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 AMICI CURIAE LAW PROFESSORS S. TODD BROWN, G. MARCUS COLE, RONALD D. ROTUNDA, AND TODD J. ZYWICKI IN SUPPORT OF RESPONDENT

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INTEREST OF AMICI

Amici curiae are law professors with expertise in bankruptcy law, federal courts and federal jurisdiction. This case addresses important issues regarding the extent to which the judicial power of the United States can, consistent with the Constitution, be delegated to Article I bankruptcy courts. *Amici* have a professional interest in the proper application and development of the law in this area.[1]

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1. No counsel for a party authored this brief in whole or in part, and no such counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than the amici, or their counsel, made a monetary contribution intended to fund its preparation or submission. The parties have filed blanket waivers with the Court consenting to the submission of all amicus briefs.

STATEMENT

This case is not about bankruptcy jurisdiction. Bankruptcy jurisdiction is governed by 28 U.S.C. § 1334, and reaches as far as all matters "related to" a bankruptcy case. Bankruptcy *jurisdiction* is not at issue in this case.

Rather, this case is about limitations on the exercise of the judicial power of the United States by Article I judges. Congress has limited the extent of judicial power that can be exercised by Article I bankruptcy judges through the distinction between "core" matters that "arise under" the Bankruptcy Code[2] or "arise in" a bankruptcy case, on the one hand, and "non-core" matters that are "related to" a case, on the other.

The distinction is set out in 28 U.S.C. § 157. For "core" matters arising under the Code or arising in a bankruptcy case, bankruptcy courts are authorized to exercise the full range of judicial power of the United States and can enter final orders reviewable only by appeal. For "non-core" matters that are merely "related to" a bankruptcy case, bankruptcy courts cannot exercise the full extent of that power without the parties' express written consent, and may instead only enter proposed findings of fact and conclusions of law that are reviewable, *de novo*, by an Article III district court.[3] In either case, jurisdiction is present and the

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2. 11 U.S.C. §§ 101 *et seq.* (hereinafter, the "Code").

3. *See* 28 U.S.C. §§ 157(c)(1) (de novo review), 158 (appellate review); G. Marcus Cole & Todd J. Zywicki, *Anna Nicole Smith Goes Shopping: The New Forum-Shopping Problem In Bankruptcy*, 2010 UTAH L. REV. 511, 531 (2010) (hereinafter, "*Forum-Shopping*") (discussing review).

matter can be heard by the bankruptcy court; the distinction is the type of order that can be entered by the bankruptcy court.[4] The question here is whether the counterclaim at issue can be considered a "core" matter "arising under" the Code or "arising in" a bankruptcy case for which a bankruptcy court can enter a final order.

Article III of the Constitution provides that "[t]he judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as Congress may from time to time ordain and establish," and that the judges of those courts must have life tenure (assuming "good Behavior") and receive undiminished compensation during that tenure. U.S. CONST. art. III, § 1. These protections ensure the independence of the judiciary, which is an "inseparable element of the constitutional system of checks and balances." *N. Pipeline Constr. Co. v. Marathon Pipe Line Co.*, 458 U.S. 50, 58 (1982).[5]

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4. Petitioner misapplies this concept. Pet. Br. at 35 ("splinter[s]" jurisdiction "into different forums"); 36 (requires district courts to determine counterclaims); 47 (citing *Alexander v. Hillman*, 296 U.S. 222 (1935), and implying the decision below requires Petitioner to "go to another court to recover [on the counterclaim]."). If jurisdiction is present under 28 U.S.C. § 1334 and referral made under 28 U.S.C. § 157(a), the matter can be heard by the bankruptcy court (unless removal or abstention is applied). The difference is in the type of order the bankruptcy court can enter.

5. *See* Rotunda & Nowak, 1 TREATISE ON CONSTITUTIONAL LAW: SUBSTANCE & PROCEDURE § 2.1 (4th ed. 2007) ("*Article I Courts*"; discussing the *Marathon* principle, *Thomas v. Union Carbide Agricultural Products, Inc.* and *Commodity Futures Trading Comm'n v. Schor*); *id.* § 3.7 ("*Sources of Federal Power—Bankruptcy*"; discussing *Marathon*).

Nevertheless, Congress may, pursuant to Article I, vest decision-making authority over certain disputes in tribunals that lack the attributes of Article III courts. *Thomas v. Union Carbide Agric. Prods., Inc.*, 473 U.S. 568, 583 (1986). Whether a congressional delegation of adjudicative functions to a non-Article III tribunal is constitutionally permissible "must be assessed by reference to the purposes underlying the requirements of Article III." *Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 847-48 (1986).

In 1978, Congress re-wrote the nation's bankruptcy laws, replacing the Bankruptcy Act of 1898 with the Code. Under the 1978 Code, bankruptcy courts had broad jurisdiction over "all civil proceedings arising under title 11 [the Code] or arising in or related to cases under title 11." 28 U.S.C. § 1471(b) (repealed 1984). The 1978 Code did not distinguish between "core" and "non-core" matters. Instead, bankruptcy courts had plenary jurisdiction over all proceedings "arising under" the Code or "arising in or related to" cases under the Code.

Marathon addressed whether that jurisdictional scheme violated Article III. After Northern Pipeline filed for bankruptcy, it brought suit in the bankruptcy court against Marathon on a state-law breach-of-contract claim. *Marathon*, 458 U.S. at 56. The state-law claim did not arise under the Code or arise in the bankruptcy case, but was "related to" the bankruptcy case because any recovery on the claim would have increased the estate's assets. *Id.* at 54, 71-72 (plurality). Under the 1978 Code, the bankruptcy court had plenary jurisdiction over proceedings "related to" the bankruptcy case. *Id.* at 54. The Court held that

permitting non-Article III bankruptcy courts to exercise plenary jurisdiction over state-law contract claims merely because those claims were "related to" the bankruptcy case contravened Article III because doing so removed "the essential attributes of the judicial power from the Article III district court and vested those attributes in a non-Article III adjunct." *Id.* at 87 (plurality opinion); *id.* at 91-92 (Rehnquist, J., concurring).

A plurality of four Justices concluded that there was a constitutionally significant difference between "public rights" matters "arising between the Government and persons subject to its authority" that historically could have been determined by Congress or the executive branch, on the one hand, and "private rights" matters, which include disputes between individuals arising under common law, on the other. *Id.* at 67-70. "Public rights" matters could under certain circumstances be constitutionally adjudicated by non-Article III tribunals. *Id.* at 69. But "private rights" matters generally could not. *Id.* at 70-71, 83-87.

In response to the constitutional concern articulated in *Marathon*, in 1984 Congress amended title 28 to limit the power of bankruptcy courts to enter final judgment to the type of "public rights" matters that *Marathon* suggested may be constitutionally adjudicated in an Article I court. The statute achieves this goal by distinguishing between "core" bankruptcy proceedings that "aris[e] under" the Code or "aris[e] in a case under" the Code, and "non-core" bankruptcy proceedings that are "otherwise related to" a case under the bankruptcy laws. 28 U.S.C. § 157. Today, any interpretation of 28

U.S.C. § 157 must be consistent with *Marathon*. This is especially so considering that Congress amended the Code in an effort to comply with *Marathon*.

The amended statute gives federal district courts original and exclusive jurisdiction over "all cases under title 11." 28 U.S.C. § 1334(a).[6] The amended statute also gives district courts original jurisdiction over "all civil proceedings arising under" the Code, "or arising in or related to cases under" the Code. 28 U.S.C. § 1334(b). District courts may refer any of those proceedings to a bankruptcy court. *Id*. § 157(a).[7] Bankruptcy courts have authority to enter final judgments only in "core" bankruptcy proceedings that "aris[e] under" the Code, or "aris[e] in a case under" the Code. *Id*. § 157(b)(1).[8] In contrast, for "non-core" matters that are only "related

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6. There is no insolvency requirement for relief under present-day title 11, although such a requirement existed at times under prior bankruptcy laws. *See* Thomas E. Plank, *The Constitutional Limits Of Bankruptcy*, 63 TENN. L. REV. 487, 546 (Spring 1996) (historical analysis).

7. "All U.S. district courts, by operation of local rules, automatically refer bankruptcy petitions filed with their respective clerk of court's office to the district's bankruptcy court." *Forum-Shopping*, 2010 UTAH L. REV. at 530-31.

8. *Forum-Shopping*, 2010 UTAH L. REV. at 526 ("In order to have final order jurisdiction, the bankruptcy court must have before it a 'core' matter that also 'arises in' or 'arises under' a case under title 11. The distinction may appear to be a subtle one, but it is one of enormous consequence.") (footnote omitted); *id*. at 534 ("[T]he party asserting bankruptcy jurisdiction must demonstrate not only that the matter is 'core' within the meaning of § 157(b)(2), but also that it 'arises under' or 'arises in' a case under title 11.").

to" a bankruptcy case, bankruptcy courts cannot enter final judgments without the parties' express consent, and may only enter proposed findings of fact and conclusions of law subject to *de novo* review by the district court. *Id.* § 157(b)(1), (c).

Proceedings that "arise under" the Code involve rights created or determined by federal bankruptcy law. *See* 1 ALAN N. RESNICK & HENRY J. SOMMER, COLLIER ON BANKRUPTCY ¶ 3.01[3][c][i] (16th ed. 2010). Proceedings that "arise in a case" under the Code are matters that arise *only* in bankruptcy cases. *See id.* at ¶ 3.01[3][c][iv]. In short, proceedings that invoke substantive rights created by federal bankruptcy law or that could arise only in the context of a bankruptcy case are the kinds of "core" proceedings that a bankruptcy court may finally determine. 28 U.S.C. § 157(b)(1). Being creatures of federal creation unique to bankruptcy proceedings, these matters can be viewed as involving "public rights" that can be resolved by entry of final orders by Article I bankruptcy courts (when consistent with *Granfinanciera*, discussed *infra*).[9]

The Court's post-*Marathon* cases suggest that, if a state-law counterclaim to a proof of claim in bankruptcy can be considered a "core" proceeding that an Article I bankruptcy court may determine by entry of a final order, resolution of that counterclaim must be necessary to determine the allowance or disallowance of the underlying claim against the estate—*i.e.*, it is so

9. One view is that public rights matters require that the United States be a party to the litigation. For purposes of this case, *amici* discuss a broader rule.

intertwined with a function that the bankruptcy court must perform that it may properly be assigned to a non-Article III judicial officer. Those cases reveal that although a majority of the *Marathon* Court did not adopt the plurality's reasoning that the public/private right distinction was dispositive, the basic distinction drawn in *Marathon* between matters of public right that are at the core of the bankruptcy process, and matters of private right that are not, is still viable.

Thomas v. Union Carbide Agricultural Products, Inc., considered the constitutionality of provisions of the Federal Insecticide, Fungicide, and Rodenticide Act and whether disputes over related licensing fees could be decided by a non-Article III tribunal with limited Article III review. 473 U.S. 568 (1986). To evaluate the constitutional propriety of this statutory scheme, the Court adopted a balancing test, under which the public/private right determination was one important factor. *Id.* at 587. The Court concluded that although the license fee disputes were between private parties, the licensing provision had "many of the characteristics of a 'public right'" because it was an integral part of a federal regulatory scheme. In those circumstances, the Court concluded that "Congress may create 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." *Id.* at 593-94.

Commodity Futures Trading Commission v. Schor, considered the constitutionality of a scheme under which non-Article III tribunals could adjudicate state-law counterclaims between private parties. 478 U.S. 833

(1986). Under the Commodity Exchange Act, the Commodity Futures Trading Commission ("CFTC") administered a reparations procedure under which customers of commodity brokers could seek monetary redress for violations of the Act. As part of adjudicating reparations claims, the CFTC was also permitted to adjudicate state-law counterclaims by brokers arising out of the same transaction or occurrence. *Id.* at 837. Applying the *Thomas* balancing test, the Court found that this scheme did not violate Article III, even though the state-law counterclaim was a matter of "private right" "at the 'core' of matters normally reserved to Article III courts." *Id.* at 853. The Court concluded that the scheme was permissible because the CFTC's jurisdiction was limited to "a narrow class" of state-law counterclaims arising out of the same transaction or occurrence, resolution of which was "a necessary incident to the adjudication of federal claims." *Id.* at 865, 856-57.[10]

Granfinanciera, S.A. v. Nordberg, addressed whether a person who had not submitted a claim against a bankruptcy estate had a right to a jury trial when sued by a bankruptcy trustee to recover alleged fraudulent transfers from the debtor. 492 U.S. 33, 36 (1989). The Court held that the defendant was entitled to a jury trial, relying on the public/private right distinction. Notably, Congress had designated fraudulent transfer actions as "core proceedings" in 28 U.S.C. § 157(b)(2)(H), strongly suggesting that Congress viewed them as

10. Another consideration was that the CFTC's decisions were reviewable *de novo* in federal court. *Id.* at 852-56. *De novo* review was applied by the district court in this case.

"public rights" matters under *Marathon*. Nonetheless, the Court concluded that a fraudulent transfer action was not a matter of "public right" and instead, was a matter of "private right" because historically it was a common-law action that more closely resembled a contract suit brought by a debtor to augment the estate than creditors' claims to distributions from the estate. *See id.* at 55-56.

Accordingly, the Court held that, where the defendant had not filed a claim against the estate, it was entitled to a jury trial in a fraudulent transfer action. *See id.* at 64. By contrast, where a creditor has filed a proof of claim, and a trustee brings a preference action against the creditor such that resolution of those claims is intertwined and "integral" to the public right involved in the claims allowance and disallowance process, a jury trial is not required. *Langenkamp v. Culp*, 498 U.S. 42, 44 (1990); *see also Katchen v. Landy*, 382 U.S. 323, 330-31 (1966) (claim could be neither allowed nor disallowed until preference was determined; therefore, whether creditor has received voidable preference is "part and parcel of the allowance process" subject to summary adjudication by bankruptcy court).

The Court's approach since *Marathon* retains the public/private right distinction and permits a non-Article III tribunal to adjudicate state-law "private rights" only where the state-law claim is so intertwined with a public right that resolution of the state-law claim is necessary to determine federal rights. Likewise, here, *amici* submit that a state-law counterclaim can be a "core" proceeding "arising in a case under" the Code, that a bankruptcy judge may finally determine under

28 U.S.C. § 157(b)(2)(C), only if the counterclaim is so closely related to the proof of claim that resolution of the counterclaim is necessary to resolve the allowance or disallowance of the underlying claim.

Finally, in drawing the line of demarcation between what can and cannot be permissibly considered a "core" counterclaim "arising in" a bankruptcy case within the scope of 28 U.S.C. § 157(b)(2)(C), *amici* submit that two practical points should be kept in mind.

First, Petitioner emphasizes that this case involves a "compulsory" counterclaim and asks that the Court infer from the "compulsory" label that the counterclaim is necessarily a core matter because it "had to" be asserted. *Amici* submit that the compulsory label is not in and of itself relevant. Moreover, Petitioner contends that "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." Pet. Br. at 45 (emphasis supplied). This is an inaccurate and restrictive description of what constitutes compulsory counterclaims in federal court litigation, and as a result understates the rule Petitioner advocates.

Rule 13(a) of the Federal Rules of Civil Procedure, which governs compulsory counterclaims, embodies a rule of convenience. FED. R. CIV. P. 13. It has been broadly construed. Its goals are judicial efficiency and a desire to avoid a multiplicity of suits. It is a *jurisdictional* concept in that it brings into federal court certain state-law counterclaims. 6 WRIGHT-MILLER-KANE,

FEDERAL PRACTICE AND PROCEDURE § 1409 at 49-50 (West 2010) (noting jurisdictional distinctions between compulsory and permissive counterclaims). The most frequently used test for whether a counterclaim is "compulsory" considers whether the counterclaim is "logically related" to the underlying claim, or arises out of "the same transaction or occurrence[,]" or a series of transactions or series of occurrences. *Id.* at § 1410 (generally).[11]

Amici submit that the policy-driven analysis of whether the "compulsory" label applies in a given case has little if any relevance to the question of whether a counterclaim should be considered "core." Those considerations may be relevant in the context of an Article III court's exercise of its plenary adjudicative authority, but are not relevant in the context of a non-Article III bankruptcy court's function of administering the Code. Where the power of a bankruptcy court to enter a final order is at issue, *amici* submit that the rule of convenience contained in Rule 13(a) is not a relevant consideration.[12]

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11. *See Moore v. N.Y. Cotton Exch.*, 270 U.S. 593, 609-10 (1926) ("'Transaction' is a word of flexible meaning. It may comprehend a series of many occurrences, depending not so much on the immediateness of their connection as upon their logical relationship . . ."); *Malinowski v. N.Y. State Dep't of Labor*, 156 F.3d 131, 133 (2d Cir. 1998) ("a transaction 'may comprehend a series of many occurrences, depending not so much upon the immediateness of their connection as upon their logical relationship.'").

12. *See Forum-Shopping*, 2010 UTAH L. REV. at 532 ("Although bankruptcy jurisdiction is necessarily broad, it does not follow that the powers of the bankruptcy court are likewise broad.") (discussing *Wood v. Wood (In re Wood)*, 825 F.2d 90 (5th Cir. 1987)).

Second, *amici* believe it is important to bear in mind the process by which claims can be pursued by creditors in bankruptcy cases, because it is only through the pursuit of an underlying claim that this case differs from *Marathon*.

It is very easy to file claims in bankruptcy cases. As a creditor, you typically get a claim form in the mail. If you are not mailed a form, they are available for free on-line.[13] Neither the form nor its instruction sheet say anything about counterclaims or jurisdiction. You fill out the one-page form, attach to it copies of your invoices or other evidence of the debt, and then mail it back. In many cases, you can electronically file claims, and need not even incur the expense of a stamp. It is that simple.

The broad scope of the compulsory counterclaim rule and the ease with which claims can be asserted, considered together, reveal that construing 28 U.S.C. § 157(b)(2)(C) as permissibly reaching all compulsory counterclaims would constitute an extremely broad delegation of the full range of judicial power of the United States to a non-Article III court. The following hypothetical fact pattern makes the point:

- You sell widgets.

- Over the years, you have sold two types of widgets: old widget A, and new widget B.

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13. *See* United States Courts, Bankruptcy Forms, http://www.uscourts.gov/FormsAndFees/Forms/BankruptcyForms.aspx (last visited December 15, 2010).

- You have a contract with a large corporation to sell to it any kind of widgets you make.

- After years of buying widget A, your customer stopped ordering that kind of widget two years ago. Since then, it has only ordered widget B.

- You sent a shipment for $50 worth of widget B to the corporation. You were not paid. Thereafter, the corporation files bankruptcy, even though it is not insolvent.

- A one-page claim form is mailed to you. You fill it out, put a stamp on it, and mail it back.

- You have submitted to bankruptcy court jurisdiction to have your claim determined. Resolution of your claim is a "core" matter.

Simple enough. But what happens next identifies the problem with Petitioner's reading of the statute:

- Responding to your $50 claim for widget B sales, debtor counterclaims for $100 million.

- The counterclaim alleges that widget A the debtor bought years ago – not the widgets on which your claim is based – was defective and caused the debtor to suffer tremendous losses. You had no idea this counterclaim, or the facts underlying it, existed.

- The counterclaim can be heard by the bankruptcy court because jurisdiction is present under 28 U.S.C. § 1334 and referral is made under 28 U.S.C. § 157(a).

- The debtor contends that because both matters arise out of the same contract, the counterclaim is compulsory and, thus, a "core" matter under 28 U.S.C. § 157(b)(2)(C). The bankruptcy court agrees, and you have lost your right to have an Article III court adjudicate the counterclaim.

The distinction between the extent of judicial power that has been granted to Article III courts, and that which can be delegated to Article I courts, is not so insignificant.

SUMMARY OF ARGUMENT

With *Marathon* as a backdrop, the basic question presented by this case is whether and where a line should be drawn between: (i) counterclaims that are "core" matters "arising under" or "arising in" that can be decided by entry of a final judgment by a bankruptcy court; and (ii) counterclaims whose relationship with the underlying bankruptcy claim is too tenuous to fit within the concept of "core" bankruptcy matters "arising in" a bankruptcy case and that are, instead, merely "related to" a bankruptcy case. In either case, jurisdiction is present but the extent of judicial power that can be exercised by Article I bankruptcy courts differs.

Amici submit that 28 U.S.C. § 157(b)(2)(C) should be construed to provide that when a counterclaim *must* be resolved in order for the underlying claim against the estate to be determined, the counterclaim can be a "core" matter for which bankruptcy courts can enter final orders reviewable only by appeal. Counterclaims that *do not* have to be resolved in order for the

underlying claim to be resolved are not core matters "arising under" title 11 or "arising in" a bankruptcy case. For such counterclaims, bankruptcy courts may exercise "related to" jurisdiction only, and may enter proposed findings of fact and conclusions of law that are reviewable *de novo* by an Article III district court.

This reading of the statute is consistent with a close reading of the Court's Article I jurisprudence. Moreover, this reading of the statute is based upon an analysis of the distinction between Article I and Article III that is grounded in context. *Amici* respectfully submit that when this analytical framework is applied, Petitioner's counterclaim should be considered a non-core matter and that the decision of the court of appeals should be affirmed.

ARGUMENT

I. Article I Courts May Finally Determine State-Law Counterclaims When Necessary To Resolve The Claim To Which It Responds

A. Context: Bankruptcy As Compared With Limited Legislative Schemes

There are three areas where the use of Article I tribunals has been permitted: (i) territorial courts; (ii) courts-martial; and (iii) legislative courts and administrative agencies created by Congress to adjudicate matters involving "public rights." *Marathon*, 458 U.S. at 65-66. Bankruptcy matters fall within the third category.

The difficulty in discerning the boundaries between what constitute "public rights" and "private rights" in the context of the Code arises out of the unique nature of the bankruptcy laws, the state-law nature of most claims, and the broad reach of bankruptcy jurisdiction.

Generally, Article I is used to establish judicial or quasi-judicial tribunals within the sphere of legislative courts and federal administrative and regulatory agencies. Bankruptcy is unique when viewed against this backdrop because the reach of bankruptcy jurisdiction greatly exceeds that which is generally granted to administrative agencies, and the scope of matters and claims that fall within bankruptcy jurisdiction is likely more expansive than that which is delegated to any administrative agency setting. *See* 28 U.S.C. § 1334. Thus, although precedent addressing the delegation of judicial power to administrative agencies is a useful reference, *amici* submit that heightened sensitivity is required in the bankruptcy context because of the exceptionally broad grant of jurisdiction.

Through the Code and Rules, Congress has put in place a framework for the processing of claims against a bankruptcy estate. This is consistent with the fundamental *in rem* nature of bankruptcy proceedings. *Cent. Va. Comm. Coll. v. Katz*, 546 U.S. 356, 362 (2006) ("Bankruptcy jurisdiction, at its core, is *in rem*."). The breadth of the "claims" from which a debtor is given relief through a discharge is exceptionally broad. *See* 11 U.S.C. §§ 101(5), 1141(d)(1), 1228(a), 1328(a). Most commonly, creditors seeking a distribution from the *res* in possession of the bankruptcy court assert state-law claims. *See Travelers Cas. & Sur. Co. of Am. v. Pac. Gas*

& Elec. Co., 549 U.S. 443, 451 (2007); *Butner v. United States*, 440 U.S. 48, 57 (1979).

This unique statutory framework makes elusive a precise definition of what are properly considered "public rights" in the bankruptcy context. Decisions from the Court have not fully resolved this line-drawing exercise. In *Marathon*, the Court described two types of bankruptcy matters the Court viewed as being squarely on opposite sides of the line: (i) matters involving "the restructuring of debtor-creditor relations"[14] and (ii) "the adjudication of state-created private rights[.]" *Marathon*, 458 U.S. at 71. Thus, in *Marathon*, since the non-debtor party had not asserted a claim against the bankruptcy estate, the Court held that a state-law claim by the debtor against its contract counter-party could not be fully adjudicated by the non-

14. Subsequent decisions retreated from the suggestion that an open-ended, broad category of matters–"restructuring of debtor-creditor relations"–qualifies. *Granfinanciera*, 492 U.S. at 56 n.11. Petitioner relies on this categorical description. Pet. Br. at 56-57 ("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.") (emphasis supplied). In doing so, Petitioner effectively seeks review of 28 U.S.C. § 157(b)(2)(O), which addresses "the adjustment of the debtor-creditor . . . relationship[.]" Review was not sought, nor was *certiorari* granted, with respect to 28 U.S.C. § 157(b)(2)(O).

Tethering the "public right" distinction to the federal statute for claims allowance – 11 U.S.C. § 502 – rather than to a broad, ill-defined categorical description, is the better approach. Even so, 11 U.S.C. § 502 does not provide a federal right to pursue *counterclaims*; rather, it provides a mechanism for pursuing *claims* against the *res*.

Article III bankruptcy court. It was a "private right" action to augment the *res*, not a claim against the *res*.

Here, Respondent filed a claim against the bankruptcy estate. The assertion of this claim implicated the claims allowance and disallowance process; but even so, characterizing a claim against a bankruptcy estate as a "public right" is an awkward fit. The defamation claim against the *res* here arises under state law. Congress did not create this right, nor is the Government a party to it. Thus, the "claim," in and of itself, falls outside any commonly accepted description of a "public right." However, Congress created the statutory framework through which claims against the *res* are processed. With context in mind, the allowance or disallowance pursuant to 11 U.S.C. § 502 of a state-law defamation claim against the bankruptcy estate can be viewed as implicating a "public right" because absent the framework put in place by Congress, the right to share in the bankruptcy estate through an allowed claim would not exist.

Other rights and claims, created by the Code, fall within the "public rights" domain as well. Claims that a debt is nondischargeable, claims of exemptions, and assertion of an entitlement to a discharge, are matters that can be considered "public rights." *See* 11 U.S.C. §§ 522, 523, 1141, 1228, 1328. These matters "arise under" the Code or "arise in" a bankruptcy case. The claim asserted by Petitioner is none of those things. Rather, it is a state law tort claim for damages personal to Petitioner that may augment the estate, much like the claim that was asserted in *Marathon*. There is no provision in the Code for the "recovery of estate

counterclaims" or "recovery on causes of action in favor of the estate." Rather, where state-law counterclaims are involved, the federal statutory right implicated is a *creditor's* right to have its claim against the bankruptcy estate allowed or disallowed under 11 U.S.C. § 502. Since 11 U.S.C. § 502 is the federal statutory provision implicated, the question here is whether Petitioner's private right of action counterclaim can nonetheless be adjudicated to judgment by the Article I bankruptcy court not on its face, but rather, as incident to the allowance or disallowance of the proof of claim filed by Respondent.

Interpreting 28 U.S.C. § 157(b)(2)(C) consistently with *Marathon* reveals that the statute cannot be construed to provide that *all* "counterclaims by the estate against persons filing claims against the estate" are core proceedings. Such an interpretation of the statute, divorced from the "arising in" limitation Congress created in response to *Marathon*, would necessarily encompass not only counterclaims that involve rights under federal bankruptcy law ("arising under") and that arise *only* in the context of a bankruptcy case ("arising in"), but also counterclaims that are only "related to" cases under the Code. It would include private rights matters having nothing to do with (i) claims against the *res* in possession of the bankruptcy court or (ii) the allowance or disallowance of claims that is the focus of the Code and Rules.[15] Reading the statute

15. Such a rule has "no limiting principle." *Marathon*, 458 U.S. at 73-74; *see* Jeffrey T. Ferriel, *Constitutionality Of The Bankruptcy Amendments And Federal Judgeship Act Of 1984*, 63 Am. Bankr. L.J. 109, 135-36 (Spring 1989) (hereinafter, "*Constitutionality Of The Bankruptcy Amendments*") (discussing transactional approach, noting that transactional counterclaims can be litigated in a claim objection).

to mean that all counterclaims are "core" matters based on "public rights" (even where they are, substantively, private rights matters) would directly contravene *Marathon* and the Article III concerns that the amended statutory scheme was intended to address.[16] It would ignore *context*, the basic and fundamental nature of bankruptcy proceedings as being a process for resolving claims against a *res*, and the Article I implications of the broad jurisdictional grant in 28 U.S.C. § 1334.

B. Not All Counterclaims Can Be "Core"

In order to avoid the constitutionally dubious conclusion that all counterclaims can be "core" proceedings that a bankruptcy court may finally determine, *amici* submit that the statute should be construed to provide that a counterclaim can be a "core" proceeding if resolution of that counterclaim is necessary as part of the allowance or disallowance of the underlying claim against the estate. *See Crowell v. Benson*, 285 U.S. 22, 62 (1932) ("[When] a serious doubt of constitutionality is raised [about an act of Congress], it is a cardinal principle that this Court will first ascertain whether a construction of the statute is fairly possible by which the question may be avoided.").

A tortious interference counterclaim does not "arise under" the Code because it is a matter of state law and no provision in title 11 provides for the allowance or disallowance of *counter*claims. However, title 11 does

16. It would also be contrary to *Granfinanciera*, discussed *infra* at Point I.B.

provide for the allowance and disallowance of claims against the bankruptcy estate by creditors, and the allowance of claims against the *res* can fairly be described as a "public right." 11 U.S.C. § 502. Thus, under the requirement for "arising in a case" under the Code, a state-law counterclaim might be viewed as a public right "arising in" a bankruptcy case if it is a necessary incident to the claim allowance process. But the extent of possible counterclaims is a matter of *in personam* rights that extends well beyond matters responsive to, or dispositive of, claims against the *res*. This raises the question of whether filing a claim against the *res* categorically transforms all counterclaims from private rights matters into public rights matters.

In resolving the question of whether private rights matters can be categorically recharacterized as public rights/core matters, *Granfinanciera v. Nordberg*, 492 U.S. 33 (1989), is instructive. In *Granfinanciera*, the Court addressed fraudulent transfer claims brought by a bankruptcy estate against parties that had not filed claims against it, and whether those claims were "core" matters that could be determined by a bankruptcy court without trial by jury.

In analyzing whether a Seventh Amendment right to a jury trial existed, the Court analyzed whether the fraudulent transfer action was a matter of "public rights" that could be assigned to a non-Article III court. The reason for this analysis was straightforward:

> [I]f a statutory cause of action, such as respondent's right to recover a fraudulent conveyance under 11 U.S.C. § 548(a)(2), is not

> a "public right" for Article III purposes, then Congress may not assign its adjudication to a specialized non-Article III court lacking "the essential attributes of the judicial power."

Granfinanciera, 492 U.S. at 53.

Addressing the public/private right distinction, the Court found that the cause of action in 11 U.S.C. § 548(a)(2) was a private, rather than public, right. Notwithstanding that the cause of action was a matter of statute under the Code, the Court based its finding on historical analysis of fraudulent transfer actions. *Id.* at 55-56. The Court stated:

> There can be little doubt that fraudulent conveyance actions by bankruptcy trustees–suits which, we said in *Schoenthal v. Irving Trust Co.*, 287 U.S. at 94-95, 53 S.Ct. at 51 (citation omitted), "constitute no part of the proceeding in bankruptcy but concern controversies arising out of it"–are quintessentially suits at common law that more nearly resemble state-law contract claims brought by a bankruptcy corporation to augment the bankruptcy estate than they do *creditors' hierarchically ordered claims to a pro rata share of the bankruptcy res. See Gibson* 1022-1025. They therefore appear matters of private rather than public right.

Id. at 56 (emphasis supplied); *see Marathon*, 458 U.S. at 72 n.26 ("This claim may be adjudicated in federal court on the basis of its relationship to the petition for

reorganization. But this relationship does not transform the state-created right into a matter between the Government and the petitioner for reorganization. Even in the absence of the federal scheme, the plaintiff would be able to proceed against the defendant on the state-law contractual claims.") (internal citations omitted). Thus, the cause of action could not be adjudicated to final judgment by an Article I bankruptcy court without respecting the defendant's right to a jury trial, because the action was a matter of "private rights."[17] The "core" label didn't matter; the substance of the claim did.

The same reasoning applies here. Although Congress has included counterclaims by the estate in a list of "core" matters, the fact remains that state-law counterclaims that will augment the estate, but that need not be resolved as part of a claim against the estate, are matters of private right, as *Granfinanciera* confirms. Matters of private right that are not intertwined with matters of public right (*e.g.*, the allowance of claims) such that resolution of the public right requires resolution of the private right, cannot be determined by entry of a final judgment by an Article I court. That is precisely the case here.

C. *Schor* and *Katchen*

Petitioner relies on *Commodity Futures Trading Commission v. Schor*, 478 U.S. 833 (1986), to support his position, but context is important. In *Schor*, the

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17. The Court did not address whether permitting a jury trial to be held by an Article I court would satisfy the requirements of Article III. *Granfinanciera*, 492 U.S. at 50.

underlying claim was created by federal law. Schor asserted a reparations complaint against his broker arising out of his broker's alleged violations of the Commodity Exchange Act ("CEA") in handling Schor's accounts. Being a federally-created right, Congress provided that the reparations claim was to be heard by the Commodity Futures Trading Commission ("CFTC"), an Article I tribunal.

Schor's broker counterclaimed. The substance of the counterclaim is important to understanding the holding in *Schor*. It was a state law claim. After Schor's account was liquidated there was a debit balance, and the broker sought payment of that balance through the counterclaim. The claim and counterclaim arose out of the same account. The counterclaim alleged that the debit balance was a valid debt owed by Schor. Schor disagreed, and argued that the debit balance "was the result of [the broker's] numerous violations of the CEA." *Schor*, 478 U.S. at 837. Essentially, Schor said he *should not* have to pay the debit charges, and the broker said that Schor *should* have to pay the charges. The claims were based on the same debt. The success of one dictated the failure of the other.[18]

The Court upheld the authority of the CFTA to adjudicate state-law counterclaims "aris[ing] out of the

18. *See Constitutionality Of The Bankruptcy Amendments*, 63 Am. Bankr. L.J. at 136 (the counterclaim was "the only likely counterclaim that will be brought in a reparations proceeding [and that] the broker's right to recover the balance . . . is likely to turn more on resolution of the facts alleged by the customer in the reparations proceeding than on any independent factual basis").

transaction or occurrence or series of transactions or occurrences set forth in the complaint." *Schor*, 478 U.S. at 837 (quotations omitted). From this, Petitioner argues that the bankruptcy court below could enter a final order on Petitioner's counterclaim, because it was a compulsory counterclaim, and the test for whether a counterclaim qualifies for the "compulsory" label is the equivalent of the language used in the statute at issue in *Schor*.

Petitioner's argument ignores context. The reparations claim asserted in *Schor* was in a narrow class of statutory claims created by federal law. That is not the case here, and it is unrealistic to suggest that it would be the case in any bankruptcy proceeding, because the overwhelming majority of claims in bankruptcy are based on state law. Moreover, resolution of the counterclaim in *Schor* was part and parcel of resolution of the underlying claim. Resolution of one necessarily resolved the other. That is not the case here. Here, the claim was determined on November 5, 1999, when Petitioner was granted summary judgment, but the bankruptcy court did not rule on the counterclaim until September 27, 2000, nearly one year later. PA18-19. Here, one had nothing to do with the other. The rule from *Schor*, viewed alongside its facts, is not nearly as broad as Petitioner suggests by arguing that it controls here.

Nor should *Schor* be read so expansively. The dissent, authored by Justice Brennan (who authored the plurality opinion in *Marathon*), noted that although *Schor* involved a narrow set of facts, the rule from *Schor* could be broadened. *Schor*, 478 U.S. at 865-66. Justice Brennan warned that an expansive reading of *Schor*

would put the protections of Article III on a slippery slope that could lead to their erosion and dilution. *Id.* at 866. That erosion is precisely what Petitioner seeks here.[19] Bearing in mind that Justice Brennan authored the plurality opinion in *Marathon* that addressed the public/private right question in the bankruptcy context, his concerns in *Schor* reinforce the conclusion that 28 U.S.C. § 157(b)(2)(C) should not be read as expansively as its text (all counterclaims), or even as expansively as Petitioner suggests (at a minimum, all compulsory counterclaims).

Katchen v. Landy, 382 U.S. 323 (1966), is consistent with *Schor*. In *Katchen*, a creditor filed a claim and in response the trustee asserted a preferential transfer action. The Bankruptcy Act in effect at the time provided that before a creditor could be given an allowed claim, it had to pay back to the estate the amount of any preferential payment it received. The question before the Court was whether the Bankruptcy Act enabled the preference action, and an order requiring repayment to the estate, to be summarily decided as part of the allowance or disallowance of the claim that was filed against the *res*, without a plenary action. The Court held that it *could* be summarily tried, because the objection had to be fully resolved before the claim could be allowed. It was part and parcel of the claims allowance process. *Id*. at 336. Indeed, the statute implicated in *Katchen* was entitled "Proof and Allowance of Claims."

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19. Query whether jurisdiction would exist if the broker alleged that Schor defamed him years ago when, after Schor incurred losses, he told friends the broker gave bad advice, and as counterclaims the broker sought recovery for defamation and tortious interference with prospective economic advantage.

See id. at 330-31 (discussing 11 U.S.C. § 93(g) (1964 ed.)).[20]

In *Katchen*, the Court observed:

> [The] power to allow or to disallow claims includes full power to inquire into the validity of any alleged debt or obligation of the bankrupt upon which a demand or a claim against the estate is based. This is essential to the performance of the duties imposed upon it. . . . The whole process of proof, allowance, and distribution is, shortly speaking, an adjudication of interests claimed in a *res*, and thus falls within the principle quoted above that bankruptcy courts have summary jurisdiction to adjudicate controversies relating to property within their possession.

Id. at 330 (internal quotations and citations omitted). This passage emphasizes that the bedrock bankruptcy function of resolving claims focuses on the *res*, not claims to augment the estate such as the claims at issue here.

The Court also noted that lower court decisions "[upholding] summary jurisdiction to grant affirmative relief on related counterclaims *that would also be defenses to the claim*" were consistent with its holding

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20. Subsection (g) provided: "The claims of creditors who have received or acquired preferences . . . void or voidable under this Act, shall not be allowed unless such creditors shall surrender such preferences . . . ."). *See* App. A, Lawrence P. King, Collier On Bankruptcy, App. Pt. 3(a), at 3-47 and 3-48 (15th ed. revised 2010).

in *Katchen*. *Id*. at 336 n.12 (emphasis supplied). The Court's later holding in *Schor* is consistent with this aspect of *Katchen*, because in *Schor*, resolution of the claim necessarily determined the counterclaim, and vice versa. *Schor*, 478 U.S. at 856 ("The CFTC adjudication of common law counterclaims is incidental to, and completely dependent upon, adjudication of reparations claims created by federal law, and in actual fact is limited to claims arising out of the same transaction or occurrence as the reparations claim.").

Amici submit that *Schor* and *Katchen* provide that when resolution of a counterclaim is necessary for a bankruptcy court to fulfill its obligations under 11 U.S.C. § 502 to determine the allowance or disallowance of claims against the estate, or resolution of the claim resolves the counterclaim, it can be a core matter consistent with the Court's "public rights" jurisprudence. Conversely, if the proof of claim and counterclaim are *not* so intertwined that the counterclaim implicates the claim allowance statute, the counterclaim cannot be transformed into a public rights "core" matter. Rather, it is then a non-core matter that implicates "related to" jurisdiction alone.[21]

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21. The Code must be construed to respect state law rights except for rare circumstances in which bankruptcy requires otherwise. *Butner v. United States*, 440 U.S. 48, 55 (1979) ("Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. Uniform treatment of property interests by both state and federal courts within a State serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving a windfall merely by reason of the happenstance of bankruptcy.") (citation omitted).

Rather than tethering the public/private right distinction to the federal statute, Petitioner relies on a broad, categorical description of what can constitute core matters. Petitioner argues: "[C]laims 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." *See* Pet. Br. at 56-57 (emphasis added). The Court previously declined the invitation presented by Petitioner's argument–to find that a category of matters, as open-ended and broad as "the restructuring of debtor-creditor relations," should be considered public rights. *See Granfinanciera*, 492 U.S. at 56 n.11. *Amici* submit that grounding the "public right" distinction in the federal *statute* – 11 U.S.C. § 502 – is the more appropriate and supportable approach.[22]

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22. There is confusion in Petitioner's approach. At times, Petitioner advocates a narrow rule. *See* Pet. Br. at 16 ("integrally-related counterclaims"). At other times, Petitioner advocates an expansive rule. *See* Pet. Br. at 32 ("core bankruptcy function of restructuring *and* adjusting debtor-creditor rights") (emphasis supplied); 56 ("claims allowance *and* the adjustment of the debtor-creditor relationship . . .") (emphasis supplied). 28 U.S.C. § 157(b)(2)(O) addresses "the adjustment of the debtor-creditor . . . relationship" and is not implicated by the questions for which the Court granted *certiorari*. *See* n.11, *supra*. Regardless, courts have read *Marathon* as limiting 28 U.S.C. § 157(b)(2)(O). *See Wood v. Wood (In re Wood)*, 825 F.2d 90, 95-98 (5th Cir. 1987); *Forum-Shopping*, 2010 Utah L. Rev. at 526 ("[I]t is conceivable that a bankruptcy court, in making the determination as to whether a matter is a 'core' proceeding, might rely on this language and sweep into its final order jurisdiction a case wholly reliant upon state law and rights created by it, thereby elevating its powers to those of an Article III federal court.").

II. *Marathon's* Concerns About An Independent Judiciary Are Not Eliminated By The Present-Day Bankruptcy Code

Petitioner suggests that because the present-day statutory framework provides that bankruptcy judges are appointed and removed by Article III judges, that the independence of the judiciary concerns highlighted in *Marathon* are *de minimis*. Pet. Br. at 55-59. This is incorrect.

As the Court recognized in *Marathon*:

> Periodic appointments, however regulated, or by whomsoever made, would, in some way or another, be fatal to [the courts'] necessary independence. If the power of making them was committed either to the Executive or legislature, there would be danger of an improper complaisance to the branch which possessed it; if to both, there would be an unwillingness to hazard the displeasure of either; if to the people, or to persons chosen by them for the special purpose, there would be too great a disposition to consult popularity, to justify a reliance that nothing would be consulted but the Constitution and the laws.

Marathon, 458 U.S. at 58-59 (internal quotations omitted) (quoting THE FEDERALIST NO. 78, at 489 (Alexander Hamilton) (H. Lodge ed., 1888)); *see Schor*, 478 U.S. at 859-60 (Brennan, J., dissenting).

More directly addressing Petitioner's contention, the Court noted:

> The guaranty of life tenure insulates the individual judge from improper influences not only by other branches but by colleagues as well, and thus promotes judicial individualism.

Marathon, 458 U.S. at 59 n.10; *see also Schor*, 478 U.S. at 860-61 (Brennan, J., dissenting) (noting Alexander Hamilton's observation "[t]hat inflexible and uniform adherence to the rights of the Constitution, and of individuals, which we perceive to be indispensable in the Courts of justice can certainly not be expected from Judges who hold their offices by a temporary commission.") (*quoting* The Federalist No. 78, at 546 (Alexander Hamilton) (H. Dawson ed. 1876)) (internal quotations omitted); *Forum-Shopping*, 2010 Utah L. Rev. at 538-39 (noting problems with reappointment system).

The structural protections of the Constitution requiring that the adjudication of private rights matters be reserved for the Article III judiciary remain important in the bankruptcy context regardless of the fact that, today, bankruptcy judges are appointed by their colleagues instead of by the Executive or legislature. This very circumstance was foretold by Justice Brennan in *Marathon*, and further "incremental erosion" of these structural protections was warned against by Justice Brennan in *Schor*.

Faced with a choice, Congress chose not to create a system within which bankruptcy judges would be given

Article III status. Instead, Congress chose to create a system in which there are limitations. Those limitations cannot be ignored.

III. Petitioner's Counterclaim Was Not Integral To Allowance Or Disallowance Of Claims Against The Estate

Amici submit that Petitioner's tortious interference claim can only be a "core" proceeding "arising in" a case under the Code if resolution of the counterclaim was necessary in order to resolve the allowance or disallowance of Respondent's claim against the estate.

Here, the Court of Appeals found it to be an "inescapable conclusion" that "resolution of [Petitioner's] counterclaim was not a necessary predicate to the bankruptcy court's decision to allow or disallow [Respondent's] claim." PA52. Petitioner disagrees, contending that success on the tortious interference counterclaim would have "establish[ed] the affirmative defense of truth" to Respondent's defamation claim. Pet. Br. at 14.

In dissecting Petitioner's argument, it is important to recognize that the *defense* is separate and distinct from the *counterclaim*. ER-938, 941-54.[23] Petitioner

23. The counterclaims were varied, based upon different theories and sought varied relief. *See Marshall v. Marshall*, 275 B.R. 5, 9 (C.D. Cal. 2002) (counterclaims for fraudulent transfer, injunction, conversion, tortious interference, breach of fiduciary duty, abuse of process, fraud, promissory estoppel, breach of contract (third-party beneficiary), imposition of constructive trust, accounting, indemnity and contribution).

blurs this distinction, combining the two separate concepts into one: "success on [Petitioner's] counterclaim would necessarily defeat [Respondent's] proof of claim by establishing the affirmative defense of truth[.]" Pet. Br. at 14. This is a flaw in Petitioner's argument, not a strength. In substance, Petitioner argues that resolution of the tortious interference counterclaim would have "brought with it" resolution of the affirmative defense.[24] Clever wordsmithing, but this bootstraps the *counterclaim* (that both the district court and court of appeals said had an attenuated relationship to the underlying claim) to the affirmative *defense* (that has a direct relationship to it). The stand-alone *defense* was all that might have been necessary to resolve as part of the allowance or disallowance of the claim. The counterclaim was not. Indeed, the history of this case makes this clear: the bankruptcy court granted Petitioner summary judgment on Respondent's claim on November 5, 1999, and it was nearly a year later (September 20, 2000) before it ruled on the counterclaim. PA18-19.

Amici submit that for the reasons noted above, and regardless of the fact that Petitioner's counterclaim was found to satisfy the rules of convenience and judicial economy on which the compulsory counterclaim rule is based, resolution of Petitioner's counterclaim was not necessary to resolve the allowance or disallowance of Respondent's claim against the estate. PA18-19 (noting

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24. Whether this is correct is debatable when the one-sentence affirmative defense, *see* ER-938, is compared with the nineteen paragraphs detailing the counterclaim, *see* ER-941-45, 948-49.

dates of entry of summary judgment on claim and decision on counterclaim); PA51 ("[Petitioner's] compulsory counterclaim is not a core proceeding arising in a case under the Bankruptcy Code because it is not so closely related to [Respondent's] defamation claim that it must be resolved in order to determine the allowance or disallowance of his claim against her bankruptcy estate."); PA52 (noting an attenuated nexus between the claim and counterclaim); PA52 (noting differences between the nature and scope of allegations); PA53-54 (noting differences in proof and legal issues). Accordingly, *amici* submit that it does not implicate "public rights" and cannot be considered a "core" matter under 28 U.S.C. § 157.

CONCLUSION

Amici submit that 28 U.S.C. § 157 should be interpreted such that only those counterclaims that independently "arise under" the Code or that "arise in" a bankruptcy case may be "core" matters that can be finally adjudicated by a non-Article III bankruptcy court. If the Court concludes that a state-law counterclaim "arises in" a bankruptcy case since it is a response to a proof of claim, *amici* submit that such a counterclaim can be a "core" proceeding *only* where resolution of the counterclaim is intertwined with resolution of the allowance or disallowance of the claim itself. That is the only way in which a counterclaim can be viewed as being a matter of public rights. Here, the state-law tortious interference claim is a "non-core" proceeding that is merely "related to" the bankruptcy

case and over which *amici* submit the bankruptcy court lacked authority to issue a final judgment.

Respectfully submitted,

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