No. 10-179

In The Supreme Court of the United States

HOWARD K. STERN, EXECUTOR OF THE ESTATE OF VICKIE LYNN MARSHALL,

Petitioner,

v.

ELAINE T. MARSHALL, EXECUTRIX OF THE ESTATE OF E. PIERCE MARSHALL,

Respondent.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

BRIEF OF PETITIONER

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QUESTIONS PRESENTED

In the 1984 Bankruptcy Act, Congress divided bankruptcy court jurisdiction into "core" proceedings, in which bankruptcy judges can enter final orders, and "non-core" proceedings that are subject to district court de novo review. *See* 28 U.S.C. §157(b). Congress expressly identified certain core proceedings, including "counterclaims by the estate against persons filing claims against the estate." §157(b)(2)(C). Despite Article III challenges, lower courts across the country have uniformly held for decades that bankruptcy courts can enter final orders on debtors' compulsory counterclaims to proofs of claim.[1] Until now.

The Ninth Circuit opinion here holds that under *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) (*Marathon*) and *Katchen v. Landy*, 382 U.S. 323 (1966), core jurisdiction constitutionally exists under §157(b)(2)(C) only for compulsory counterclaims entirely encompassed within the allowance or disallowance of the creditor's claim against the estate and that raise no issue beyond that claim. Even though here the debtor's compulsory counterclaim constituted an affirmative defense to

[1] A debtor's compulsory counterclaim to a proof of claim is any counterclaim that, at the time of pleading, arises out of the same transaction or occurrence as the creditor's claim against the estate and is not already pending in another action. Fed. R. Bankr. P. 7013; Fed. R. Civ. P. 13(a).

QUESTION PRESENTED – Continued

the proof of claim and, if decided first, would have defeated it entirely, the Court held the counterclaim was non-core because the debtor had to prove additional elements to prevail on it.

Accordingly, the questions presented are:

1. Whether the Ninth Circuit opinion, which renders §157(b)(2)(C) surplusage in light of §157(b)(2)(B), contravenes Congress' intent in enacting §157(b)(2)(C).

2. Whether Congress may, under Articles I and III, constitutionally authorize core jurisdiction over debtors' compulsory counterclaims to proofs of claim.

3. Whether the Ninth Circuit misapplied *Marathon* and *Katchen* and contravened this Court's post-*Marathon* precedent, creating a circuit split in the process, by holding that Congress cannot constitutionally authorize non-Article III bankruptcy judges to enter final judgment on all compulsory counterclaims to proofs of claim.

PARTIES TO THE PROCEEDING

The original parties to this case, Vickie Lynn Marshall and Pierce Marshall, died during the pendency of this appeal. The current parties are Howard K. Stern, Executor of the Estate of Vickie Lynn Marshall, and Elaine T. Marshall, Executrix of the Estate of E. Pierce Marshall.

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OPINIONS BELOW

The Ninth Circuit's opinion is reported at 600 F.3d 1037 (9th Cir. 2010), Appendix to the Petition for a Writ of Certiorari ("App.") at 1-89.

Three opinions of the District Court for the Central District of California are reported at 275 B.R. 5 (C.D. Cal. 2002), App. 90-214; 271 B.R. 858 (C.D. Cal. 2001), App. 217-34; and 264 B.R. 609 (C.D. Cal. 2001), App. 239-85. A fourth is unpublished, App. 235-38.

Two opinions of the Bankruptcy Court for the Central District of California are reported at 257 B.R. 35 (Bankr. C.D. Cal. 2000), App. 286-99; and 253 B.R. 550 (Bankr. C.D. Cal. 2000), App. 313-36. A third is unpublished, App. 305-12.

JURISDICTION

The Ninth Circuit issued its opinion on March 19, 2010; it denied panel and *en banc* rehearing on May 5, 2010. App. 1, 337-38.

This Court has jurisdiction under 28 U.S.C. §1254(1). Jurisdiction was proper in the District Court under 28 U.S.C. §§1331 and 1334, and in the Ninth Circuit under 28 U.S.C. §1291.

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

Relevant portions of Article I, § 8, and the entirety of Article III of the United States Constitution are reprinted at App. 339-41.

28 U.S.C. §§157 ("§157"), 1331 and 1334 are reprinted at App. 342-47.

STATEMENT OF THE CASE

Both the bankruptcy and district courts below found that Vickie's[2] husband J. Howard Marshall, II ("Howard") attempted to provide for Vickie through an inter vivos trust. App. 25-26, 134-48, 198-202. Those courts concluded that his son Pierce suppressed or destroyed the trust instrument and stripped Howard of his assets before his death. App. 25-26, 143-202, 211-14. The bankruptcy and district courts found Pierce liable for tortious interference and awarded Vickie millions in compensatory and punitive damages. App. 3, 214.

A. The Bankruptcy Proceedings.

In January 1996, Vickie sought Chapter 11 bankruptcy protection following Howard's death.

[2] For the sake of readability, we adopt the Ninth Circuit's approach and refer to the petitioner as Vickie Lynn Marshall ("Vickie") and the respondent as Pierce Marshall ("Pierce").

App. 91-93. Pierce, after stating his unequivocal intention to file "proofs of claims that provide us the maximum range of options" in the "VLS bankruptcy," Joint Appendix ("JA") 55, dismissed a pending state-court defamation suit against Vickie and brought his defamation claims into the bankruptcy court by filing, in May 1996, a nondischargeability complaint to pursue claims against Vickie personally, and, in June 1996, a separate proof of claim for an unliquidated amount of damages against Vickie's bankruptcy estate. App. 14-16 nn.10 & 11, 77-87, 266-67 n.17, 274-76; JA 57, 59, 105; Supplemental Excerpts of Record ("SER") 6101-02, 6801 (Pierce telling bankruptcy court that the amount of his creditor's claim "shall be determined by the adversary proceedings filed herein" and he is "happy" to litigate "[his] claim here" because "we did choose this forum"); *see* SER 8409-19 (Pierce requesting from the bankruptcy court an $8.5 million estimation of his claim for plan confirmation and voting purposes).

Vickie objected to Pierce's proof of claim, answered his adversary complaint pleading truth as an affirmative defense, and filed a compulsory counterclaim for tortious interference with an inter vivos gift. App. 15-16, 48 n.29, 94, 378-81; SER 12204. This was the first time Vickie asserted that claim in any court. App. 48 n.29; JA 84; *In re Marshall*, 273 B.R. 822, 825-26 (Bankr. C.D. Cal. 2002); SER 12260.

Shortly after Vickie filed her counterclaim, the bankruptcy court found that it was compulsory as it arose out of the same transactions and occurrences as

Pierce's proof of claim and that it was core under subsections (B) and (C) of §157(b)(2), which includes as core proceedings, respectively, "allowance or disallowance of claims against the estate" and "counterclaims by the estate against persons filing claims against the estate." App. 294-96, 306-07.[3]

More than two years after filing his proof of claim, and faced with the imminent prospect of monetary and terminating sanctions by the bankruptcy court, Pierce moved for the first time to withdraw the reference of the adversary proceeding "so that the case will proceed before the District Court for purposes of the mandatory status conference, dispositive motions and trial." JA 95, 128-29; Excerpts of Record ("ER") 1949-57; SER 8697, 8703-10.[4]

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[3] Pierce acknowledged that "the defamatory statements and the challenged transactions" that were at issue in his dismissed state-court defamation action and carried over into his proof of claim "are at the heart of" Vickie's counterclaim. JA 107. And he told the bankruptcy court that his defamation claim and Vickie's counterclaim constituted "both halves" of the same action. App. 275.

[4] After the close of pleadings, Pierce unsuccessfully filed motions in the bankruptcy court to stay Vickie's counterclaims, to dismiss her counterclaims and, belatedly, in January 1997, for abstention. ER 957, 1049; SER 6111, 6114, 6122, 6748, 8596-97. In addition, there was pervasive judicial activity in the bankruptcy court regarding Pierce's resistance to discovery, including his failure to produce critical documents, his admitted destruction of potentially relevant documents after Vickie's requested production, his failure to appear for depositions (at least once in direct violation of a court order), and his failure to pay discovery sanctions. *See* ER 1949-57; SER 8697, 8703-10.

The district court initially granted Pierce's motion, ordering the defamation claim and Vickie's compulsory counterclaim "withdrawn to this Court." JA 122-23. However, it vacated its initial order and referred the case back to the bankruptcy court. JA 129, 138-39. It explained that its decision was driven by Pierce's "selection of forum," stressing that Vickie did not include Pierce in the litigation, that Pierce "wanted to be included" and that "much of what we see here is the spawn of what he begot." JA 129-30. The court also mentioned, inter alia, "judicial economy reasons" and "the immersion the bankruptcy judge has in this case." JA 130.

Trial began in the bankruptcy court in late 1999. During trial, the court granted Vickie's pending motion for summary judgment on Pierce's defamation claim on the ground that Vickie neither published nor ratified the alleged defamatory statements, App. 18, 244-45, a decision Pierce never appealed. After a full trial, the bankruptcy court found Pierce liable for tortious interference with a gift and awarded compensatory damages of $449 million (the amount of the intended trust) and $25 million in punitive damages, entering judgment in December 2000. App. 18-20, 286-336.[5] Under Vickie's bankruptcy plan, the counterclaim proceeds are to be applied first to creditor claims. App. 17; SER 6074-75.

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[5] The judgment was based partly on evidentiary sanctions, the court having found that Pierce engaged in "massive discovery abuse," including destroying documents relevant to Vickie's claim. App. 19-20 n.17, 317 n.5, 320-26.

B. The Texas Probate Proceedings.

A Texas probate court began administering Howard's estate in August 1995. App. 11. Vickie first appeared in that proceeding in 1998, when she joined a pending will contest filed by Pierce's brother. App. 12, 48 n.29. In January 2000, Vickie prophylactically filed her tortious interference with gift claim in the probate court after Pierce argued that the bankruptcy court lacked jurisdiction under the probate exception. *Marshall*, 273 B.R. at 825-26; SER 12260.

After the bankruptcy court entered judgment for Vickie in December 2000, Vickie immediately filed the bankruptcy judgment in the Texas probate court and voluntarily nonsuited her claims there without prejudice. App. 20, 232; *Marshall*, 273 B.R. at 826; SER 8426-27, 10306.

After nonsuiting her claims, Vickie at first remained in the probate proceedings only as a counter-defendant on a sanctions claim Pierce had brought in 1999. App. 21 & n.18, 223 n.4; SER 8422-27. Pierce then brought new claims against Vickie in an effort to re-litigate the issues the bankruptcy court had already decided. *Marshall*, 273 B.R. at 825-26; SER 8427-28, 8606-28, 12260-61.

Although the bankruptcy court directed Pierce to dismiss all his new probate claims, *Marshall*, 273 B.R. at 826, 831; SER 8431-33, Pierce's attorneys dismissed only a tortious interference claim, assuring the bankruptcy court that any risk of inconsistent judgments had been eliminated, that the "only" issue

in the probate-court trial "directed at Ms. Marshall" was whether Howard and Vickie had an agreement for him to give her one-half his property and that, in seeking declaratory relief and submitting that issue, Pierce "only seek[s] to avoid any possibility of future litigation with Vickie Marshall over [Howard's estate] and to ensure that the Texas Probate Court can determine all claimants and efficiently administer that estate," ER 3782; SER 6624, 8438, 8446, 8470, 12514. Based on these representations, and its later finding that Pierce's claim in Texas was "entirely consistent" with its own judgment, which was not based on a "finding of an 'agreement' between [Vickie] and [Howard] to give her one-half of all his property," the bankruptcy court ultimately permitted Pierce to proceed in the limited fashion he had represented to the bankruptcy court. *Marshall*, 273 B.R. at 826-27, 831-32; SER 8585-86, 12261 & n.2.

Vickie thereafter participated in the probate-court trial only as a counterdefendant, App. 21, 232, and none of her earlier-proposed jury questions was presented to the jury, SER 12260-61 & n.2; *compare* ER 3713-99 *with* ER 4076-77. Pierce obtained a judgment against Vickie based on his "no agreement" theory, which became final in February 2002. App. 92; *Marshall*, 273 B.R. at 826-27; SER 12260-61 & n.2. Explaining the scope of its judgment, the probate court confirmed that it "didn't try any issue of tortious interference with inter vivos gift in this case at all" and only decided "all the issues concerning the Estate"

and "[n]ot anything to do with what complaints that [Vickie] has against [Pierce]." SER 8660, 8664.[6]

C. The District Court Proceedings.

Shortly after the bankruptcy court entered judgment and over a year before the Texas probate judgment became final, Pierce appealed the bankruptcy court judgment to the district court. App. 20, 96.

The district court concluded that Vickie's counterclaim was a compulsory counterclaim to Pierce's defamation claim; however, it also held the counterclaim was not a "core" proceeding because of certain post-pleading developments, such as the amount Vickie recovered on the counterclaim and the bankruptcy court's rationale in dismissing Pierce's claim. App. 236-38, 265-83; SER 12204. It therefore treated the bankruptcy court's judgment as proposed and

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[6] Notably, the gift Howard intended was an irrevocable gift during his lifetime, not a testamentary disposition. App. 136-48, 233, 316-20, 330-31; SER 11788. And Pierce conceded that Howard could have funded Vickie's gift during his lifetime by borrowing against his assets, without ever taking funds from the living trust. Pierce's Substituted Reply Br. 2, Sept. 18, 2003 (9th Cir. docket entry 98) ("the Living Trust's terms allowed J. Howard to borrow against his assets up until the day he died," so that "if he had really wanted to give Vickie a large gift, he could have notwithstanding the exchanges [of property] in the Living Trust"). Indeed, Howard's attorney contemplated funding the trust by issuing notes or stock measured by an increase in value of Howard's Koch stock. SER 9567.

undertook a "comprehensive, complete and independent review of" the issues. App. 97, 284.

Pierce subsequently moved for summary judgment, claiming res judicata and collateral estoppel based on the Texas probate judgment. The district court denied the motion on the grounds that the requisite identity of issues was lacking, that Pierce's motion was untimely and that applying preclusion in these circumstances was fundamentally unfair. App. 56 n.32, 223-33.

In March 2002, about a month after the Texas judgment had become final, the district court affirmed the bankruptcy court's findings and entered judgment for Vickie. App. 91, 194-95, 215-16. It concluded Howard had directed his lawyers to prepare an inter vivos trust for Vickie's benefit consisting of half the appreciation of his assets from the date of their marriage, App. 134-48, 198-202, but that Pierce conspired to suppress or destroy the trust instrument and to strip Howard of his assets, App. 145-202, 211-14.

It awarded compensatory damages of approximately $44.3 million and the same amount in punitive damages, finding "overwhelming" evidence of Pierce's "willfulness, maliciousness, and fraud." App. 26, 212, 214.[7] It characterized Pierce's litigation

[7] While the district court agreed with the bankruptcy court that Howard intended to give Vickie half the increase of his assets from the date of their marriage, it valued the increase only until the date of Howard's death, while the bankruptcy court valued it through the date of trial. App. 204.

tactics as "the height of bad faith," App. 148-49 n.21, noted that if the evidence of the trust for Vickie had been insufficient "the discovery abuses in this case might have led the Court to deem this fact as established," App. 137 n.17, and "encourage[d]" the Justice Department to investigate Pierce's chief witness, Edwin Hunter, for perjury prosecution, App. 160 n.28.

D. Ninth Circuit Appeal I.

Pierce appealed and Vickie cross-appealed. App. 26-27. The Ninth Circuit reversed the judgment, concluding the probate exception to federal jurisdiction barred Vickie's counterclaim. *Id.*

In May 2006, this Court unanimously reversed and remanded to the Ninth Circuit for further proceedings to consider whether Vickie's claim was core and to address claim and issue preclusion. *Marshall v. Marshall*, 547 U.S. 293, 315 (2006).[8]

E. Ninth Circuit Appeal II.

On March 19, 2010, nearly four years after remand, the Ninth Circuit again reversed the district court's judgment in favor of Vickie, holding that her compulsory counterclaim was not a core proceeding under 28 U.S.C. §157(b)(2)(C); her bankruptcy court

[8] Shortly after remand, Pierce died, and several months later, Vickie died; each was substituted on the appeal by the respective executor of the estate. App. 5-6 n.1.

judgment was therefore not "final"; and her district court judgment, entered after the Texas probate judgment, was barred by that judgment on the ground of issue preclusion. App. 55-58, 64-65.

In so concluding, the Ninth Circuit made several significant rulings:

- Vickie's counterclaim was a compulsory counterclaim to Pierce's proof of claim, "because the 'operative facts underlying [her] action' are the same as those underlying [Pierce's] defamation claim" and "[t]he defamation claim, [Vickie's] affirmative defense of truth, and her counterclaim for tortious interference all concern the alleged efforts by [Pierce] to obtain control of his father's estate" through improper means, App. 47-48 & n.29;
- Core jurisdiction can exist over a counterclaim "based upon state law, not the Bankruptcy Code or something else that is unique to the bankruptcy context," even if the counterclaim "could have been brought in state court," App. 43-44 & nn.26, 27;
- The determination whether a counterclaim to a proof of claim is core under §157(b)(2)(C) "must focus largely on what is available to the court at the time of filing, that is, the parties' pleadings," App. 51-52;

- Vickie's success on her counterclaim would defeat Pierce's defamation claim by establishing the affirmative defense of truth, App. 47-48, 55.

Although these holdings supported the conclusion that Vickie's counterclaim was core, the court – relying principally on *Katchen v. Landy*, 382 U.S. 323 (1966) and *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982) (*Marathon*) – narrowly construed §157(b)(2)(C) to mean that even a compulsory counterclaim to a proof of claim does not qualify as core unless it is "'so closely related to the proof of claim that the resolution of the counterclaim is necessary to resolve the allowance or disallowance of the claim itself.'" App. 49-50. It held Vickie's compulsory counterclaim was non-core because even if she proved through her counterclaim that the alleged defamatory statements were true, thus defeating Pierce's proof of claim, she would have had to prove additional facts to prevail on her counterclaim, including damages; therefore, "its resolution was not a necessary precursor" to resolving Pierce's defamation claim against the estate and it "was not so closely related to his claim that they essentially merged, with her counterclaim becoming part and parcel of the bankruptcy court's claims determination and allowance process." App. 4, 49-50, 55.

To hold otherwise, the court concluded, would be "an expansive reading of §157(b)(2)(C) [that] would certainly run afoul of the Court's holding in *Marathon*" and "arguably be inconsistent with the

Congress' intent to revise the Bankruptcy Code in a manner consistent with the principles of *Marathon* to make its jurisdictional grant constitutional." App. 46.

Because the conclusion that Vickie's counterclaim was non-core meant her bankruptcy judgment was not final when entered in December 2000, the Ninth Circuit, as noted above, reversed the district court judgment on the ground of issue preclusion, concluding that the Texas probate court's judgment was the earliest final judgment on "several of the legal and factual issues that Vickie Lynn Marshall sought to litigate in the bankruptcy proceeding." App. 4-5, 55-56, 58, 64. The Ninth Circuit never addressed the district court's determination that binding her to the Texas court's findings would be fundamentally unfair. App. 56 n.32, 232.

Vickie petitioned for rehearing *en banc* on the ground that the opinion erred in determining her counterclaim was non-core. App. 348-77. She also sought panel rehearing based on the panel's failure to determine whether the district court properly exercised its discretion to deny issue preclusion on fundamental fairness grounds. *Id.* The petition was denied. App. 337-38.

This Court granted certiorari on September 28, 2010.

SUMMARY OF ARGUMENT

Purporting to follow *Marathon*, 458 U.S. 50, and *Katchen*, 382 U.S. 323, the Ninth Circuit has held that, even though 28 U.S.C. §157(b)(2)(C) empowers bankruptcy courts to finally adjudicate "counterclaims by the estate against persons filing claims against the estate," Article III forecloses them from finally adjudicating even a *compulsory* counterclaim to a claim against the estate – unless the counterclaim's resolution is a "necessary precursor" to resolving the creditor's claim and "so closely related to [the] claim that they essentially merge[ ], with [the] counterclaim becoming part and parcel of the bankruptcy court's claims determination and allowance process." App. 4.

Thus, even though Pierce forced Vickie to file her compulsory counterclaim in the bankruptcy by filing his proof of claim for defamation, even though success on her counterclaim would necessarily defeat his proof of claim by establishing the affirmative defense of truth, and even though the counterclaim arose out of the same transaction that Pierce placed at issue by seeking a distribution from the bankruptcy estate, the Ninth Circuit concluded that the bankruptcy court could not resolve Pierce's claim and Vickie's compulsory counterclaim together. The Ninth Circuit's new test, which effectively reverses settled bankruptcy practice both before and after *Marathon*, is insupportable.

• ***Congress intended that §157(b)(2)(C) empower bankruptcy courts to enter final judgment on all compulsory counterclaims to proofs of claim.*** The Ninth Circuit's test contravenes congressional intent. Section 157(b)(2)(C)'s plain language and the legislative history behind the 1984 Bankruptcy Act show that Congress intended to confer core jurisdiction over *all* estate counterclaims to proofs of claim and that Congress drafted the 1984 Act to conform to its understanding of *Marathon*'s constitutional strictures.

Not only does the Ninth Circuit's construction reduce §157(b)(2)(C) to surplusage – since Congress already specified in §157(b)(2)(B) that core proceedings include the "allowance or disallowance of claims against the estate" – its splintered approach to bankruptcy jurisdiction will confound bankruptcy administration and directly undermine the efficiencies Congress intended. Because Congress meant what it said in §157(b)(2)(C), the true question on appeal is whether §157(b)(2)(C)'s grant of core jurisdiction over all compulsory counterclaims is constitutional.

• ***Section 157(b)(2)(C)'s grant of core jurisdiction over all compulsory counterclaims is constitutional.*** This Court has acknowledged repeatedly that its Article III precedents "do not admit of easy synthesis." *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 847 (1986) (*Schor*). Nonetheless, our brief shows that §157(b)(2)(C)'s grant of core jurisdiction over all compulsory counterclaims is

constitutional under each of this Court's various announced standards and considerations, whether viewed individually or collectively. For example:

This Court's pre- and post-*Marathon* precedent recognizes that creditors submitting proofs of claim for adjudication to non-Article III bankruptcy judges acquiesce to the adjudication of integrally-related counterclaims because they invoke the benefits of claims allowance, a process integral to the restructuring of debtor-creditor relations. A creditor seeking such distribution from the estate must also accept the burdens of the bankruptcy process, including the bankruptcy court's equitable power to issue complete relief over the entire dispute that the creditor placed at issue.

Core jurisdiction over all compulsory counterclaims is also consistent with this Court's post-*Marathon* precedent assessing the congressional delegation of decisionmaking to non-Article III tribunals by considering practical consequences of the adjudicatory scheme in light of the concerns underlying Article III. Core jurisdiction over all compulsory counterclaims tracks historical practice, promotes Congress' goals of efficient bankruptcy administration, and falls within Congress' plenary Article I power over bankruptcies. Conversely, it poses only a *de minimis* intrusion on the separation-of-powers concerns that underlie Article III and much of *Marathon*.

Finally, core jurisdiction over all compulsory counterclaims comports with this Court's post-*Marathon*

cases upholding non-Article III adjudication of "public rights," which includes private rights closely integrated with public regulatory schemes, and with this Court's precedent upholding factfinding by specialized adjuncts to Article III courts.

ARGUMENT

I. CONGRESS INTENDED FOR 28 U.S.C. §157(b)(2)(C) TO EMPOWER BANKRUPTCY COURTS TO RENDER FINAL JUDGMENT ON ALL COMPULSORY COUNTERCLAIMS TO CREDITOR CLAIMS AGAINST THE ESTATE AND IT DRAFTED THE STATUTE TO CONFORM TO *MARATHON*'S CONSTITUTIONAL STRICTURES.

A. Backdrop To *Marathon*, The 1984 Bankruptcy Act And §157(b)(2)(C).

1. Prior to the 1978 Bankruptcy Act, bankruptcy referees exercised the summary jurisdiction in bankruptcy of the district court, including the determination of compulsory counterclaims to proofs of claim.

Before Congress enacted the 1978 Bankruptcy Act ultimately invalidated by *Marathon*, bankruptcy proceedings were either summary or plenary under the 1898 Bankruptcy Act. *Marathon*, 458 U.S. at 53. District courts sitting in bankruptcy, and referees to whom they could refer matters and who lacked Article III salary and tenure protections, had summary

jurisdiction to adjudicate controversies regarding property in the court's actual or constructive possession (such as creditor claims against the estate) and even "plenary" claims (for example, actions involving property in the possession of third parties) where the parties expressly or impliedly consented to adjudication. *Id.*; *Katchen*, 382 U.S. at 327-32 & n.9.

"The referee would initially hear and decide practically all matters arising in the proceedings, including the allowance and disallowance of the claims of creditors." *Marathon*, 458 U.S. at 99 (White, J., dissenting). The bankruptcy referees were subordinate adjuncts of the district courts; the district courts appointed and removed them and had absolute discretion to refer or withdraw the reference of the bankruptcy case. *Id.* at 79 n.31.

When a creditor filed a proof of claim in the bankruptcy, the district court and the non-Article III bankruptcy referees generally had summary jurisdiction over the bankruptcy trustee's compulsory counterclaims. 1 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy, ¶3.02[3][d][i], p. 3-32 (16th ed. 2010); *see*, *e.g.*, *Peters v. Lines*, 275 F.2d 919, 924-25 (9th Cir. 1960); *In re Majestic Radio & Television Corp.*, 227 F.2d 152, 156 (7th Cir. 1955).[9]

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[9] Courts were split as to whether summary jurisdiction extended to unrelated or permissive counterclaims to proofs of claim. 1 Collier on Bankruptcy, *supra*, ¶3.02[3][d][i], at 3-32; *compare Peters,* 275 F.2d at 924-25 *with Inter-State Nat'l Bank of Kansas City v. Luther*, 221 F.2d 382, 389-90 (10th Cir. 1955).

In *Katchen*, this Court upheld a bankruptcy referee's summary jurisdiction to decide a trustee's counterclaim to recover a voidable preference from a creditor who filed a proof of claim, irrespective of whether the preference counterclaim arose from the same transaction as the proof of claim. 382 U.S. at 326 n.1. It held that, even though the trustee would have had to file a plenary action to recover the preference had the creditor not filed a proof of claim, the bankruptcy court could enter a money judgment for the amount of the preference counterclaim because, inter alia, (a) having "'invoke[d] the aid of the bankruptcy court by offering a proof of claim and demanding its allowance,'" the creditor "'must abide the consequences of that procedure'" and submit to the bankruptcy court's jurisdiction to decide "'all matters in dispute [between the parties] and decree complete relief'"; (b) the counterclaim was "part and parcel of the [claims] allowance process"; and (c) there was no jury trial right because issues that arise "as part of the process of allowance or disallowance of claims" are triable in equity. *Id.* at 327-28, 330-32 & n.9, 335-38.

After *Katchen*, some commentators argued that creditors who file proofs of claim should be held to acquiesce to summary jurisdiction over any debtor counterclaim. *See In re Depo*, 40 B.R. 537, 541-42 (N.D.N.Y. 1984) (citing authorities). Yet, most courts held that a proof of claim established the creditor's submission to summary jurisdiction over "same transaction" counterclaims plus permissive counterclaims

statutorily connected to claims allowance, such as preferences or voidable transfers. *See*, *e.g.*, *id.*; *In re Carnell Constr. Corp.*, 424 F.2d 296, 298-99 (3d Cir. 1970); *In re L.A. Trust Deed & Mortg. Exch.*, 464 F.2d 1136, 1138-39 (9th Cir. 1972).

2. In the 1978 Bankruptcy Act, Congress expanded the jurisdiction of non-Article III bankruptcy judges to encompass all proceedings relating to bankruptcy and substantially reduced control by Article III judges.

In the Bankruptcy Act of 1978, Congress eliminated the summary/plenary distinction, substantially broadening bankruptcy jurisdiction by conferring on non-Article III bankruptcy courts jurisdiction over all "civil proceedings arising under title 11 [the Bankruptcy title] or arising in or related to cases under title 11" and by vesting them with "all of the 'powers of a court of equity, law and admiralty.'" *Marathon*, 458 U.S. at 54-55 & n.3 (emphasis omitted). In contrast to the 1898 Act, bankruptcy courts were "'independent of the United States district courts'" and the President (instead of the district courts as before) appointed the bankruptcy judges (to 14-year terms), with the advice and consent of the Senate. *Id.* at 53, 79 n.31.

B. Congress Enacted The 1984 Bankruptcy Act To Comply With *Marathon*'s Constitutional Concerns.

1. *Marathon*'s plurality and concurrence.

In its 1982 *Marathon* decision, which triggered four separate opinions, none of which commanded a majority, this Court held the 1978 Act was unconstitutional because it authorized a bankruptcy judge lacking Article III tenure and salary guarantees to determine state common law (contract and tort) claims the debtor had commenced against a non-creditor defendant (Marathon) that had not filed a proof of claim or otherwise previously appeared in the bankruptcy case. *Id.* at 76, 87 (plurality), 89-91 (Rehnquist, J., concurring), 92 (Burger, C.J., dissenting).

***The plurality*:** The four-justice plurality concluded that the Court had previously upheld congressional grants of plenary power directly to non-Article III tribunals only in relation to territorial courts, military courts, and legislative courts and administrative agencies adjudicating "public rights." *Id*. at 63-71. It concluded that the debtor's contract claims, which merely sought damages from a non-creditor defendant to augment the estate, could not be deemed a public right, because

> the restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power, must be distinguished from the adjudication of state-created private rights, such as the right to recover contract damages that

> is at issue in this case. The former may well be a "public right," but the latter obviously is not.

Id. at 71. The plurality's constitutional concern focused on the "broad range of questions that can be brought into a bankruptcy court because they are 'related to cases under title 11.'" *Id.* at 74.

The plurality also concluded that the Act did not fall within the Court's precedent approving "the use of administrative agencies and magistrates as adjuncts to Art. III courts," because bankruptcy courts were not true adjuncts under the new act. *Id.* at 77-87. It concluded adjunct power was "at a minimum" for the debtor's state common law claims against the non-creditor defendant, noting that, in contrast, "[o]f course, bankruptcy adjudications themselves, as well as the manner in which the rights of debtors and creditors are adjusted, are matters of federal law." *Id.* at 84 n.36.[10]

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[10] The plurality described when specialized factfinding tribunals are constitutional – language Congress later emphasized in defining bankruptcy court power under the 1984 Bankruptcy Act, *see* §I.C.2, *post*:

- "[I]t is clear that when Congress creates a substantive federal right, it possesses substantial discretion to prescribe the manner in which that right may be adjudicated – including the assignment to a[ ] [non-Article III] adjunct of some functions historically performed by judges," including factual determinations "by a specialized factfinding tribunal designed by Congress, without constitutional bar," *id.* at 80-81;

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The plurality never addressed whether non-Article III bankruptcy judges could determine estate counterclaims to proofs of claim. However, the three-justice dissent described *Katchen* as upholding a bankruptcy referee's power "to hear and decide a counterclaim against the creditor arising out of the same transaction" and noted that, had Marathon filed a claim against the estate, the bankruptcy court properly could have adjudicated the debtor's state-law claim as a counterclaim. 458 U.S. at 97 n.4, 99-100 (White, J., dissenting). The plurality did not disagree, but stated in a footnote that *Katchen* did not discuss Article III and that the 1978 Act fundamentally changed prior bankruptcy practice because bankruptcy referees formerly "were 'subordinate adjuncts of the district courts,'" were "appointed and removable only by the district court," and district courts had the power to withdraw cases from the referee. *Id.* at 79 n.31.

- "[W]hen Congress creates a statutory right, it clearly has the discretion, in defining that right, to create presumptions, or assign burdens of proof, or prescribe remedies; it may also provide that persons seeking to vindicate that right must do so before particularized tribunals created to perform the specialized adjudicative tasks related to that right," *id.* at 83; and
- Although such provisions "affect the exercise of judicial power," they are constitutional because they are "incidental to Congress' power to define the right that it has created." *Id.*

***The two-justice concurrence*:** Acknowledging that the Court's Article III precedent does "not admit of easy synthesis," Justice Rehnquist's concurrence concluded that whatever the correct standard might be, bankruptcy courts were not adjuncts of the district court under the 1978 Act and no case "has gone so far as to sanction the type of adjudication as to which Marathon will be subjected against its will under the provisions of the 1978 Act" – a claim that arises entirely under state law because it is a traditional state common law claim ("the stuff of the traditional actions at common law tried by the courts at Westminster in 1789") that has no relation to the bankruptcy other than the plaintiff being the debtor. *Id.* at 90-91.

Chief Justice Burger explained in a separate opinion that Justice Rehnquist's concurrence establishes *Marathon*'s holding, that the holding prohibits non-Article III bankruptcy courts from adjudicating only "a relatively narrow category of claims," and that Congress could resolve the constitutional issue simply by routing *Marathon*-type claims – "ancillary common-law actions" that are "related only peripherally to an adjudication of bankruptcy under federal law" – to the district court. *Id.* at 92 (Burger, C.J., dissenting).

2. The 1984 Act.

Congress enacted the 1984 Bankruptcy Act "for the specific purpose of curing the constitutional

problems of the scheme under which [*Marathon*] arose." *In re Mankin*, 823 F.2d 1296, 1306 (9th Cir. 1987); *accord*, *In re Arnold Print Works, Inc.*, 815 F.2d 165, 166 (1st Cir. 1987) (Breyer, J.) (1984 Act was "an effort to cure the constitutional defect").

Among the changes: (1) Congress conferred jurisdiction over "all civil proceedings arising under title 11, or arising in or related to cases under title 11" on the district courts and gave the district courts the discretion to refer those matters to bankruptcy judges and the power to withdraw referred matters at any time, 28 U.S.C. §§1334(a), (b), 157(a), (d); (2) bankruptcy courts were now units of the district courts, and bankruptcy judges serve as judicial officers of the district courts, 28 U.S.C. §§151, 152(a)(1); and (3) Article III judges appoint the bankruptcy judges (instead of the President and Senate) and control any removal for cause during their term, 28 U.S.C. §152(a), (e).

Consistent with *Marathon*'s limited holding, Congress also divided bankruptcy court jurisdiction into "core" proceedings, in which bankruptcy courts could render final orders subject to traditional appellate review by the district court, and proceedings that are only "related to a case under title 11," which are subject to district court de novo review absent the parties' consent to bankruptcy court determination. §§157(b)(1), (3), (c)(1)-(2), 158.

C. Congress Intended §157(b)(2)(C) To Authorize Bankruptcy Courts To Render Final Judgment On All Compulsory Counterclaims By The Estate Against Creditors Filing Claims Against The Estate.

1. The statute's plain language.

Section 157(b)(2) provides that "[c]ore proceedings include, but are not limited to" a number of specific types of proceedings. Thus, while Congress did not attempt to identify every proceeding within a bankruptcy court's core jurisdiction, §157(b)(2) "lists various types of proceedings *deemed by Congress* to be core proceedings." *Mankin*, 823 F.2d at 1299 (emphasis added). "Section 157(b)(2) does not set categorical limits on the jurisdiction of bankruptcy courts over core proceedings, but rather merely enumerates examples of proceedings falling within a bankruptcy court's core proceeding jurisdiction." *Id.* at 1300.

Accordingly, §157(b)(2)'s plain language establishes that Congress, by designating "counterclaims by the estate against persons filing claims against the estate" as core in §157(b)(2)(C), intended to empower bankruptcy courts to render final judgment on estate counterclaims to creditors' claims against the estate.

"The linguistic structure of §157 lends further support to this conclusion. Subsection (b)(1) equates core proceedings with those 'arising under title 11, or

arising in a case under title 11,' whereas subsection (c)(1) makes 'non-core' proceedings synonymous with 'otherwise related to' proceedings." *In re Toledo*, 170 F.3d 1340, 1349 (11th Cir. 1999); *see also In re Robino*, 243 B.R. 472, 493 (Bankr. N.D. Ala. 1999) (§157(b)(2) provides a "nonexclusive list of 'arising in' or 'arising under' proceedings"). Unlike the debtor's claim against the non-creditor defendant in *Marathon*, a debtor's counterclaim to a proof of claim "arises in" the bankruptcy case even if it involves rights created by state law, because the claims allowance process only exists in bankruptcy. *In re Bar M Petroleum Co.*, 63 B.R. 343, 346 (Bankr. W.D. Tex. 1986) ("[w]hile the facts alleged by the Trustee could have been the basis for a State Court suit commenced totally independently of the Chapter 11 case, the counterclaim, supported coincidentally by those same facts, could only be asserted in the Debtor's reorganization case in which the claim of Defendant was filed").[11]

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[11] *See also In re Asousa P'ship*, 276 B.R. 55, 77 (Bankr. E.D. Pa. 2002) ("objections to claims [against the estate] and counterclaims which are part and parcel of the claims allowance process, by their nature, could arise only in the context of a bankruptcy case since absent the bankruptcy case, the claims allowance process would not exist"); *Robino*, 243 B.R. at 493 ("arising in" proceedings include "the filing of proofs of claims" and "counterclaims by the bankruptcy estate against filed claims" because such proceedings "would not exist outside of bankruptcy"); *In re Manville Forest Prods. Corp.*, 896 F.2d 1384, 1390 (2d Cir. 1990) (although state-law rights underlying proofs of claim are enforceable in state court absent a bankruptcy, " 'the

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A compulsory counterclaim, in particular, necessarily "arises in" the bankruptcy case because the debtor *must* file it in the bankruptcy case; if the debtor fails to assert it and the creditor's claim is successful, res judicata bars its subsequent assertion. 10 Alan N. Resnick & Henry J. Sommer, Collier on Bankruptcy, ¶7013.02, p. 7013-2 (15th ed. 2010); *Baker v. Gold Seal Liquors, Inc.*, 417 U.S. 467, 469 n.1 (1974) ("[a] counterclaim which is compulsory but is not brought is thereafter barred").

2. Legislative history.

The legislative history confirms that Congress meant what §157(b)(2)(C)'s plain language says.

Congress intended for the 1984 Act to codify judiciary-created emergency bankruptcy rules enacted in *Marathon*'s wake. 1 Collier on Bankruptcy, *supra*, ¶3.10[2][b], at 3-99; *see* 130 Cong. Rec. 6045, 6241-44 (1984) (statements of co-sponsor Reps. Kastenmeier and Kindness). Those rules prohibited bankruptcy courts from entering final judgments in "related proceedings," which included "claims brought by the estate against parties *who have not filed claims against the estate*" and did "*not* include . . . counterclaims by the estate in whatever amount

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nature of the state proceeding would be different from the nature of the proceeding following the filing of a proof of claim' "; a claim against the estate is a core proceeding because " 'it could arise only in the context of bankruptcy' ").

against persons filing claims against the estate." 1 Collier on Bankruptcy, *supra*, ¶3.10[2][b], at 3-96, 3-97 n.15 (emphasis added). Congress codified that same principle – such counterclaims are not "related proceedings" – by defining them as core in §157(b)(2)(C).[12]

The legislative history demonstrates that Congress believed its mandate was constitutional. As the 1984 Act's co-sponsors explained,

> *Marathon* held only that: First, bankruptcy courts were not true adjuncts of the district courts because the district courts had no control over them; and second, a separate nonarticle III court could not properly decide State law claims that were not *integral to the core bankruptcy function of restructuring debtor-creditor rights*.

130 Cong. Rec. 6046 (co-sponsor Rep. Kastenmeier) (emphasis added); *see also id.* at 6242 (co-sponsor Rep. Kindness: "*Marathon* was concerned with a very limited kind of proceeding. . . . It was not concerned even with all bankruptcy proceedings involving

[12] The legislative history confirms Congress' intent that bankruptcy courts could render final judgment in *all* core proceedings. *See*, *e.g.*, 130 Cong. Rec. 6045 (Rep. Kastenmeier: the bill "authorizes bankruptcy judges to decide all core bankruptcy proceedings"); *id.* at 6242 (Rep. Kindness: "Bankruptcy judges will be able to enter a final judgment in much the same way as an article 3 judge would in all proceedings integral to the core bankruptcy functioning of restructuring the obligations of the debtor and his creditors").

questions of State law in some way. It was concerned only with State law issues that did not arise in the core bankruptcy function *of adjusting debtor-creditor rights*.") (emphasis added).

The co-sponsors emphasized the *Marathon* plurality's statements that (a) Congress has broad power when it creates statutory rights; and (b) bankruptcy adjudications and the adjustment of debtor-creditor rights are matters of federal law. *See id.* at 6046-47 (quoting *Marathon*, 458 U.S. at 83, 84 n.36); *see also* §I.B.1 & n.10, *ante*. The co-sponsors explained that in contrast to the claims at issue in *Marathon*, which arose entirely under state law, core bankruptcy proceedings "arise under Federal law" even where they "involve incidental questions of State law" because the proceedings are "integral to the restructuring of debtor-creditor rights." 130 Cong. Rec. 6046; *see also id.* (Rep. Kastenmeier stating that "[t]he Supreme Court previously held in *Katchen* . . . that State common law actions become transformed into Federal bankruptcy matters when brought in proceedings integral to a bankruptcy case"), *id.* at 6047 ("[s]tate law issues that arise in the course of restructuring debtor-creditor rights may be decided by a bankruptcy judge" because "[t]hese are core bankruptcy proceedings").

> In this respect, State law rights arising in core bankruptcy proceedings are functionally equivalent to congressionally created rights, because Congress has the power to modify State law rights in bankruptcy

> proceedings. . . . Indeed, the very purpose of bankruptcy is to modify the rights of the debtors and creditors, and the bankruptcy code authorizes the bankruptcy court to abrogate or modify State-created obligations in many ways.

Id. at 6047 (Rep. Kastenmeier); *see also id.* at 6243 (Rep. Kindness: *Marathon* "dealt only with noncore bankruptcy proceedings that arise under State law, outside of the bankruptcy estate, outside of but related to the bankruptcy estate").

Congress believed that *almost all proceedings* before bankruptcy judges – the co-sponsors said 95% – would be core. *Arnold Print Works*, 815 F.2d at 168-69 (Breyer, J.); *see* 130 Cong. Rec. 6045, 6047, 6240, 6242-43 (95% core); *see also id.* at 6241 (Rep. Kastenmeier: *Marathon* "held that only a narrow class of matters taken up in some bankruptcy cases could not be decided by an article I judge").[13]

The legislative history thus demonstrates that Congress, based on its reading of *Marathon*, understood that core jurisdiction constitutionally exists over all counterclaims to proofs of claim because –

[13] Representative Kastenmeier also explained that core bankruptcy jurisdiction "is broader than the summary jurisdiction of the bankruptcy courts under pre-1978 law" because "[c]ore proceedings include all those in which the right to relief is created by Federal law, whether or not the proceeding concerns property in the possession or constructive possession of the trustee." 130 Cong. Rec. 6045.

in contrast to the claim against the non-creditor third party in *Marathon* – such counterclaims are part of the core bankruptcy function of restructuring and adjusting debtor-creditor rights and they therefore arise under federal law even where the underlying claims involve rights created by state law.

D. The Ninth Circuit Approach Nullifies Congress' Intent.

1. The opinion below ignores §157(b)(2)(C)'s plain language and legislative history.

The opinion makes no legitimate attempt to reconcile its narrow construction of §157(b)(2)(C) with the statute's plain language and legislative history. Instead, it simply states that an expansive reading would "arguably be inconsistent with the Congress' intent to revise the Bankruptcy Code in a manner consistent with the principles of *Marathon* to make its jurisdictional grant constitutional." App. 46; *see also* App. 50 (stating its narrow construction comports with "Congress' desire to revise the Bankruptcy Code in a manner consistent with the Constitution").

But as this Court recognized in *Schor*, 478 U.S. 833, rejecting a circuit court's similar effort to straightjacket a counterclaim statute under *Marathon*, the canon that courts should construe statutes to avoid constitutional questions "does not give a court the prerogative to ignore the legislative will in order to avoid constitutional adjudication." 478 U.S. at 841;

see also Mankin, 823 F.2d at 1301 & n.3 (Ninth Circuit noting that although the canon that constitutional problems are to be avoided in construing statutes is apt in construing §157(b)(2)'s two catch-all provisions, subsections (A) and (O), the more apt principle in construing subsections (B)-(N) is "that the will of the legislature underlying the provision is not to be ignored").

The legislative history confirms that Congress believed that §157(b)(2)(C), as written, is constitutional under *Marathon*. By re-formulating the statute to comport with its own view of constitutionality, the Ninth Circuit impermissibly bypassed and directly contravened congressional intent.

2. The opinion below reduces §157(b)(2)(C) to surplusage.

The opinion violates cardinal rules of statutory construction in re-writing §157(b)(2)(C). Citing this Court's precedent, the opinion acknowledges that courts should avoid construing statutes "'in a manner that is strained and, at the same time, would render a statutory term superfluous.'" App. 43-44 (citing *United Sav. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 370-71 (1988) and *Dole Food Co. v. Patrickson*, 538 U.S. 468, 477 (2003)). It applies that rule to reject Pierce's contention that Vickie's counterclaim is non-core because it could have been brought in state court and is not bankruptcy-specific, reasoning "[w]e do not believe that

Congress intended §157(b)(2)(C) to be a meaningless (or near meaningless) provision, which is what it would become under Pierce Marshall's overly restrictive approach." App. 43-44.

But the opinion, perversely, then adopts a core-jurisdiction test that renders §157(b)(2)(C) meaningless. By prohibiting core jurisdiction over a compulsory counterclaim unless it is necessary to determine the allowance or disallowance of the creditor claim and raises no issues outside that claim, the opinion makes §157(b)(2)(C) superfluous, because Congress already specified in §157(b)(2)(B) that core proceedings include the "allowance or disallowance of claims against the estate."

If Congress had intended to limit core counterclaim jurisdiction to the mere allowance/disallowance of creditor claims, as the opinion holds, it would not have included a separate counterclaim provision.

3. The opinion below flouts the congressional goals of efficient and expeditious bankruptcies.

Congress enacted the 1984 Act "to reduce substantially the time-consuming and expensive litigation regarding a bankruptcy court's jurisdiction over a particular proceeding" and to ensure "the efficient and expeditious resolution of all matters connected to the bankruptcy estate." *In re Fietz*, 852 F.2d 455, 457 (9th Cir. 1988).

It "'realized that the bankruptcy court's jurisdictional reach was essential to the efficient administration of bankruptcy proceedings and intended that the 'core' jurisdiction would be construed as broadly as possible subject to the constitutional limits established in *Marathon*.'" *In re CBI Holding Co.*, 529 F.3d 432, 459-60 (2d Cir. 2008). "By specifically including as core proceedings counterclaims brought by a debtor as a result of claims filed by creditors against the estate, Congress apparently believed that it is more efficient having a single court decide all cases based on the same facts and circumstances." *In re Fang Operators*, 158 B.R. 643, 647 (Bankr. N.D. Tex. 1993).

The Ninth Circuit's construction of §157(b)(2)(C) scuttles these goals. If upheld, it would:

- render most counterclaims non-core, because compulsory counterclaims (and permissive counterclaims even more so) will rarely "essentially merge" with the creditor's claim in terms of proof, as the Ninth Circuit's test requires;
- splinter the determination of creditor claims against the estate and compulsory counterclaims into different forums;
- produce the absurd result that debtors must file compulsory counterclaims in bankruptcy courts that cannot finally adjudicate them;

- swamp bankruptcy and district courts with abstention and withdrawal motions; and
- spawn endless litigation and confusion over jurisdictional limits and claim and issue preclusion, because district courts would end up determining counterclaims that are legally and factually interconnected to creditor claims adjudged by the bankruptcy court.

This mayhem is not what Congress intended.

* * *

In sum, §157(b)(2)(C)'s plain language and legislative history demonstrate that Congress intended to confer on bankruptcy courts core jurisdiction over all estate counterclaims against persons filing claims against the estate. While the legislative grant includes permissive counterclaims, the only constitutional question before this Court – based on the Ninth Circuit's holding and the specific questions on which certiorari was granted – is the constitutionality of bankruptcy courts hearing and deciding all *compulsory* counterclaims.[14] We now demonstrate that

[14] We also are mindful of Justice Rehnquist's warning in *Marathon*: "Particularly in an area of constitutional law such as that of 'Art. III Courts,' with its frequently arcane distinctions and confusing precedents, rigorous adherence to the principle that this Court should decide no more of a constitutional question than is absolutely necessary accords with both our decided cases and with sound judicial policy." *Marathon*, 458 U.S. at 90 (Rehnquist, J., concurring).

Congress was correct that its grant of core jurisdiction over compulsory counterclaims to proofs of claim is constitutional.

II. SECTION 157(b)(2)(C)'S GRANT OF CORE JURISDICTION OVER ALL COMPULSORY COUNTERCLAIMS IS CONSTITUTIONAL.

Article III, section 1, is facially absolute: "The judicial Power of the United States, shall be vested in one Supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish" and those judges shall "hold their offices during good Behaviour" and receive compensation that "shall not be diminished. . . ." U.S. Const. art. III, § 1. Article I is equally unlimited on its face in defining responsibility and power reserved exclusively to Congress, including the power to establish "uniform Laws on the subject of Bankruptcies throughout the United States." U.S. Const. art. I, § 8.

This Court "has long recognized that Congress is not barred from acting pursuant to its powers under Article I to vest decisionmaking authority in tribunals that lack the attributes of Article III courts." *Thomas v. Union Carbide Agr. Prods. Co.*, 473 U.S. 568, 583 (1985). Thus, there is a long history of decisionmaking by judges lacking Article III's tenure and compensation guarantees, including in territorial courts, military courts, legislative courts, agency commissions, and bankruptcy proceedings.

"The cases dealing with the authority of Congress to create courts other than by use of its power under Art. III do not admit of easy synthesis." *Marathon*, 458 U.S. at 91 (Rehnquist, J., concurring). *Marathon* did not definitively resolve the line-drawing conundrum as to when non-Article III judges are constitutionally permissible. *See id.* (concurrence declining to assess whether precedent supports "a general proposition and three tidy exceptions, as the plurality believes"); *id*. at 104 (White, J., dissenting) (describing the plurality's attempt to "cabin the domain of Art. I courts" into three narrow exceptions as "quite unrealistic" and belied by its adjunct-court discussion).

Nor has this Court's post-*Marathon* precedent clarified the uncertainty. *See*, *e.g.*, *Schor*, 478 U.S. at 847 ("our precedents in this area do not admit of easy synthesis"); *Thomas*, 473 U.S. at 583 ("[a]n absolute construction of Article III is not possible in this area of 'frequently arcane distinctions and confusing precedents'").

Given the absence of a precedential synthesis, we show below that §157(b)(2)(C)'s grant of core jurisdiction over all compulsory counterclaims is constitutional under this Court's various announced theories and considerations, whether viewed individually or collectively.

A. Creditors Who Submit Claims Against The Estate To The Non-Article III Bankruptcy Court Invoke That Court's Equitable Jurisdiction To Resolve All Compulsory Counterclaims.

1. *Marathon* did not alter the basic principle that the filing of a proof of claim invokes the special rules of bankruptcy.

Although some lower courts at first construed *Marathon* as broadly invalidating non-Article III adjudications, this Court quickly clarified that *Marathon*'s constitutional strictures are narrow and that the *Marathon* concurrence – whose conclusion solely turned on the fact that the case involved a debtor's common law claims against a non-creditor defendant that were only peripherally related to the bankruptcy case – established the holding. *See Thomas*, 473 U.S. at 584 (noting the "divided [*Marathon*] Court was unable to agree on the precise scope and nature of Article III's limitations" and the holding "establishes only that Congress may not vest in a non-Article III court the power to adjudicate, render final judgment, and issue binding orders in a traditional contract action arising under state law, without consent of the litigants, and subject only to ordinary appellate review"); *Schor*, 478 U.S. at 838-39, 847-48 (same).

In so doing, the Court effectively confirmed that Congress was correct in narrowly construing *Marathon*'s constitutional strictures when enacting the 1984 Act. *See In re Kaiser Steel Corp.*, 95 B.R. 782,

787 (Bankr. D. Colo. 1989) ("The holdings of *Schor* and *Thomas* in the bankruptcy setting had, in fact, been anticipated by Congress in the enactment of 28 U.S.C. §157(c)(2)").

The crucial distinction is that *Marathon* did not involve a debtor's counterclaim to a proof of claim. As the Second Circuit recently summarized, *Marathon* merely held that "a non-Article III bankruptcy judge could not adjudicate a pre-petition contract dispute arising under state law against a party that had not filed a proof of claim and was not otherwise related to the bankruptcy proceedings," and *Marathon* distinguished that type of dispute from " 'the restructuring of debtor-creditor relations, which is at the core of the federal bankruptcy power.' " *CBI*, 529 F.3d at 459-60 (emphasis added); *see also In re SG Philips Constructors, Inc.*, 45 F.3d 702, 706 (2d Cir. 1995) (the *Marathon* defendant was "involuntarily subjected to having the debtor's state law claim against it decided by an Article I judge" because it "had not filed a proof of claim and had no other connection with the bankruptcy").

Nothing in *Marathon* " 'alters the basic principle that the filing of a proof of claim invokes the special rules of bankruptcy. . . .' " *CBI*, 529 F.3d at 462; *see id.* at 437-38, 442, 459-65 (upholding core jurisdiction over $70 million tort and contract counterclaims filed against $210,000 proof of claim for unpaid services).

2. This Court's post-*Marathon* decisions confirm the constitutionality of non-Article III bankruptcy judges resolving all compulsory counterclaims to proofs of claim.

a. *Granfinanciera* and *Langenkamp*.

In *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989), this Court held that Congress could not deprive defendants who had not filed proofs of claim of their jury-trial right on a trustee's fraudulent conveyance action, reasoning that the "fraudulent conveyance action does not arise 'as part of the process of allowance or disallowance of claims'" and is not "integral to the restructuring of debtor-creditor relations." *Id.* at 58; *see also id.* at 60 (fraudulent conveyance actions are "not integrally related to the reformation of debtor-creditor relations").

The Court cited *Katchen* as "mak[ing] clear" that "by submitting a claim against the bankruptcy estate, creditors subject themselves to the [bankruptcy] court's equitable power to disallow those claims, even though the debtor's opposing counterclaims are legal in nature and the Seventh Amendment would have entitled creditors to a jury trial had they not tendered claims against the estate." *Id*. at 59 n.14. Thus, while non-Article III bankruptcy courts can resolve debtors' preference or fraudulent conveyance claims when they arise as counterclaims to proofs of claim, a jury-trial right exists if the defendant never filed a proof of claim. *See id.* at 56-59, comparing *Schoenthal v.*

Irving Trust Co., 287 U.S. 92 (1932) (no proof of claim) to *Katchen*, 382 U.S. 323 (proof of claim filed).

The *Granfinanciera* court analogized the fraudulent conveyance action to the debtor's claims against the non-creditor defendant in *Marathon*, in that it did not involve creditors' "claims to a pro rata share of the bankruptcy res" and "more nearly resemble[d] state-law contract claims brought by a bankrupt corporation to augment the bankruptcy estate." *Granfinanciera*, 492 U.S. at 56. Because the defendants in the fraudulent conveyance action had not filed a claim against the estate, the Seventh Amendment entitled them to a jury trial notwithstanding Congress' designation of fraudulent conveyance actions as "core proceedings." *Id.* at 36.

Langenkamp v. Culp, 498 U.S. 42 (1991), decided two years later, determined the flip side of *Granfinanciera* – the defendants there did file proofs of claim, so the trustee's avoidable preference claims were filed as counterclaims to creditors' claims against the estate. 498 U.S. at 42-43. Accordingly, the Court held the creditors were not entitled to a jury trial on the counterclaims because "by filing a claim against a bankruptcy estate the creditor triggers the process of 'allowance and disallowance of claims,' thereby subjecting himself to the bankruptcy court's equitable power," and the trustee's preference counterclaim "becomes part of the claims-allowance process which is triable only in equity." 498 U.S. at

44.[15] Thus, "the creditor's claim and the ensuing preference action by the trustee become integral to the restructuring of the debtor-creditor relationship through the bankruptcy court's equity jurisdiction." *Id.* (emphasis omitted).

Although *Granfinanciera* and *Langenkamp* involved the right to jury trial, *Granfinanciera* holds that the question of whether the Seventh Amendment permits Congress to assign the adjudication of a statutory cause of action that is legal in nature "to a tribunal that does not employ juries as factfinders requires the same answer as the question whether Article III allows Congress to assign adjudication of that cause of action to a non-Article III tribunal." *Granfinanciera*, 492 U.S. at 53.

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[15] The principle that bankruptcy courts are specialized courts of equity with respect to claims allowance is well rooted in this Court's jurisprudence. *See*, *e.g.*, *Barton v. Barbour*, 104 U.S. 126, 134 (1881) ("[I]n cases of bankruptcy, many incidental questions arise in the course of administering the bankrupt estate, which would ordinarily be pure cases at law, and in respect of their facts triable by jury, but, as belonging to the bankruptcy proceedings, they become cases over which the bankruptcy court, which acts as a court of equity, exercises exclusive control. Thus, a claim of debt of damages against the bankrupt is investigated by chancery methods."); *Pepper v. Litton*, 308 U.S. 295, 307 (1939) ("the bankruptcy court in passing on allowance of claims sits as a court of equity"); *Atlas Roofing Co. v. Occupational Safety & Health Review Comm'n*, 430 U.S. 442, 454 n.11 (1977) (as recognized in *Curtis v. Loether*, 415 U.S. 189, 194-95 (1974) and *Katchen*, "a bankruptcy court, exercising its summary jurisdiction, was a specialized court of equity").

Thus, although Justice Brennan noted in the *Marathon* plurality that *Katchen* did not discuss "the Art. III issue" (*Marathon*, 458 U.S. at 79 n.31, plurality opinion), he later explained in *Granfinanciera* that bankruptcy jury-trial decisions such as *Katchen*, *Granfinanciera* and *Langenkamp* are germane to the Article III issue. *See also Curtis*, 415 U.S. at 195 (citing *Katchen* as upholding "congressional power to entrust enforcement of statutory rights to an administrative process or specialized court of equity free from the strictures of the Seventh Amendment").

Katchen, *Granfinanciera* and *Langenkamp* all support the constitutionality of non-Article III bankruptcy judges resolving all compulsory counterclaims to proofs of claim. Compulsory counterclaims to proofs of claim necessarily arise "as part of the process of allowance or disallowance of claims" and are "integral to the restructuring of the debtor-creditor relations," the same as the preference and fraudulent conveyance counterclaims at issue in *Katchen* and *Langenkamp*. *See In re Yagow*, 53 B.R. 737, 740 (Bankr. D.N.D. 1985) ("[a] counterclaim, compulsory in nature, is the type of counterclaim which would be considered integral"); *In re Beugen*, 81 B.R. 994, 1000 (Bankr. N.D. Cal. 1988) ("[a] compulsory counterclaim against a creditor that has asserted a claim is closely connected to the central bankruptcy function of determining claims"); *Asousa P'ship*, 276 B.R. at 66 ("counterclaims that could affect the allowance or disallowance of a proof of claim are part and parcel of the claims allowance process").

By definition, compulsory counterclaims arise out of the same transaction that the creditor, by filing the proof of claim, submitted to the bankruptcy court for resolution and constitute potential affirmative defenses to the creditor's claim. Here, for example, success on Vickie's counterclaim for tortious interference with gift would necessarily defeat Pierce's proof of claim by establishing the affirmative defense of truth to the defamation allegations. App. 47-48, 55. Moreover, compulsory counterclaims – since they arise from the same transaction as the claim that triggered their filing – fall within a court's ancillary jurisdiction and need no independent jurisdictional basis. *Baker v. Gold Seal Liquors*, *Inc.*, 417 U.S. at 469 n.1. Proofs of claim and the bankruptcy estate's resulting compulsory counterclaims are two halves of a single dispute.

b. *Schor*.

In *Schor*, this Court effectively recognized that *Katchen*'s analysis of preference counterclaims extends to all compulsory counterclaims. In upholding the constitutionality of Congress authorizing non-Article III commissioners of the Commodity Futures Trading Commission to adjudicate counterclaims "'aris[ing] out of the transaction or occurrence or series of transactions or occurrences set forth in the complaint,'" the Court observed that such jurisdiction was "not without precedent" because *Katchen* upholds "a bankruptcy referee's power to hear and decide state law counterclaims against a creditor who filed a

claim in bankruptcy when those counterclaims arose out of the same transaction." *Schor*, 478 U.S. at 833, 852; *see also Marathon*, 458 U.S. at 97 n.4 (White, J., dissenting) (*Katchen* recognizes "that when a creditor files a claim, the [bankruptcy] referee is empowered to hear and decide a counterclaim against that creditor arising out of the same transaction").

3. In addition, longstanding precedent holds that creditors, by submitting claims against the estate to a non-Article III bankruptcy court for adjudication, invoke that court's equitable power to resolve the entire dispute and issue complete relief.

Core jurisdiction over all compulsory counterclaims is equally compelled by the fact that bankruptcy courts "passing on allowance of claims" sit as courts of equity and therefore apply "principles and rules of equity jurisprudence." *Pepper v. Litton*, 308 U.S. at 305-07; *accord*, *Katchen*, 382 U.S. at 334-38; *see also Young v. United States*, 535 U.S. 43, 50 (2002) (bankruptcy courts "are courts of equity and 'appl[y] the principles and rules of equity jurisprudence' ").

A fundamental principle of equity jurisprudence, as recognized and followed in *Katchen*, is that courts of equity " 'having jurisdiction of the parties to controversies brought before them, they will decide all matters in dispute and decree complete relief.' " *Katchen*, 382 U.S. at 335 (quoting *Alexander v. Hillman*, 296 U.S. 222, 241-42 (1935)). *Katchen* held that

the rationale of *Alexander v. Hillman*, a receivership case, was "equally applicable" to the bankruptcy referee's power to hear and decide the trustee's preference counterclaim. *Katchen*, 382 U.S. at 335-36; *see Granfinanciera*, 492 U.S. at 59 n.14 (noting *Katchen* "adopted a rationale articulated in *Alexander v. Hillman*").

Hillman involved an equity receivership created for the purposes of liquidating a corporation and distributing its assets. 296 U.S. at 230. After officers of the corporation filed claims to share in distribution of the receivership res, the receiver counterclaimed for affirmative relief, alleging the claimant-officers fraudulently diverted corporate funds for their own benefit and received excessive salaries. *Id.* at 235-36. The officers argued they were entitled to plenary determination of the counterclaims in the state of their residence. *Id.* at 236, 238.

This Court held that the officers, by filing claims to participate in the receivership res, "subjected themselves to all the consequences that attach to an appearance." *Id.* at 241. The receivership court therefore could adjudicate the counterclaims to "decide all matters in dispute and decree complete relief," even though the counterclaims exceeded the officers' claims against the receivership res. *Id.* at 242-43. This Court rejected the argument that the receiver must split the causes of action by adjudicating the counterclaims only to the extent they are "purely defensive" and "go to another court to recover the rest." *Id*.

In *Katchen*, this Court recognized that the *Hillman* rationale equally applied to summary proceedings before bankruptcy referees, and that bankruptcy referees are empowered to issue affirmative relief on preference counterclaims, even if the amount exceeds the proof of claim. *See Granfinaciera*, 492 U.S. at 59 n.14 (noting *Katchen* stands for the proposition that, once a creditor files a claim against the bankruptcy estate, the trustee may recover the full amount of any preference, "even if that amount exceeds the amount of the creditor's claim").

Katchen recognized that, just as the *Hillman* claimants could not invoke the receivership court's equity jurisdiction by filing claims against the res but then preclude that court from resolving the entire dispute, so too a creditor cannot invoke the aid of the bankruptcy referee by filing a claim against the bankruptcy estate but then deny that court the ability to decide the entire dispute and issue complete relief. *Katchen*, 382 U.S. at 335-36.

This rationale applies equally to all compulsory counterclaims to proofs of claim.[16] In stark contrast to

[16] Circuit courts, construing the 1898 Bankruptcy Act, recognized that *Hillman*'s rationale supported summary jurisdiction over compulsory counterclaims to proofs of claim. *See*, *e.g.*, *Florance v. Kresge*, 93 F.2d 784, 786 (4th Cir. 1938); *Floro Realty & Inv. Co. v. Steem Elec. Corp.*, 128 F.2d 338, 340-41 (8th Cir. 1942); *In re Solar Mfg. Corp.*, 200 F.2d 327, 329-31 (3d Cir. 1952); *Conway v. Union Bank of Switz.*, 204 F.2d 603, 607 (2d Cir. 1953); *Cont'l Cas. Co. v. White,* 269 F.2d 213, 214-15 (4th Cir. 1959); *Inter-State Nat'l Bank of Kansas City v. Luther*, 221

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the non-creditor in *Marathon* whom the debtor involuntarily dragged into the bankruptcy, a creditor cannot ask the bankruptcy court to determine its right to distribution from the bankruptcy estate, while denying that court the ability to resolve the entire dispute and issue complete relief. By invoking the aid of the bankruptcy court, the creditor "risk[s] all of the disadvantages which may flow to him as a consequence, as well as gaining all of the benefits." *Case v. L.A. Lumber Prods. Co.*, 308 U.S. 106, 126-27 (1939). "A debtor as well as a creditor who invokes the aid of the federal courts in reorganization or rehabilitation . . . assumes all of the consequences which flow from that jurisdiction. Once the property is in the hands of the court private rights as respect that res are subject to the superior dominion of the court and are to be adjudicated pursuant to the standards prescribed by the Congress." *Id.* at 125.[17]

F.2d at 388-89; *In re Carnell Constr. Corp.*, 424 F.2d at 298-99; *In re L.A. Land & Invs. Ltd.*, 447 F.2d 1366, 1367 (9th Cir. 1971).

[17] *See also Wiswall v. Campbell*, 93 U.S. 347, 351 (1876) ("Every person submitting himself to the jurisdiction of the bankrupt [sic] court in the progress of the cause, for the purpose of having his rights in the estate determined, makes himself a party to the suit, and is bound by what is judicially determined in the legitimate course of the proceeding. A creditor who offers proof of his claim, and demands its allowance, subjects himself to the dominion of the court, and must abide the consequences.").

B. Core Jurisdiction Over All Compulsory Counterclaims To Proofs Of Claim Is Constitutional Under The *Thomas*/*Schor* "Purposes Of Article III" Approach.

In *Thomas*, after noting the justices could not agree on Article III's scope in *Marathon*, this Court mandated that "practical attention to substance rather than doctrinaire reliance on formal categories should inform application of Article III" and that courts must consider the "concerns guiding the selection by Congress of a particular method for resolving disputes" when "assessing the degree of judicial involvement required by Article III." 473 U.S. at 569, 587.

The next year, in *Schor,* the Court similarly rejected "formalistic and unbending rules" that might "unduly constrict Congress' ability to take needed and innovative action pursuant to its Article I powers." 478 U.S. at 851; *see also id.* at 857 ("bright-line rules cannot effectively be employed"). It held that "the constitutionality of a given congressional delegation of adjudicative functions to a non-Article III body must be assessed by reference to the purposes underlying the requirements of Article III" and therefore "due regard must be given in each case to the unique aspects of the congressional plan at issue and its practical consequences in light of the larger concerns that underlie Article III." *Schor*, 478 U.S. at 847, 857.

Core jurisdiction over all compulsory counterclaims is constitutional under the *Thomas*/*Schor* approach of focusing on the purposes of Article III.

1. Core jurisdiction over all compulsory counterclaims is fair to creditors who seek to share in the bankruptcy estate.

Article III, section 1's "guarantee of an independent and impartial adjudication by the federal judiciary of matters within the judicial power of the United States . . . serves to protect primarily personal, rather than structural, interests." *Schor*, 478 U.S. at 848. It "does not confer on litigants an absolute right to the plenary consideration of every nature of claim by an Article III court." *Id*.

Although proofs of claim can only be filed in the bankruptcy case, creditors do not have to file proofs of claim at all. If concerned about defending compulsory counterclaims in the bankruptcy court, creditors can opt not to seek recovery from the bankruptcy estate. "[M]any creditors do not file claims" and the fact that a creditor might find unattractive the choice between submitting to the bankruptcy court's jurisdiction and foregoing a claim against the estate to avoid that jurisdiction "does not convert the choice into an

involuntary decision." *In re Lazar*, 200 B.R. 358, 380 (Bankr. C.D. Cal. 1996).[18]

A creditor's decision to file a proof of claim triggers the "traditional bankruptcy law that he who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance must abide the consequences of that procedure." *Gardner v. New Jersey*, 329 U.S. 565, 573 (1947) (by choosing to file proof of claim, government waived sovereign immunity as to claim's adjudication). Creditors cannot invoke the aid of the bankruptcy court, seeking the benefits of the bankruptcy process, and at the same time prevent that court from resolving the entire dispute that the proof of claim placed at issue. *See* §II.A.3, *ante*.[19] As courts construing the 1898

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[18] *See*, *e.g.*, *In re Applied Thermal Sys., Inc.*, 294 B.R. 784, 791 (Bankr. N.D. Okla. 2003) ("if [the creditor] was concerned about defending counterclaims in bankruptcy court, it should have foregone filing its proof of claim against the estate of [the debtor]"); *In re Lion Country Safari, Inc. Cal.*, 124 B.R. 566, 572 (Bankr. C.D. Cal. 1991) ("The filing of a proof of claim by a creditor is 'voluntary' in the sense that a creditor is not required to file a proof of claim, and pursue it within the bankruptcy court"); *In re Wiener Pharms., Inc.*, No. 086-60909-21, 1988 Bankr. LEXIS 1097, at *16 (Bankr. E.D.N.Y. June 20, 1988) ("To call it jurisdiction by ambush is simply to use pejorative terms for what is the well known consequence of filing a claim. The defendants here could have avoided the jurisdiction of the bankruptcy court by refraining from asserting a right to share in the distribution of the debtor's estate.").

[19] This Court has similarly recognized in non-bankruptcy contexts that a plaintiff, who "by his voluntary act in demanding justice from the defendant, submitted himself to the jurisdiction

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Bankruptcy Act stated in upholding summary jurisdiction over compulsory counterclaims to proofs of claim:

> No party can invite summary adjudication on only part of the relevant evidence relating to the subject matter of the claim. . . . [I]f you invite a Bankruptcy Court to review a set of facts for your benefit, you invite it to review all pertinent related facts even though they tend to prove your opponent's case.

Majestic Radio & Television Corp., 227 F.2d at 156; *accord*, *Peters v. Lines*, 275 F.2d at 924-25 ("[i]n submitting one side of a controversy for resolution logic dictates that the entire controversy should be open for resolution").[20] Nor can creditors, given

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of the court, there is nothing arbitrary or unreasonable in treating him as being there for all purposes," including counterclaims. *Adam v. Saenger*, 303 U.S. 59, 67-68 (1938); *accord*, *Frank L. Young Co. v. McNeal-Edwards Co.*, 283 U.S. 398, 400 (1931) (where the plaintiff is already in court by "'his own voluntary act, it is reasonable to treat him as being there for all the purposes for which justice requires his presence'"); *Gen. Elec. Co. v. Marvel Rare Metals Co.*, 287 U.S. 430, 435 (1932) ("[t]he setting up of a counterclaim against one already in a court of his own choosing is very different, in respect to venue, from hailing him into that court").

[20] Pre- and post-*Marathon*, lower courts often describe this principle as meaning creditors "impliedly consent" to compulsory-counterclaim adjudication. *See*, *e.g.*, *Applied Thermal Sys.*, 294 B.R. at 788-89 & n.15; *Asousa P'ship*, 276 B.R. at 66-67; *Beugen*, 81 B.R. at 1001; *In re STN Enters.*, 73 B.R. 470, 483 (Bankr. D. Vt. 1987); *In re Sun West Distribs.*, 69 B.R. 861, 864-65 (Bankr. S.D. Cal. 1987). But it is more a matter of creditors being bound

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§157(b)(2)(C)'s express language, legitimately claim surprise that their proof of claim triggered core jurisdiction over all compulsory counterclaims – claims the debtor must file to avoid relinquishing forever.[21]

Pierce, for example, admitted in his bankruptcy-court filings that "[a] review of [Vickie's] counterclaim demonstrates that the defamatory statements and the challenged transactions at issue in [Pierce's] Defamation Action are at the heart of [Vickie's] causes of action against [Pierce]. . . ." JA 107; *see also* App. 275 (district court emphasizing Pierce's statement that the defamation claim and Vickie's counterclaim were "both halves" of the same action). Pierce cannot cry foul over the bankruptcy court

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by the benefits and burdens of the bankruptcy process they invoked by seeking a share of the bankruptcy res.

[21] As this Court said long ago, in the context of upholding the Court of Claims' power to issue relief on counterclaims:

> Congress, by the act in question, informs the claimant that if he avails himself of the privilege of suing the government in the special court organized for that purpose, he may be met with a set-off, counter-claim, or other demand of the government, upon which judgment may go against him, without the intervention of a jury, if the court, upon the whole case, is of the opinion that the government is entitled to such judgment. If the claimant avails himself of the privilege thus granted, he must do so subject to the conditions annexed by the government to the exercise of the privilege.

McElrath v. United States, 102 U.S. 426, 440 (1880).

adjudicating the entire dispute that his proof of claim placed at issue.[22]

2. Core jurisdiction over all compulsory counterclaims comports with historical standards and poses *de minimis* separation-of-powers concerns under the current bankruptcy law.

Schor and *Thomas* "turned to history and tradition to help define the type of adjudicatory proceeding that the Constitution reserves exclusively for Article III Courts." *Arnold Print Works*, 815 F.2d at 169 (Breyer, J.). A historical definition supports core jurisdiction over all compulsory counterclaims, since "[c]ounterclaims arising from the same transaction as the creditor's claim have also been traditionally adjudicated by non-Article III bankruptcy judges." *Beugen*, 81 B.R. at 1000; *see Marathon*, 458 U.S. at 97-100 & n.4 (White, J., dissenting) (historical discussion); *Schor*, 478 U.S. at 852; §1.A.1, *ante*.

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[22] That is particularly true given that Pierce would not have been left empty-handed had he opted against filing a proof of claim. He filed both (1) a proof of claim, to obtain a recovery from Vickie's bankruptcy estate on his defamation claim, and (2) a nondischargeability complaint, to obtain a judgment against Vickie personally that would survive the bankruptcy discharge. He could have avoided core jurisdiction under §157(b)(2)(C) entirely by seeking only a nondischargeability ruling. Pierce is bound by his tactical choices.

Further, "[t]here is no constitutional right to obtain a discharge of one's debts in bankruptcy." *United States v. Kras*, 409 U.S. 434, 446 (1973). Nor is there any constitutional or common law right to file proofs of claim in bankruptcies, to request participation in bankruptcy estates, or to seek the adjustment of debtor-creditor rights. Rather, the statutory scheme of allowing debtors to obtain a discharge of debts "is a legislatively created benefit" stemming from Congress' "plenary and exclusive" power over bankruptcy. *Id.* at 447; *see also id.* (noting Congress could have delegated "to an administrative agency," rather than a court, the responsibility for processing petitions for discharge).

In light of Congress' plenary Article I power, this Court previously rejected an Article III challenge to Congress' decision to delegate to an administrative agency (the Interstate Commerce Commission) certain bankruptcy decisionmaking involving the rights of debtors and creditors in railroad reorganizations. *RFC v. Bankers Trust Co.*, 318 U.S. 163, 168-70 (1943). It recognized that there was no reason why the specialized factfinding "should not be litigated, as are other claims against bankrupt estates, by such machinery and in such manner as Congress shall prescribe. . . ." *Id.* at 170; *see id.* at 175 (Douglas, J., concurring) ("that Congress has customarily entrusted administration of the various bankruptcy acts to the courts does not mean that it must do so").

Accordingly, claims allowance and the adjustment of the debtor-creditor relationship is a scheme

of congressionally-created rights involving a specialized area where Congress has plenary Article I power. It is a distinctly federal scheme, even though the underlying bankruptcy adjudications between debtors and creditors may involve the adjustment of rights created under state law. *See Schor*, 478 U.S. at 852 (citing *RFC*, 318 U.S. 163, as upholding a non-Article III agency adjudicating state law claims that are "ancillary to a federal law dispute"); *Schor*, 478 U.S. at 856 (emphasizing that "[t]he CFTC adjudication of common law counterclaims is incidental to, and completely dependent upon, adjudication of reparations claims created by federal law"); *id.* at 853 (emphasizing that the non-Article III commission in *Schor* and non-Article III agency in *Crowell v. Benson*, 285 U.S. 22 (1932) deal "with a 'particularized area of law'").

As the *Marathon* plurality recognized, "when Congress creates a substantive federal right, it possesses substantial discretion to prescribe the manner in which that right may be adjudicated," including requiring persons seeking to vindicate those rights to "do so before particularized tribunals created to perform the specialized adjudicative tasks related to that right," even if they perform factfinding and other "functions historically performed by judges." *Marathon*, 458 U.S. at 80-81, 83.

Core jurisdiction over all compulsory counterclaims is also appropriate in light of the concerns that motivated Congress. *See Thomas*, 473 U.S. at 587; *Schor*, 478 U.S. at 857. It promotes the expeditious

and efficient administration of claims administration and adjustment of debtor-creditor relations, considerations this Court deemed worthy in *Katchen*. *See Katchen*, 382 U.S. at 328 ("this Court has long recognized that a chief purpose of the bankruptcy laws is 'to secure a prompt and effectual administration and settlement of the estate of all bankrupts within a limited period'"); *see also Schor*, 478 U.S. at 855 (Congress authorized the CFTC to adjudicate the "same transaction" counterclaims to create "an inexpensive and expeditious" forum for claims resolution).

In addition, core compulsory-counterclaim jurisdiction is appropriate in light of the concerns that underlie Article III's tenure and salary protections – preserving "to litigants their interest in an impartial and independent federal adjudication of claims within the judicial power of the United States" and preventing the executive and legislative branches from encroaching on the judiciary. *Schor*, 478 U.S. at 850; *see id.* at 856 (concluding that under the CFTC scheme, "the magnitude of any intrusion on the Judicial Branch can only be termed *de minimis*"). Compulsory counterclaim jurisdiction poses only a *de minimis* intrusion on those interests, under the current bankruptcy law.

The 1984 Act's procedural changes diminish the threat of political-branch encroachment that undergirded much of the *Marathon* plurality's concerns. *See* §§I.A.2, I.B.1, I.B.2, *ante*; *see also Mankin*, 823 F.2d at 1309; *In re Finevest Foods, Inc.*, 143 B.R. 964, 966-71 (Bankr. M.D. Fla. 1992); *In re Jennings*, 83 B.R. 752,

759-61 (D. Nev. 1988). Under the current adjunct approach, Article III judges (instead of the political branches) control the appointment and removal of bankruptcy judges, the Article III district courts have unfettered discretion to refer or withdraw bankruptcy cases, bankruptcy judges can issue only proposed findings on matters peripherally related to the bankruptcy case (such as the debtor's claim against the non-creditor in *Marathon*), and all bankruptcy court decisions are subject to *two levels* of review by Article III courts (the district court and the circuit court), plus potential discretionary review by this Court.[23]

C. Core Jurisdiction Over All Compulsory Counterclaims To Creditor Claims Against The Estate Is Constitutional Under A "Public Rights" Or A *Crowell* Adjunct-Court Theory.

1. Public rights theory.

Although the *Marathon* plurality recognized that non-Article III judges can adjudicate "public rights," it described that doctrine as applying to matters arising "'between the government and others.'" 458 U.S. at 69. This Court has since held, however, that the doctrine applies to contexts where the federal

[23] If all parties consent, the appeal from the bankruptcy court can instead be heard by a bankruptcy appellate panel comprised of three bankruptcy judges. 28 U.S.C. §158(b)(1), (5), (c)(1). The panel's decision is appealable to the Article III circuit court. *Id.*, §158(c)(2), (d)(1).

government is not a party. *Thomas*, 473 U.S. at 585-88 (O'Connor, J., majority); *id.* at 598-600 (Brennan, J., concurring); *Granfinanciera*, 492 U.S. at 54.

In cases not involving the federal government, the test to determine whether a right is a "public right" that can be relegated to a non-Article III tribunal is whether "'Congress, acting for a valid legislative purpose pursuant to its constitutional powers under Article I, [has] create[d] a seemingly "private" right that is so closely integrated into a public regulatory scheme as to be a matter appropriate for agency resolution, with limited involvement by the Article III judiciary.'" *Granfinanciera*, 492 U.S. at 54 (quoting *Thomas*, 473 U.S. at 593-94).

The statutory process of bankruptcy courts adjudicating proofs of claim and compulsory counterclaims falls squarely within this definition. This Court effectively recognized that in *Langenkamp* when it held that there was no jury-trial right because the counterclaims to proofs of claim were "part of the claims-allowance process" and therefore "integral to the restructuring of the debtor-creditor relationship through the bankruptcy courts' equity jurisdiction." 498 U.S. at 44; *see*, *e.g.*, *In re Americana Expressways*, *Inc.*, 161 B.R. 707, 711 (D. Utah 1993) ("Although the *Granfinanciera* Court equivocated on the question whether the restructuring of debtor-creditor relations is a public right, . . . it apparently affirmed this proposition in *Langenkamp*. . . . [T]he *Langenkamp* Court implicitly recognized the restructuring of the debtor-creditor relationship through the

claims allowance process as a public right"); *Applied Thermal Sys.*, 294 B.R. at 789 ("the adjudication of counterclaims in the context of claims allowance constitutes the adjudication of public rights by the bankruptcy court").[24]

2. *Crowell* adjunct-court theory.

Expansion of the public rights doctrine beyond contexts where the federal government is a party has elicited criticism. *See*, *e.g.*, *Granfinanciera*, 492 U.S. at 68-69 (Scalia, J., concurring) (arguing that the expanded version means "a purely private federally created action d[oes] not require Article III courts" and that the Court should return to requiring that the United States be a party). But that terminological battle largely stems from the conflation of adjunct-court concepts with the traditional "public rights"

[24] *See also In re Hudson*, 170 B.R. 868, 873 (E.D.N.C. 1994) ("by filing a claim with the bankruptcy court against the bankruptcy estate, a creditor places his dispute with the debtor into the arena of public rights"); *In re Lloyd Secs., Inc.*, 156 B.R. 750, 752 (Bankr. E.D. Pa. 1993) (under *Granfinanciera* and *Langenkamp*, "when a creditor presents a 'claim' against the bankruptcy estate, that creditor triggers the process of allowance and disallowance of claims, thereby . . . placing the parties' dispute into the arena of 'public rights' "); *In re Ne. Graphic Supply, Inc.*, No. 03-20069, 2003 WL 22848944, at *3 (Bankr. D. Me. 2003) ("[o]therwise legal causes of action tried in the bankruptcy court do not lose their Seventh Amendment entitlement because they are being tried in a court of equity, but rather because they are subsumed within a public rights legislative scheme for restructuring the debtor-creditor relationship").

concept that adjudications involving the federal government differ because the government can define the extent to which it waives its sovereign immunity.

In *Granfinanciera*, for example, Justice Brennan acknowledged that *Atlas Roofing*, 430 U.S. at 450 n.7, and *Crowell*, 285 U.S. at 51-65, upheld the assignment of "private rights," *i.e.*, "the liability of one individual to another under the law as defined" (*Crowell*, 285 U.S. at 51) to non-Article III adjudicators in contexts where an administrative agency or a specialized court of equity serves as a fact-finding adjunct to an Article III court. *See Granfinanciera*, 492 U.S. at 55 n.10. But he then labeled this adjunct approach as "involving statutory rights that are integral parts of a public regulatory scheme" and chose to "now refer to those rights as 'public' rather than 'private.'" *Id*.

As shown above, core jurisdiction over all compulsory counterclaims to proofs of claim fits within Justice Brennan's re-formulation of "public rights" theory. But even if one rejects that re-formulation, such core jurisdiction falls within the adjunct-court approach recognized in *Crowell*.

In *Crowell*, this Court upheld the constitutionality of a statutory scheme holding employers strictly liable in certain admiralty proceedings, under which the findings of a non-Article III commissioner, "supported by evidence and within the scope of his authority," were final as to employee injuries within the statute's purview. 285 U.S. at 46. The Court

recognized that the proceeding is "one of private right, that is, of the liability of one individual to another under the law as defined," and did not fall within any of the Court's prior categories for upholding non-Article III adjudications, including public rights cases. *Id.* at 51.

Nonetheless, it upheld the commissioner's authority to determine all "questions of fact as to the circumstances, nature, extent, and consequences of the injuries sustained by the employee for which compensation is to be made in accordance with the prescribed standards," emphasizing that the district court retained full authority over all matters of law, including determining whether evidence in the record supported the commissioner's award. *Id.* at 46-48, 54. The Court also concluded that the district court must independently determine whether the circumstances fell within the commissioner's statutorily-defined jurisdiction. *Id.* at 63-64.

Thus, as the *Marathon* plurality acknowledged, *Crowell* recognized that "with respect to congressionally created rights, some factual determinations may be made by a specialized tribunal designed by Congress," so long as an Article III court retained full authority over matters of law. *Marathon*, 458 U.S. at 80-81; s*ee also RFC*, 318 U.S. at 171 (upholding specialized bankruptcy-related factfinding by non-Article III commission that was only subject to "a court's supervision in matters of law").

The current bankruptcy scheme for core proceedings is analogous to the adjunct approach upheld in *Crowell*. On appeal from the bankruptcy court's judgment in a core proceeding, the district court independently reviews and decides all matters of law, including reviewing whether substantial evidence supports the bankruptcy court's findings and whether the bankruptcy court correctly concluded that core jurisdiction existed, all consistent with *Crowell*.[25]

A *Crowell* adjunct-court theory supports core jurisdiction over all compulsory counterclaims to proofs of claim, because the Article III district court retains the requisite level of control.

[25] In non-core proceedings, the district court treats any bankruptcy court findings as proposed and engages in de novo review of facts, consistent with the standard that *United States v. Raddatz*, 447 U.S. 667 (1980) upheld for magistrate review.

CONCLUSION

For all the foregoing reasons, petitioner respectfully submits that the decision below should be reversed.

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