation.[2]

c) Third, the CLLA recommends that the UST help to insure that there is adequate statistical recording keeping and analysis as it pertains to venue and transfer issues, in order to better monitor the status and impact of the venue issue on the practice of bankruptcy law and the administration of the bankruptcy system.

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[2] Proposed changes to the bankruptcy venue statute are attached as Exhibit B.