

Chapter 11 Bankruptcy Venue Reform

It is logical to assume that a bankruptcy proceeding should take place in the jurisdiction where the debtor is largely located. However, current law allows debtors to file in the district in which they are headquartered, in the district in which their principal assets are located, in any district in any state in which they are incorporated, or in any district in which one of their affiliates have filed. Such flexibility lead to what many term as “forum shopping”. The law allows debtors to choose jurisdictions who applies certain laws that are often more sympathetic to their needs or management-friendly, although that very same management may have driven the company into financial distress. Allowing such elasticity in the law can create severe burdens on creditors, employees, and customers, who become part of the case, to travel hundreds or thousands of miles to participate, even though they did business with the debtor in a completely different location. A prime example is The Los Angeles Dodgers who filed their bankruptcy in the District of Delaware where they have an incorporated entity, but no assets, operations, or even substantial creditors.

Certain members of Congress are now aiming to put an end to forum shopping. On July 14, 2011 House Judiciary Chairman Lamar Smith, a Republican from Texas, and John Conyers, Jr., a Democrat from Michigan, introduced the Chapter 11 Bankruptcy Venue Reform Act of 2011 (H.R.2533). The act would require corporations to file their Chapter 11 Bankruptcy Petitions in the judicial district where they have there principal place of business or assets. This narrow specification in the proposed change will limit the courts in which bankruptcy cases can be heard. The act would retain the exceptions needed to remove a case to another location for good cause or convenience. However, the focus of the law requires that the interest of the entire creditor body be evaluated, and not just the mere preference of the debtor when choosing a forum.

It is no coincidence that the bi-partisan sponsorship comes from congressmen representing states that have produced landmark bankruptcy cases: Enron from Texas and General Motors from Michigan. Upon filing for bankruptcy, both of these companies sought to file petitions in the Southern District of New York, which is more than 500 miles from Detroit and 1,500 from Texas. While the aim is to end forum shopping, the goal of the act is to ultimately level the playing field and restore fairness, said Congressman Conyers.

Opponents to the proposed legislation argue that the courts already have mechanisms in place, via 28 U.S.C. §1412, to transfer venue to another jurisdiction if they determine that the current venue was initially chosen in an improper manner or that the existing forum is inconvenient for the relevant parties. Aside from the argument above, opponents have also pointed to a slew of protections afforded to employees, retirees, and trade vendors, which Congress has enacted through changes to the BAPCPA. In sum, detractors dispute the haste and legitimacy of the legislation.

As a creditor, the advantages to this act appear quite clear. Cumbersome travel to courts located in the far corners of the U.S. may become a thing of the past. Techniques such as bootstrapping, in which debtors-to-be create subsidiaries in bankruptcy friendly venues in order to have the ability to file there, will be eliminated. The benefits would appear to give employees, creditors and the likes not even an upper hand, but a level playing field, which may be deserved, in bankruptcy various proceedings, including

preference actions. But there could be adverse consequences, such as overstressing the limited resources in the judiciary and delaying the administration of the proceedings due to court inefficiencies.

On Thursday, September 8, 2011 at 10:00 a.m. a hearing is set for the subcommittee on Courts, Commercial, and Administrative Law of the House Judiciary Committee to meet and discuss H.R. 2533, the “Chapter 11 Bankruptcy Venue Reform Act of 2011.”