No. 12-1200

In the Supreme Court of the United States

EXECUTIVE BENEFITS INSURANCE AGENCY,
PETITIONER,

v.

PETER H. ARKISON, TRUSTEE, SOLELY IN HIS CAPACITY AS CHAPTER 7 TRUSTEE OF THE ESTATE OF BELLINGHAM INSURANCE AGENCY, INC.,
RESPONDENT.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF OF THE ROBERT R. MCCORMICK FOUNDATION AND THE CANTIGNY FOUNDATION AS *AMICI CURIAE* SUPPORTING THE PETITIONER

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INTEREST OF *AMICI CURIAE*[1]

Amicus curiae The Robert R. McCormick Foundation (the "McCormick Foundation") is one of the nation's largest philanthropic organizations. Formed originally as a charitable trust following the death of Colonel McCormick in 1955, the McCormick Foundation has awarded grants totaling more than $1 billion to support programs promoting early childhood education and care, civic learning and engagement, veterans training and employment, and other salutary goals. *Amicus curiae* Cantigny Foundation is a charitable organization that serves as the steward of Cantigny Park, a 500-acre park, and maintains and manages the Cantigny First (Infantry) Division Museum and the Robert R. McCormick Museum.

The McCormick Foundation and Cantigny Foundation (together, the "Foundations"), are among more than three thousand former public shareholders of Tribune Company ("Tribune") who have been sued by creditors of Tribune to avoid, as fraudulent transfers, payments totaling approximately $8 billion that Tribune made to shareholders to effectuate Tribune's leveraged buyout in 2007. The Foundations are named as

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[1] Pursuant to this Court's Rule 37.3(a), all parties have consented to the filing of this brief. Letters evidencing such consent have been filed with the Clerk of the Court.

Pursuant to Rule 37.6, *amici curiae* affirm that no counsel for any party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than the *amici curiae* or their counsel made a monetary contribution to its preparation or submission.

defendants in three of 54 such lawsuits, all of which have been consolidated for coordinated pretrial proceedings in the Southern District of New York ("Tribune LBO Litigation").[2] The Foundations were among the largest shareholders of Tribune and have a commensurate stake in the outcome of the Tribune LBO Litigation. *In re Tribune Company Fraudulent Conveyance Litigation*, No. 11 MD 2296, No. 12 MC 2296 (S.D.N.Y.) (Sullivan, R.).

The case before this Court involves only two parties and modest sums. This Court's decision, however, may impact the Tribune LBO litigation, which, as noted, involves billions of dollars paid to thousands of public shareholders six years ago, and other massive and complex fraudulent transfer litigation, now pending in the bankruptcy court in the Southern District of New York. *Weisfelner v.*

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[2] One of the three suits, *Kirschner v. FitzSimons, et al.*, No. 12 CV 2652 (S.D.N.Y.), was originally brought as an adversary proceeding by the Official Committee of Unsecured Creditors of Tribune Company in the Bankruptcy Court for the District of Delaware, where Tribune's chapter 11 bankruptcy case was brought. That case is now being prosecuted by the trustee of a litigation trust formed under Tribune's confirmed plan of reorganization. The plaintiffs in the other two cases, *Deutsche Bank Trust Company Americas v. Olson Enters.*, No. 11-03754 (N.D. Ill.) and *Niese v. ABN AMRO*, No. 2011 L 005723 (Ill. Cir. Ct. Cook Cnty.), are groups of Tribune note holders and retirees, respectively, who in 2011 brought dozens of lawsuits against Tribune shareholders in a variety of state and federal courts across the nation. The state court cases were removed to U.S. district court, chiefly pursuant to 28 U.S.C. § 1334, and all of the cases, state and federal, were then transferred to the Southern District of New York for consolidated pretrial proceedings pursuant to 28 U.S.C. § 1407. *In re Tribune Company Fraudulent Conveyance Litigation*, No. 11 MC 2296, No. 12 MC 2296 (S.D.N.Y.) (Sullivan, J.).

Morgan Stanley & Co. (In re Lyondell Chemical Co.), Adv. Pro. No. 10-04609 (Bankr. S.D.N.Y.). The Foundations believe that all aspects of the case before this Court should be determined in the U.S. district court. The bankruptcy court has no proper role to play in this litigation.

It is of grave interest to the Foundations and others similarly interested that their cases be resolved in a manner and in a forum that raise no issues of constitutional or congressional authorization or competence.

SUMMARY OF ARGUMENT

The Bankruptcy Code does not authorize a bankruptcy judge to submit proposed findings of fact and conclusions of law to a district judge for final decision in a core proceeding. Proposed findings and conclusions are allowed only in non-core matters. Here, the Ninth Circuit incorrectly construed the Bankruptcy Code's allocation of power to a bankruptcy judge to "hear and determine" core proceedings as encompassing the power to issue proposed findings and conclusions. The Ninth Circuit's decision cannot be squared with the plain language of the Bankruptcy Code, which starkly distinguishes the role of bankruptcy judges in core and non-core matters and carefully allocates the responsibility of district judges and bankruptcy judges in each. Whether bankruptcy judges are to play a role in core matters that must be adjudicated in the district court, implicates important policy choices that are for Congress, not the courts, to make that determination. District judges, with the assistance of magistrate judges as necessary, are

perfectly well-qualified to preside over core proceedings, as they do in a large variety of other complex matters. The involvement of bankruptcy judges in core proceedings pending before district judges would disserve the interests of sound judicial administration because it would add delay, expense and confusion to the proceeding with no offsetting benefit in the fairness or accuracy of the result.

ARGUMENT

I. A Bankruptcy Judge Has No Statutory Authority To Submit Proposed Findings And Conclusions In An Action By A Bankruptcy Trustee To Avoid Alleged Fraudulent Transfers To Non-Creditors.

Actions by a bankruptcy trustee to avoid alleged fraudulent transfers to a non-creditor implicate private, not public, rights. *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989). Such actions are "quintessentially suits at common law that more nearly resemble state-law contract claims brought by a bankrupt corporation to augment the bankruptcy estate than they do creditors' hierarchically ordered claims to a pro rata share of the bankruptcy res." *Id.* at 56.

Because an avoidance action by a bankruptcy trustee against a non-creditor is an action to enforce a private right, it is subject to two constitutional limitations. First, the case must be adjudicated in an Article III court, by a judge with lifetime tenure whose salary Congress may not diminish. *Stern v. Marshall*, 131 S.Ct. 2594, 2611-14 (2011); *Granfinanciera*, 492 U.S. at 51. Second, the

non-creditor defendant is entitled to a jury trial under the Seventh Amendment. These constitutional consequences flow whether the trustee has sued under state law, as in *Stern*, or under the Bankruptcy Code, as in *Granfinanciera*. *See generally Exec. Benefits Ins. Agency v. Arkison (In re Bellingham Ins. Agency)*, 702 F.3d 553 (9th Cir. Dec. 4, 2012).

In the case before this Court, the Ninth Circuit correctly applied *Stern* and *Granfinanciera* in holding that the trustee's state and federal law claims to set aside pre-petition transfers from the debtor to a successor entity that had not filed a claim against the debtor's estate could not be adjudicated outside of an Article III court, at least absent the consent of the transferee. *Bellingham*, 702 F.3d at 565.[3] That non-controversial aspect of the Ninth Circuit's ruling is not before the Court.

The Ninth Circuit also opined, however, that even though a fraudulent conveyance suit by a trustee against a non-creditor must be decided by an Article III judge, a bankruptcy judge, whose appointment is for a limited term and whose salary is not constitutionally protected, may nevertheless hear the case in the first instance and propose findings of fact and conclusions of law to a district judge for *de novo* consideration. *Id.* at 566. The

[3] The Foundations take no position as to the first two issues presented for this Court's review—whether a constitutional objection to a bankruptcy court's determination of a core proceeding involving private rights may be waived and, if so, whether waiver may be implied from the facts of this case.

Ninth Circuit anomalously based its decision on Section 157(c)(1) of the Judicial Code, which delimits the authority of bankruptcy judges in *"non-core"* proceedings:

> A bankruptcy judge may hear a proceeding that is not a core proceeding but that is otherwise related to a case under title 11. In such proceeding, the bankruptcy judge shall submit proposed findings of fact and conclusions of law to the district court, and any final order or judgment shall be entered by the district judge after considering the bankruptcy judge's proposed findings and conclusions and after reviewing *de novo* those matters to which any party has timely and specifically objected. 28 U.S.C. § 157(c)(1).

The Ninth Circuit acknowledged (*Bellingham*, 702 F.3d at 565) that an action by a bankruptcy trustee to avoid an alleged fraudulent transfer is a "core" proceeding, not a "non-core" proceeding, and therefore lies outside the scope of Section 157(c). *See* 28 U.S.C. § 157(b)(2) ("'Core' proceedings include, but are not limited to . . . (H) proceedings to determine, avoid or recover fraudulent conveyances . . . .") The Ninth Circuit also acknowledged (*Bellingham*, 702 F.3d at 565) that while the Judicial Code expressly authorizes bankruptcy judges to "hear and determine" core proceedings—a grant of authority this Court limited on constitutional grounds in *Stern*

v. Marshall—nowhere does it authorize a bankruptcy judge in a core proceeding, unlike in a non-core proceeding, to submit proposed findings and conclusions to a district judge for final decision. In an evident non-sequitur, however, the Ninth Circuit nevertheless reasoned that the power to "hear and determine" a core proceeding "surely encompasses" the power to hear the case and propose findings of fact and conclusions of law to the district court. *Bellingham*, 702 F.3d at 565. Otherwise, the Ninth Circuit continued, bankruptcy judges would be "impotent to address fraudulent conveyance cases," which would "fall in[to] the interstices" of the Judicial Code. *Id.*

The Ninth Circuit's reasoning is unsound and its conclusion should be rejected. Section 157 sharply distinguishes the respective roles of bankruptcy judges and district court judges in core and non-core proceedings (except by consent of all parties under Section 157(c)(2)). Core proceedings are to be heard and determined by a bankruptcy judge, subject to *de novo* review in the district court. Non-core proceedings may be heard by a bankruptcy judge but must be decided by a district judge. Non-core proceedings do not overlap core proceedings, and the bankruptcy court's authority to act in the former does not extend to the latter. The Seventh Circuit made this point clearly and succinctly in its very recent opinion in *Wellness Int'l Network Ltd. v. Sharif*, No. 12-1349, 2013 WL 4441926 (7th Cir. Aug. 21, 2013),

> No statutory provision authorizes a bankruptcy court to propose

> findings of fact and conclusions of law in a core proceeding; such a report and recommendation from the bankruptcy court is statutorily authorized only in noncore proceedings, *see* [Section] 157(c)(1).

While allowing a bankruptcy judge to propose findings and conclusions may appear to be a "practical remedy" in some cases, the Judicial Code does not expressly permit it. *Waldman v. Stone*, 698 F.3d 910, 921 (6th Cir. 2012).

Section 157 thus presents "[t]wo options," core and non-core, each of which conclusively determines "[t]he manner in which a bankruptcy judge may act on" the matter. *Stern*, 131 S.Ct. at 2604-05. In *Stern*, Pierce Marshall argued that even though Vicki Marshall's counterclaim for defamation was a core proceeding under Section 157(b)(2)(C), it was not one that the bankruptcy court could "hear and determine" because it merely "related to" rather than "arose in" Vicki Marshall's bankruptcy. This Court rejected that argument, holding that Section 157 did not recognize a category of core proceeding that was merely "related to" a case under title 11 and thus outside the scope of cases Section 157 authorizes bankruptcy judges to "hear and determine." *Stern*, 131 S.Ct. at 2604. A bankruptcy proceeding is either core, and thus subject to adjudication by a bankruptcy judge subject to traditional appellate review by the district court, or non-core, and thus one in which the bankruptcy judge may propose findings of fact and conclusions of law for the district court's *de novo* consideration. *Id*. To the argument

that Section 157 also recognizes a third type of proceeding—that is, a proceeding that qualifies as core but may be treated as non-core—this Court responded emphatically "[N]o such category exists." *Id.*

Here, the effect of the Ninth Circuit's decision is to create precisely the type of bankruptcy proceeding that this Court declared in *Stern* does not exist: one defined as core but administered and adjudicated as non-core. The Ninth Circuit proposed this new hybrid procedure to plug what it perceived as the statutory "gap" created by *Stern*, in which, contrary to Section 157(b)(1), core proceedings involving private rights can no longer be decided in bankruptcy court. But, of course, the "interstices" the Ninth Circuit conjured are entirely imaginary: core proceedings before district judges would be addressed in just the way district judges administer the other cases on their docket, both simple and complex. Courts do not have the authority to improvise such procedural devices *ad lib*. Such innovations are for Congress, and it is not at all clear whether, when[4] or how Congress might decide to plug the "gap" that so troubled the Ninth Circuit.

Congress created the core/non-core distinction, and defined the responsibilities of the bankruptcy court and the district court with respect to each, expecting that nearly all core bankruptcy proceedings would be heard and determined by

[4] The full impact of *Stern v. Marshall*—including the range of core proceedings that must be heard in a district court and Stern's application to cases by a trustee against a debtor's creditors—may take years to unfold.

bankruptcy judges. If, as a result of *Stern*, the tide of bankruptcy litigation shifts toward the district court and away from the bankruptcy court, Congress may respond in any number of ways. The Ninth Circuit's (and Solicitor General's) jury-rigged, extemporized invention ignores the institutional and policy implications that Congress must weigh in assigning responsibility for the administration of these cases. The bankruptcy courts may, for instance, be seen as having an understandable, even laudable predilection for bringing as many assets as possible into the bankrupt's estate to be distributed to the estate's creditors. Congress, however, may be more concerned with the implications for the competing policy—salient in the cases alleging fraudulent transfers arising out of LBOs but not implicated in the case now before the Court—of protecting the stability of security markets, a policy it expressed so emphatically in section 546(e) of the Bankruptcy Code. *See generally Peterson v. Somers Dublin Ltd.*, Nos. 12–2463, 12–2464, 12–2493, 12–2494, 12–2495, 2013 WL 4767495 (7th Cir. Sept. 6, 2013) (Easterbrook, J.). Courts have no authority to anticipate how Congress might rework the Bankruptcy Code nor to implement extra-statutory stopgaps in the meantime. *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 90 (1982); *Seminole Tribe of Florida v. Florida*, 517 U.S. 44 (1996).

II. Empowering A Bankruptcy Judge To Preside Over Pretrial Matters In Fraudulent Transfer Cases Would Disserve The Interests Of Judicial Economy And The Fair And Orderly Administration Of Civil Justice.

The types of core proceedings that under *Stern* must be determined in an Article III court are those least likely to benefit from the participation of a bankruptcy judge. In *Stern*, the claim that was outside the bankruptcy judge's constitutional authority to decide was a claim for defamation. In *Granfinanciera*, it was a claim for fraudulent conveyance. Both cases thus involved private rights historically enforced in courts of law rather than claims cognizable in equity or admiralty or claims by a government agency to enforce a statute or regulation. In neither case would the specialized training and experience of a bankruptcy judge, as opposed to a district judge, lead to the fairer and more efficient administration of civil justice.

To the extent that a district judge presiding over a core proceeding might benefit from preliminary fact-finding or non-binding decision-making by a subordinate judicial officer, the district judge is free to call upon a magistrate judge for that purpose, just as in any other civil case within the court's jurisdiction. Not only may magistrate judges issue reports and recommendations on case-dispositive questions of law and fact, they may "hear and determine" other pretrial matters, subject to reconsideration by the district judge only where the magistrate judge's order is "clearly erroneous or

contrary to law." 28 U.S.C. § 636(b)(1)(A). Magistrate judges routinely serve as special masters, resolve discovery disputes, and preside over a variety of pretrial and post-trial matters. There is no role a bankruptcy judge could perform in cases requiring the exercise of federal judicial power that district judges do not already assign, frequently and confidently, to magistrate judges.

Perhaps the greatest contribution magistrate judges routinely make to the orderly administration of complex, multiparty litigation is in overseeing pretrial discovery. But while the authority of magistrate judges to exercise near plenary authority over discovery issues is clear and well-established, *see generally* 28 U.S.C. § 636, the authority of a bankruptcy judge to exercise any control whatsoever over the discovery process in a fraudulent transfer case or other core proceeding requiring an Article III judge is highly suspect:

> There is no statutory provision authorizing a bankruptcy court to preside over discovery, apart from its statutory authority over core and non-core matters. It is true that magistrate judges often preside over pretrial matters such as discovery, even if the district court ultimately decides the claim for which discovery is sought, but 28 U.S.C. § 636(b)(1)(A) expressly authorizes a district judge to "designate a magistrate judge to hear and determine any pretrial

> matter pending before the court," with certain exceptions and subject to reconsideration by the district judge if "the magistrate judge's order is clearly erroneous or contrary to law." No analogous statutory authorization exists for bankruptcy judges.

Wellness Int'l Network Ltd., No. 12-1349, 2013 WL 4441926.

The involvement of a bankruptcy judge in a core proceeding justiciable in an Article III court would be particularly inappropriate and superfluous where the case is triable to a jury. Bankruptcy judges have no statutory authority to conduct jury trials absent consent of the parties, *see* 28 U.S.C. § 157(e)—and perhaps no constitutional authority even in those cases—and few bankruptcy judges have likely ever conducted a jury trial through judgment. Where the case is to be tried to a jury, proposed findings and conclusions by a bankruptcy judge would be wasteful and moot.

In short, there is no role for a bankruptcy judge in a fraudulent transfer case or other core proceeding justiciable only in an Article III court. The involvement of a bankruptcy judge in such cases would only add confusion, expense and delay with no countervailing enhancement to the fairness or accuracy of the result.

CONCLUSION

For the foregoing reasons, the judgment of the court of appeals should be vacated.

Respectfully submitted,

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