Six Degrees of Separation: Exploring the Limits of Related-To Jurisdiction

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EXPLORING THE LIMITS OF RELATED-TO JURISDICTION IN BANKRUPTCY

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I. A Brief Primer on Bankruptcy Jurisdiction Under 28 U.S.C. § 1334(b)

A. The statutes

28 U.S.C. § 1334(a) provides that federal district courts have exclusive jurisdiction of cases under title 11 (the Bankruptcy Code), and § 1334(b) provides that they have "original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11." 28 U.S.C. § 157(a) provides that the district court can refer any or all of those matters to the bankruptcy court in its district.

B. Arising-under and arising-in jurisdiction

The Eighth Circuit has explained the arising-under and arising-in parts of § 1334(b) this way:

> Bankruptcy courts have jurisdiction over civil proceedings "arising under," "arising in," or "related to" title 11. 28 U.S.C. § 157(b)(1), (c)(1). "Civil proceedings in a bankruptcy case are divided into two categories, core proceedings and non-core, related proceedings." *Specialty Mills, Inc. v. Citizens State Bank*, 51 F.3d 770, 773 (8th Cir.1995). Core proceedings are those cases "arising under title 11, or arising in a case under title 11 . . . ." 28 U.S.C. § 157(b)(1). Non-core "related to" proceedings "could conceivably have an[ ] effect on the estate being administered in bankruptcy. . . ." *Specialty Mills*, 51 F.3d at 774 (quotation omitted). . . .
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> . . . . Claims "arising under" Title 11 are "those proceedings that involve a cause of action created or determined by a statutory provision of title 11." *In re Wood*, 825 F.2d 90, 96 (5th Cir.1987); *see also Browning v. Levy*, 283 F.3d 761, 773 (6th Cir.2002) (providing that "arising under" jurisdiction exists where one "invoke[s] a substantive right created by federal bankruptcy law" (quotation omitted)). . . .
>
> "'[A]rising in' proceedings are those that are not based on any right expressly created by title 11, but nevertheless, would have no existence outside of

> the bankruptcy." *In re Wood*, 825 F.2d at 97. As the Third Circuit further explained, "claims that 'arise in' a bankruptcy case are claims that by their nature, not their particular factual circumstance, could only arise in the context of a bankruptcy case." *Stoe v. Flaherty*, 436 F.3d 209, 218 (3d Cir.2006). Accordingly, "administrative matters" such as allowance and disallowance of claims, orders in respect to obtaining credit, determining the dischargeability of debts, discharges, confirmation of plans, orders permitting the assumption or rejection of contracts, are the principal constituents of "arising in" jurisdiction. 1 *Collier on Bankruptcy* § 3.01[4] [c][iv] (Alan N. Resnick & Henry J. Sommer eds., 15th ed. rev.2009).

GAF Holdings, LLC, v. Rinaldi (In re Farmland Industries, Inc., 567 F.3d 1010, 1017-18 (8th Cir. 2009).

The Tenth Circuit Bankruptcy Appellate Panel explained arising-under and arising-in jurisdiction this way:

> A proceeding "arises under" the Bankruptcy Code if it asserts a cause of action created by the Code, such as exemption claims under 11 U.S.C. § 522, avoidance actions under 11 U.S.C. §§ 544, 547, 548, or 549, or claims of discrimination under 11 U.S.C. § 525. H.R.Rep. No. 595, 95th Cong., 1st Sess. 445 (1977) U.S.Code Cong. & Admin.News pp. 5963, 6400; *Bergstrom v. Dalkon Shield Claimants Trust (In re A.H. Robins Co.)*, 86 F.3d 364, 371 (4th Cir.), *cert. denied*, 519 U.S. 993, 117 S.Ct. 483, 136 L.Ed.2d 377 (1996); *Eastport Assocs. v. City of Los Angeles (In re Eastport Assocs.)*, 935 F.2d 1071, 1076 (9th Cir.1991); *Barnett v. Stern*, 909 F.2d 973, 981 (7th Cir.1990); *Gower v. Farmers Home Admin. (In re Davis)*, 899 F.2d 1136, 1140–41 (11th Cir.), *cert. denied*, 498 U.S. 981, 111 S.Ct. 510, 112 L.Ed.2d 522 (1990); *Wood v. Wood (In re Wood)*, 825 F.2d 90, 96 (5th Cir.1987). Proceedings "arising in" in a bankruptcy case are those that could not exist outside of a bankruptcy case, but that are not causes of action created by the Bankruptcy Code. *A.H. Robins*, 86 F.3d at 371; *Eastport*, 935 F.2d at 1076; *Wood*, 825 F.2d at 97. For example, orders respecting the

> obtaining of credit, confirmation of a plan, the assumption or rejection of a contract are all matters which could not exist absent the filing of a bankruptcy case, but are not causes of action created by the Bankruptcy Code. *Wood*, 825 F.2d at 97; *see* 1 Lawrence P. King, *Collier on Bankruptcy* ¶ 3.01(c)[v] (15th ed. 1996).

Personette v. Kennedy (In re Midgard Corp.), 204 B.R. 764, 771 (10th Cir. BAP 1997). *See also Marc Vianello Revocable Trust v. Pete & Mac's Lenexa, LLC*, 2014 WL 1974922 at *2 (D. Kan. May 15, 2014) (citing *Personette* and quoting arising-in portion of above quote); *In re Angel Fire Corp.*, 2012 WL 5880675 at *6 (Bankr. D.N.M. Nov. 20, 2012) (citing *Personette* definitions of arising-under and arising-in jurisdiction).

So both the Eighth and the Tenth Circuits use essentially the same definitions for arising-under and arising-in jurisdiction. In fact, most courts throughout the country seem to use similar definitions, which appear to generate little litigation. Courts largely agree, too, that these definitions cover the bankruptcy jurisdiction that is called "core" in 28 U.S.C. § 157(b), while related-to jurisdiction covers non-core matters.

C. Allocating decisional authority — core versus non-core proceedings

Subsections (b) and (c) of 28 U.S.C. § 157 attempt to divide matters pending in bankruptcy courts into "core" and "non-core" proceedings, and provide that in a core proceeding, a bankruptcy court can issue a final order, but in a non-core proceeding, may only issue proposed findings of fact and conclusions of law, and must leave it to the district court to issue the final order. As the Supreme Court's decision in *Stern v. Marshall*, ___ U.S. ___, 131 S.Ct. 2594, 180 L.Ed.2d 475 (2011), made clear, the distinction between core and non-core proceedings concerns only the allocation between the bankruptcy courts and the district courts of the power to issue final orders. However, *Stern* also made clear that bankruptcy courts cannot

issue final orders in some proceedings that are defined as "core" in § 157(b). Later, in *Executive Benefits Insurance Agency v. Arkison*, ___ U.S. __, 134 S.Ct. 2165, 189 L.Ed.2d 83 (2014), the Court ruled that proceedings that are called "core" in § 157(b) but, under *Stern*, cannot be finally decided by a bankruptcy court should be treated the same way that non-core proceedings are. The core-non-core distinction has generated much more litigation in the bankruptcy courts than the definitions of arising-under and arising-in jurisdiction have.

D. Related-to jurisdiction — the *Pacor* test

Like the core-non-core distinction, the reach of related-to jurisdiction under § 1334(b) has generated a great deal of litigation in the bankruptcy courts. The Supreme Court's decision in *Stern v. Marshall* directly addressed the line between core and non-core bankruptcy matters, but has also brought increased attention to the question of the extent of related-to jurisdiction under § 1334(b).

In *Celotex Corp. v. Edwards*, 514 U.S. 300 (1995), the Supreme Court said it agreed with certain comments about related-to bankruptcy jurisdiction that the Third Circuit made in *Pacor, Inc., v. Higgins*, 743 F.2d 984 (1984), but did not affirmatively adopt the test applied by *Pacor*.

> We agree with the views expressed by the Court of Appeals for the Third Circuit in *Pacor, Inc. v. Higgins*, 743 F.2d 984 (1984), that "Congress intended to grant comprehensive jurisdiction to the bankruptcy courts so that they might deal efficiently and expeditiously with all matters connected with the bankruptcy estate," *id*., at 994; *see also* H.R.Rep. No. 95-595, pp. 43-48 (1977), and that the "related to" language of § 1334(b) must be read to give district courts (and bankruptcy courts under § 157(a)) jurisdiction over more than simple proceedings involving the property of the debtor or the estate. We also agree with that court's observation that a bankruptcy court's "related to" jurisdiction cannot be limitless. *See Pacor*, *supra*, at 994; cf. *Board of Governors, FRS v. MCorp Financial, Inc.*, 502 U.S. 32, 40, 112 S.Ct. 459, 464, 116 L.Ed.2d 358 (1991) (stating that

Congress has vested "limited authority" in bankruptcy courts).

514 U.S. at 308. In footnote 6, the Court said:

> In attempting to strike an appropriate balance, the Third Circuit in *Pacor, Inc. v. Higgins*, 743 F.2d 984 (1984), devised the following test for determining the existence of "related to" jurisdiction: "The usual articulation of the test for determining whether a civil proceeding is related to bankruptcy is whether the outcome of that proceeding could conceivably have any effect on the estate being administered in bankruptcy. . . . Thus, the proceeding need not necessarily be against the debtor or against the debtor's property. An action is related to bankruptcy if the outcome could alter the debtor's rights, liabilities, options, or freedom of action (either positively or negatively) and which in any way impacts upon the handling and administration of the bankrupt estate." *Id*., at 994 (emphasis in original; citations omitted). The First, Fourth, Fifth, Sixth, Eighth, Ninth, Tenth, and Eleventh Circuits have adopted the Pacor test with little or no variation. *See In re G.S.F. Corp.*, 938 F.2d 1467, 1475 (CA1 1991); *A.H. Robins Co. v. Piccinin*, 788 F.2d 994, 1002, n. 11 (CA4), *cert. denied*, 479 U.S. 876, 107 S.Ct. 251, 93 L.Ed.2d 177 (1986); *In re Wood*, 825 F.2d 90, 93 (CA5 1987); *Robinson v. Michigan Consol. Gas Co.*, 918 F.2d 579, 583-584 (CA6 1990); *In re Dogpatch U.S.A., Inc.*, 810 F.2d 782, 786 (CA8 1987); *In re Fietz*, 852 F.2d 455, 457 (CA9 1988); *In re Gardner*, 913 F.2d 1515, 1518 (CA10 1990); *In re Lemco Gypsum, Inc.*, 910 F.2d 784, 788, and n. 19 (CA11 1990). The Second and Seventh Circuits, on the other hand, seem to have adopted a slightly different test. *See In re Turner*, 724 F.2d 338, 341 (CA2 1983); *In re Xonics, Inc.*, 813 F.2d 127, 131 (CA7 1987); *Home Ins. Co. v. Cooper & Cooper, Ltd.*, 889 F.2d 746, 749 (CA7 1989). But whatever test is used, these cases make clear that bankruptcy courts have no jurisdiction over proceedings that have no effect on the estate of the debtor.

Id. at 308, n. 6.

Both 8th and 10th Circuits follow the *Pacor* decision about "related-to" bankruptcy

subject-matter jurisdiction. *See Dogpatch Properties, Inc., v. Dogpatch U.S.A., Inc. (In re Dogpatch, Inc.)*, 810 F.2d 782, 786 (8th Cir. 1987); *United States v. Gardner*, 913 F.2d 1515, 1518 (10th Cir. 1990). *See also Buffets, Inc., v. Leischow*, 732 F.3d 889, 894 (8th Cir. 2013) (following *Dogpatch* test for related-to jurisdiction).

Here is what *Pacor* said about related-to bankruptcy jurisdiction:

> The usual articulation of the test for determining whether a civil proceeding is related to bankruptcy is whether *the outcome of that proceeding could conceivably have any effect on the estate being administered in bankruptcy. E.g., In re Hall,* 30 B.R. at 802; *In re General Oil Distributors, Inc.,* 21 B.R. 888, 892 n. 13 (Bankr.E.D.N.Y.1982); *In re U.S. Air Duct Corp.,* 8 B.R. 848, 851 (Bankr.N.D.N.Y.1981); 1 *Collier on Bankruptcy* ¶ 3.01 at 3–49. Thus, the proceeding need not necessarily be against the debtor or against the debtor's property. An action is related to bankruptcy if the outcome could alter the debtor's rights, liabilities, options, or freedom of action (either positively or negatively) and which in any way impacts upon the handling and administration of the bankrupt estate.
>
> On the other hand, the mere fact that there may be common issues of fact between a civil proceeding and a controversy involving the bankruptcy estate does not bring the matter within the scope of section 1471(b) [the predecessor to § 1334]. Judicial economy itself does not justify federal jurisdiction. *See generally Aldinger v. Howard,* 427 U.S. 1, 15, 96 S.Ct. 2413, 2420, 49 L.Ed.2d 276 (1976). "[J]urisdiction over nonbankruptcy controversies with third parties who are otherwise strangers to the civil proceeding and to the parent bankruptcy does not exist." *In re Haug,* 19 B.R. 223, 224–25 (Bankr.D.Ore.1982); *See also In re McConaghy,* 15 B.R. 480, 481 (Bankr.E.D.Va.1981) (Bankruptcy court lacks jurisdiction to decide disputes between third parties in which the estate of the debtor has no interest).

In re Pacor, Inc., 743 F.2d 984, 994 (3d Cir. 1984).

E. Supplemental jurisdiction under 28 U.S.C. § 1367

There is a statute that extends the jurisdiction a federal court already has over a lawsuit to other matters with a sufficient connection to the pending suit. 28 U.S.C. § 1367 provides:

> (a) Except as provided in subsections (b) and (c) or as expressly provided otherwise by Federal statute, in any civil action of which the district courts have original jurisdiction, the district courts shall have supplemental jurisdiction over all other claims that are so related to claims in the action within such original jurisdiction that they form part of the same case or controversy under Article III of the United States Constitution. Such supplemental jurisdiction shall include claims that involve the joinder or intervention of additional parties.

Subsection (b) limits supplemental jurisdiction in cases where the court's jurisdiction is based on diversity of citizenship. Subsection (c) gives district courts discretion to decline to exercise supplemental jurisdiction under subsection (a) in certain situations.

This provision was intended to codify the Supreme Court's ruling in *United Mine Workers v. Gibbs*, 383 U.S. 715, 725 (1966), that a federal court already having jurisdiction over a substantial federal question could also exercise jurisdiction over another dispute that derived from "a common nucleus of operative fact" even though there was no independent basis of federal jurisdiction over that other dispute. The *Gibbs* ruling "enables federal courts to resolve entire disputes efficiently and conveniently, and avoids duplicative, overlapping federal and state court litigation." 13 Wright, Miller, Cooper, & Freer, Federal Practice & Procedure: Jurisdiction & Related Matters 3d, § 3523 at 172 (Thomson West 2008).

It is easy to think of situations that arise in bankruptcy cases where this statute would appear to provide jurisdiction even though the claim in question could have no affect on the bankruptcy estate or the debtor. For example, where one spouse files bankruptcy but the other does not, the non-filing spouse might often share with the debtor a viable claim against a creditor

or other third party, such as a claim that a mortgage on their home is invalid for some reason. Section 1367 would seem to allow federal jurisdiction over the non-filing spouse's claim (based on exactly the same facts), but the *Pacor* test would not because the resolution of the non-filing spouse's claim could not affect the bankruptcy estate or the debtor's rights. Most courts that have considered whether this statute can apply to bankruptcy matters, however, have concluded it cannot. *See* Eric C. Surette, Annotation, Exercise of Supplemental Jurisdiction by Bankruptcy Courts Pursuant to 28 U.S.C.A. § 1367, 52 A.L.R. Fed.2d 243, § 2 (2011), *available on* Westlaw at 52 A.L.R. Fed.2d 243.

II. Is *Wellness* a Cure or Merely a Band Aid?

A. Introduction

The bankruptcy courts of the United States have been operating under a cloud of uncertainty since they were first established in 1978. The goal in 1978 was to achieve greater judicial efficiency by creating a single forum with comprehensive jurisdiction that could handle any matter affecting the bankruptcy estate.

The original system was ruled unconstitutional by the United States Supreme Court shortly after it became effective. *See Northern Pipeline Constr. Co. v. Marathon Pipe Line Co.,* 458 U.S. 50, 102 S.Ct. 2858 (1982). A revised jurisdictional scheme adopted in 1984 preserved much of the single forum concept, leaving the bankruptcy judges with broad jurisdiction over matters closely related to estate administration, but involving the district courts in less central matters. That scheme functioned reasonably well until four years ago, when the Supreme Court ruled that part of the remaining bankruptcy court jurisdiction was unconstitutional. *See Stern v. Marshall*, 564 U.S. ___, 131 S.Ct. 2594 (2011). The Supreme Court's reasoning was unclear and lower courts adopted

widely divergent interpretations of the decision. The more restrictive interpretations cast doubt on the bankruptcy judges' ability to adjudicate routine matters and threatened to disrupt the bankruptcy system.

That threat was significantly reduced by the recent May decision of the Supreme Court in *Wellness International Network, Ltd. v. Sharif.* ___ U.S. ___, 135 S.Ct. 1932 (May 26, 2015). Although the *Wellness* Court did not resolve whether the bankruptcy courts' jurisdictional grant was constitutional, it held that the parties to a proceeding before the bankruptcy court could consent to adjudication of the dispute by a bankruptcy judge. This consent approach should allow the bankruptcy courts to function normally in most cases. Parties generally will consent to adjudication by the bankruptcy judge because there is little incentive to withhold consent. However, there will be situations where the power to withhold consent may provide a party with a significant advantage. In those cases, the district court must become involved. The added expense, delay and uncertainty will diminish the benefits of the single forum concept. In addition, the line between matters that can be handled by a bankruptcy judge and those that must involve a district judge remains unclear, raising the risk of wasteful litigation over jurisdictional questions.

B. The Constitutional Challenge

The constitutional challenge presented by the bankruptcy court scheme centers on the question whether it is constitutionally permissible for the non-Article III bankruptcy judges to exercise the extensive jurisdiction granted under United States bankruptcy law. In 2011, the bankruptcy court system was upended by the Supreme Court's decision in *Stern v. Marshall* that struck down as unconstitutional part of the core jurisdiction of the bankruptcy courts. The provision at issue granted the bankruptcy court core jurisdiction over claims brought by the bankruptcy estate against a party who had filed a claim in the case. However, the counterclaim at issue was a state-

law-based tort claim against the creditor and not a claim based on bankruptcy law. Under the structural separation of powers approach, that delegation of jurisdiction to the non-Article III bankruptcy judge should have been constitutional since it presented little threat to the judiciary's independence. Four justices, writing in dissent, adopted that pragmatic approach and would have upheld the law.

However, Chief Justice Roberts, writing the majority opinion, took a formalistic approach to the Article III question. He focused primarily on the "liberty" interest protected by Article III. In his view, the Article III salary and tenure provisions protected liberty by ensuring that only an impartial judge could impose a judgment that might result in a loss of property. Unfortunately, the rationale of that opinion was very unclear, with Chief Justice Roberts articulating a number of reasons for invalidating the challenged jurisdictional provisions, not all of which were consistent.

This led to great confusion among the lower federal courts, with some courts adopting a very limited view of the *Stern* opinion that preserved most of the 1984 grant of core jurisdiction and others adopting an expansive interpretation that greatly restricted the bankruptcy courts' powers. Thus, in the years since *Stern,* it has been unclear whether the bankruptcy judges, acting without the involvement of a federal district judge, could issue many of the routine orders that are required for a successful restructuring or value-maximizing liquidation. That question remains unresolved even after the *Wellness* decision.

Stern not only created a conflict among the lower courts as to the permissible scope of the bankruptcy courts' core jurisdiction; it also created a conflict on the issue of whether the parties to the proceeding could waive the jurisdictional objection. The question was whether *Stern* merely established that litigants had a liberty right to have a life-tenured, salary-protected judge, or whether the opinion also set forth a structural separation-of-powers limitation on jurisdictional delegation.

The liberty aspect of Article III, as a personal right of the litigant, could be waived by a litigant. In contrast, the structural aspect of Article III serves the public interest by preserving the separation of powers and it cannot be waived by a party to the proceeding.

C. *Wellness* Reinterprets *Stern*

This is the question that was answered recently by the Supreme Court in *Wellness*. The *Wellness* appeal actually presented both the consent issue and the question of *Stern's* subject matter scope. The six-justice majority in *Wellness* chose not to address whether the bankruptcy court's jurisdictional grant was constitutional, leaving that issue unresolved. Instead, the Court decided the appeal on consent grounds. The Court interpreted *Stern* as establishing an individual right to an Article III judge in certain matters and not as erecting a structural separation-of-powers barrier to bankruptcy court adjudication. Thus, as long as the parties to a proceeding knowingly and voluntarily consent to having the matter adjudicated by the non-Article III bankruptcy judge, that judge can enter a final dispositive order.

It seems clear that *Wellness* represents a major shift by the Court. The majority opinion was written by Justice Sotomayor, one of the justices who had dissented in the *Stern* case. She employed the pragmatic approach that the dissenting opinion in *Stern* had advocated unsuccessfully. Chief Justice Roberts, who authored the *Stern* opinion, filed a vigorous dissent in *Wellness* arguing that *Stern* created a structural barrier that could not be waived by the parties.

The net effect of the *Stern* and *Wellness* decisions is that the bankruptcy courts will be able to function normally in most cases. *Stern* continues to lurk in the background, imposing unclear limits on the jurisdictional reach of the bankruptcy courts. However, Chief Justice Robert's dissenting opinion in *Wellness* may have reduced the uncertainty created by *Stern*. Interestingly, the Supreme Court never has upheld *any* exercise of jurisdiction by the non-Article III bankruptcy

courts. In each case raising a jurisdictional problem that has reached the Supreme Court, the Court struck down the challenged jurisdictional grant. Thus, even the exercise of basic jurisdiction over the estate was in question before the *Wellness* decision. Indeed, the court of appeals decision in *Wellness* interpreted *Stern* in that way.

D. 3 Plus 4 Means the Narrow Core is Constitutional

While the majority in *Wellness* did not address the jurisdictional question, the three dissenting justices did. Adopting an historical approach, they affirmed the principle that non-Article III bankruptcy judges could adjudicate "the restructuring of debtor creditor relations, which is at the core of the federal bankruptcy power." While the dissenters had a narrow view of what could be delegated, they would have upheld the "summary jurisdiction" that had been exercised by the bankruptcy referees under the pre-1978 law. In their view, the bankruptcy courts could constitutionally discharge debts, resolve claims, and adjudicate interests in the bankruptcy *res*. That jurisdiction extended to the recovery of assets in the actual or constructive possession of the debtor. This interpretation gives the bankruptcy judges jurisdiction to determine which assets are in the estate and to adjudicate some claims against non-consenting third parties. However, if the third party asserts a "substantial adverse" claim to the asset at issue, then only an Article III court can issue a final order.

While there still is no Supreme Court decision upholding any exercise of jurisdiction by the bankruptcy courts, at least seven of the nine sitting justices have joined opinions that would have authorized the summary jurisdiction allowed under the prior law. Thus the Supreme Court likely would uphold the portion of the core jurisdiction that includes the jurisdiction historically exercised by the bankruptcy referees. In light of this, the lower federal courts likely will allow the bankruptcy judges to issue final dispositive orders in such matters.

As a practical matter, the *Wellness* majority opinion's approval of consent will avoid the jurisdictional problem in most cases. Consent likely will be given in the great majority of cases because there will be little strategic reason for parties to withhold it. However, the risk remains that in some important matters, parties may withhold consent and subvert the single forum goal.

III. Bootstrapping and Post-Sale Disputes

A. Introduction

Because of the very broad reach of "related-to" jurisdiction, it is tempting to assume that the bankruptcy court's jurisdiction is nearly boundless. But courts have indeed drawn lines and refused to extend related-to subject matter jurisdiction in a number of instances. This section of the materials will explore several cases discussing attempts to "bootstrap" a dispute into a bankruptcy court's subject matter jurisdiction, and cases exploring the applicability of related-to jurisdiction to decide disputes arising after the sale of estate assets.

B. Can you "bootstrap" your way into bankruptcy court jurisdiction?

1. *In re TMT Procurement Corp.*, 764 F.3d 512 (5th Cir. 2014).

[This case summary is taken in large part from the author's article in the *ABI Journal*, titled "You Can't Bootstrap Yourself into Bankruptcy Court," ABI Journal, Vol. XXXIV, No. 1, p. 22 (January 2015)]

This case from the Fifth Circuit Court of Appeals involves admittedly unique facts that are unlikely to be encountered specifically again, but the case does stand for an important proposition concerning the limits of the reach of bankruptcy court related-to jurisdiction. In *TMT*, Vantage Drilling Co. initially brought a state court action (the Vantage litigation) against an individual (Hsin-Chi Su) alleging, among other things, breach of fiduciary duty, fraud,

fraudulent inducement, and negligent misrepresentation in connection with Vantage's earlier entry into contracts with companies controlled by Su for the acquisition of offshore drilling rigs and drill ships. In connection with those earlier transactions, Vantage issued shares of its stock to F3 Capital, a company controlled by Su, and granted Su seats on Vantage's board of directors. Vantage alleged that Su's misrepresentations placed Vantage in severe financial distress, creating a situation in which Vantage was unable to perform on various of its other critical contracts.

In 2013, twenty-three companies owned directly or indirectly by Su filed voluntary petitions for relief under chapter 11. At a hearing on a motion to dismiss the bankruptcy cases, Su offered to place approximately 25 million shares of Vantage stock held by F3 Capital into escrow to be administered by the bankruptcy court to secure compliance with court orders and to serve as collateral for post-petition borrowing. The bankruptcy court denied the motion to dismiss with respect to all but two of the debtors, and ordered that the 21 remaining debtors (the Debtors) "must cause non-estate property (the 'Good Faith Property') with a fair market value of $40,750,000 to be provided to the Estates," and that, if the Good Faith Property was not provided in cash, then it "must include at least 25,000,000 shares of the common stock of Vantage."

Thereafter, the Debtors requested approval of an escrow agreement by which F3 Capital would deposit 25 million shares of Vantage stock (the Vantage Shares) with the clerk of the bankruptcy court to be held *in custodia legis* for the benefit of the Debtors. Vantage, which was not a creditor of any of the Debtors, appeared as a party in interest before the bankruptcy court and opposed the Debtors' proposed escrow of the Vantage Shares. The bankruptcy court overruled Vantage's objections, finding that the Vantage Shares were not subject to a constructive trust as a matter of law such that they could be placed *in custodia legis* "without

complaint by any other party who has claimed ownership of the shares." The bankruptcy court further found that, because F3 Capital was not a party to the Vantage Litigation and F3 Capital received the Vantage Shares prior to the commencement of the Vantage Litigation, due process prevented F3 Capital from being deprived of its property in the Vantage Litigation. Accordingly, the bankruptcy court entered an order (the Escrow Order) authorizing the escrow of the Vantage Shares and providing, among other things, that the stock would serve as collateral for working capital loans of the Debtors.

The district court withdrew the reference to the bankruptcy court, denied leave to appeal, and set a hearing to reconsider, among other issues, Vantage's objections to the Escrow Order. Before the district court hearing, the Debtors filed an emergency motion requesting permission to borrow up to $20 million in post-petition financing secured by the Vantage Shares. The district court entered an interim order authorizing an initial loan of $6 million and granted Macquarie Bank Limited (the DIP Lender) a first-priority lien and security interest in the Vantage Shares then held in escrow. The interim order provided that the DIP Lender's interests in the deposited Vantage Shares could not be compromised by any subsequent order of the bankruptcy court or of the state court in the Vantage Litigation, and that the DIP Lender had extended financing to the Debtors in good faith and was entitled to "the full protections of sections 363(m) and 364(e) of the Bankruptcy Code." The district court then re-referred the action to the bankruptcy court where the bankruptcy court approved the extension to the Debtors of the full $20 million post-petition financing requested by the Debtors pursuant to orders containing terms similar to those of the district court order. Vantage timely appealed the orders of the district court and the bankruptcy court to the Fifth Circuit.

The primary issue on appeal was the DIP lender's argument that the Vantage appeal was

moot pursuant to sections 363(m) and 364(e) of the Bankruptcy Code. The Fifth Circuit rejected that argument because the arguments raised by Vantage in its litigation against Su went to the very heart of the ownership of stock, and with that notice of an adverse claim to the shares, the DIP lender had adequate notice of the potential cloud on title. More importantly for purposes of this seminar, the Fifth Circuit also found that the bankruptcy court lacked subject matter jurisdiction over the Vantage Litigation, and therefore did not have authority to enter the DIP financing orders that essentially deprived Vantage of ownership of the disputed shares. The Debtors and DIP lender had argued that because the shares had been pledged as collateral for the post-petition loan pursuant to the bankruptcy court order, those shares thereby became property of the estate under section 541 of the Code, and therefore fell under the bankruptcy court jurisdiction. The appeals court rejected that argument, and held that the Debtors could not rely on the DIP financing orders by which the disputed Vantage Shares became property of the estate because the district court did not have the authority to enter that order unless those shares were already property of the estate. Stated otherwise, "[t]he bankruptcy court and the district court could not manufacture *in rem* jurisdiction over the Vantage Shares by issuing orders purporting to vest the Debtors with a post-petition interest in the Vantage Shares" as such "jurisdictional bootstrap[s]" would impermissibly allow the district court and bankruptcy court to "exercise jurisdiction that would not otherwise exist."

The aspect of the Fifth Circuit's opinion that may have the most far-reaching impact is the court's refusal to extend the bankruptcy court's "related-to" jurisdiction in a manner that would constitute the adjudication of Vantage's claim in the Vantage Litigation. Recognizing that the Supreme Court read "related-to" jurisdiction broadly in *Celotex* to cover non-debtor actions involving non-estate property that nonetheless affect the estate, the Fifth Circuit found

that no justifiable basis for the exercise of jurisdiction over the Vantage Litigation existed given that the "only discernable [*sic*] link between the Vantage Litigation and the Debtors' [c]hapter 11 proceedings is that F3 Capital and the Debtors' have a common owner" and that absent the bankruptcy court's actions "the resolution in the Vantage Litigation would not have had any effect on the bankruptcy."

In finding that "related-to" jurisdiction did not exist, the Fifth Circuit rejected the Debtors' arguments that core jurisdiction to enter the orders in question existed because the orders dealt with administration of the estate, the acquisition of credit, and the use of property, and the court found instead that the Vantage Litigation was not even a non-core proceeding because there was no "related-to" jurisdiction. Nor was the court swayed by the Debtors' argument that affording Vantage due process in the bankruptcy and district courts passed jurisdictional muster. In so holding, the Fifth Circuit made clear that a subject-matter jurisdiction inquiry must precede due-process inquiries and inquiries under 28 U.S.C. § 157 as to whether proceedings are core or non-core.

2. *In re Digital Impact, Inc.*, 223 B.R. 1 (Bankr. N.D. Okla. 1998).

This case arose out of a request for confirmation of the plan of reorganization proposed by a non-debtor. The proposed plan contain a release provision, purporting to release all claims against the plan proponent, of any nature whatsoever, held by any person bound by the plan. In other words, a fairly typical, broad third-party release provision. The bankruptcy court reviewed the history of non-debtor release provisions and the various statutory provisions and case law construing those provisions. As the starting point of its analysis, however, the bankruptcy court explored whether or not it had subject matter jurisdiction sufficient to authorize the releases.

The court noted that the bankruptcy court's subject matter jurisdiction extends to *cases*

under title 11, or *proceedings* arising under or arising in or related to a case under title 11. The cases and controversies that the plan proponent sought to be released from were disputes that might arise between the plan proponent (a non-debtor) and third-party claimants against the plan proponent, who might also happen to be creditors of the debtor in bankruptcy. Those cases and controversies are not cases under title 11 and do not arise under the title 11 case. The court conceded that the claims might be considered "arising in" or "related to" a bankruptcy case, but that would only be true because the plan proponent inserted the release in the plan. This attempt at bootstrapping of subject matter jurisdiction troubled the court: "If proceedings over which the Court has no independent jurisdiction could be metamorphisized into proceedings within the Court's jurisdiction by simply including their release in a proposed plan, this Court could acquire infinite jurisdiction."

The bankruptcy court then analyzed whether the released claims and controversies were related to the bankruptcy case under the *Pacor* test, and found that adjudication of third-party claims against the plan proponent would have no effect on the estate whatsoever. The court noted that a permanent injunction of the sort requested by the plan proponent amounted to the final adjudication of the anticipated legal action against the plan proponent, and as such, "all jurisdictional and due process prerequisites for such a final adjudication must be satisfied." Because the outcome of potential litigation by third parties against the non-debtor plan proponent would not affect the estate, the court found that it lacked jurisdiction to entertain and enjoin those actions, and denied confirmation of the plan.

See also, Eamonn O'Hagan, *On a "Related" Point: Rethinking Whether Bankruptcy Courts Can "Order" the Involuntary Release of Non-Debtor, Third-Party Claims*, 23 Am. Bankr. Inst. L. Rev. 531 (2015), exploring in more depth the jurisdictional basis — or lack

thereof — for bankruptcy courts to authorize non-debtor releases in chapter 11 plans. The article's author suggests that plan confirmation opponents raise the lack of subject matter (related-to) jurisdiction early and often in the plan confirmation process.

3. *In re Charles Street African Methodist Episcopal Church of Boston*, 499 B.R. 66 (Bankr. E.D. Mass 2013).

This case takes the opposing point of view concerning subject matter jurisdiction to authorize non-debtor, third-party releases in a Chapter 11 plan of reorganization. Faced with a challenge that such proposed releases were "beyond the outer, 'related-to' reaches of bankruptcy jurisdiction," the court dismissed those objections. Calling confirmation of a plan "the quintessential bankruptcy matter," the court explained that plan confirmation is not "the mere adjudication of a single claim . . . but a unitary omnibus civil proceeding for the reorganization or adjustment of all obligations of the debtor and disposition of the debtor's assets." Without any significant analysis of whether or not the claims that were proposed to be released could conceivably have any effect on the administration of the bankruptcy estate, the bankruptcy court simply held that it was "well satisfied" that the release was related to this case and therefore was easily within the court's subject matter jurisdiction.

4. *Abramowitz v. Palmer*, 999 F.2d 1274 (8th Cir. 1993).

This case does not deal with plan confirmation, but is an example of a case where a sort of bootstrapping was accepted to create subject matter jurisdiction. Pre-petition, the debtor, Dr. Palmer, sold his dental practice to Dr. Abramowitz. Dr. Palmer and his wife then moved into a new home, and used a portion of the sale proceeds to purchase the home. The husband and wife owned the home as tenants by the entirety. Following the purchase of the dental practice, Dr. Abramowitz discovered a number of instances of alleged fraud by Dr. Palmer, and filed a lawsuit

against Dr. Palmer alleging breach of contract and fraud in the sale of the dental practice. Dr. Palmer thereafter filed chapter 7 bankruptcy. Dr. Abramowitz brought an adversary proceeding in the bankruptcy case incorporating his state court complaint and specifically seeking a judgment against the debtor and his wife for fraud. Dr. Abramowitz further requested that the debt relating to the underlying claim be declared nondischargeable. The bankruptcy court entered judgment against Dr. and Mrs. Palmer on the fraud claim, found that the debt to Dr. Abramowitz was nondischargeable, and held that the Palmers held their home in constructive trust for Dr. Abramowitz.

On appeal, Mrs. Palmer contended that bankruptcy court lacked subject matter jurisdiction to enter any judgment against her and therefore also lacked subject matter jurisdiction to issue any orders relating to the couple's home. Applying the "related-to" jurisdiction analysis, the appeals court found that the bankruptcy court did indeed have subject matter jurisdiction to adjudicate Mrs. Palmer's interest in the home. Under applicable state law, Dr. Abramowitz could only have exercised any remedies against the Palmers' home (as entirety property) if both spouses had acted jointly to encumber the property. Thus, because the bankruptcy court had determined that Mrs. Palmer was liable for fraud with her husband, the bankruptcy court therefore had subject matter jurisdiction to be able to decide whether Dr. Abramowitz could impose a constructive trust on the home.

C. Are post-sale disputes still "related to" the bankruptcy case?

1. *In re Xonics, Inc.*, 813 F.2d 127 (7th Cir. 1987).

This case involved a dispute between two secured creditors claiming security interests in receivables of the debtor. During the chapter 11 case, the two creditors agreed to place certain disputed collateral proceeds in escrow, with their respective rights to be determined later. In the

meantime, the bankruptcy court confirmed a plan of reorganization. Under the plan, the debtor abandoned the accounts receivable in which the competing creditors claimed interests. The bankruptcy court then determined that it no longer had subject matter jurisdiction to decide competing claims to collateral proceeds because that property was no longer property of the bankruptcy estate. One of the two secured creditors argued that the bankruptcy court could indeed determine ownership of the proceeds because of its continuing power to enforce its earlier escrow order. In other words, the creditor argued that "once a bankruptcy court acquires jurisdiction of a dispute, the power to decide lasts forever." The Seventh Circuit disagreed because the outcome of the dispute between the two competing secured creditors would have no effect on the distribution of property to creditors or administration of the estate. The court held that "related-to" jurisdiction only exists when the outcome of the dispute affects the amount of property available for distribution or the allocation of property among creditors. Because the plan effected an abandonment of the collateral proceeds, the case did not involve an identification of the debtor's property interests nor would it increase or decrease the amount of money distributable creditors. However, the determination of ownership of the disputed funds might work to reduce the outstanding claim of one or the other creditor. In turn, that creditor's *pro rata* share of the pool of funds set aside under the plan for distribution to creditors would be reduced, thereby potentially increasing the percentage recovery for other creditors. The Seventh Circuit concluded "that effects on other creditors do matter," and remanded the case to the district court to determine whether disposition of the competing claims to the funds would indeed have any effect on payments to other creditors. If so, related-to subject matter jurisdiction would exist under 28 U.S.C. § 157(c)(1).

2. *Zerand-Bernal Group, Inc. v. Cox*, 23 F.3d 159 (7th Cir. 1994).

A chapter 11 debtor sold substantially all of its assets to a purchaser under a bankruptcy court order approving the sale free and clear of all liens, claims, or encumbrances. The sale order further provided that the bankruptcy court reserved jurisdiction to enforce the sale agreement. A few months later, the debtor confirmed a plan of liquidation, which provided for the creation of a trust fund from the sale of the debtor's assets and specified how the trust fund proceeds were to be allocated among creditors. The plan also provided that the bankruptcy court was to retain exclusive jurisdiction to enforce the sale agreement with the purchaser. Several years later, the plaintiff (who had not been a creditor or participant in the bankruptcy case at all) brought a personal injury/products liability claim against the purchaser and the debtor based upon an injury allegedly caused by a machine manufactured by the debtor well before the sale. The asset purchaser commenced an adversary proceeding in bankruptcy court seeking to enjoin the plaintiff from proceeding against the purchaser based upon the free and clear provisions of the sale agreement. The bankruptcy court determined that it lacked jurisdiction over the adversary proceeding and dismissed. On appeal, the Seventh Circuit held that the bankruptcy court had neither "arising-under" nor "related-to" jurisdiction over the adversary proceeding. The appeals court noted that the products liability suit was not a claim either by or against the debtor, and that the suit could not possibly affect the amount of property available for the debtor's creditors because all of that property had already been distributed. Thus, the plaintiff' products liability suit and the asset purchaser's adversary complaint were not related to the chapter 11 case, and had been properly dismissed for lack of subject matter jurisdiction.

3. *In re Ray*, 624 F.3d 1124 (9th Cir. 2010).

Several years prior to the commencement of its bankruptcy case, the debtor and another

party reached an agreement for the proposed sale of certain real property to a purchaser (Purchaser). The sale agreement also included a right of first refusal in favor of the Purchaser for a parcel of real property (the ROFR Property) adjacent to the property originally sold. The debtor later filed chapter 11, and ultimately confirmed a plan of reorganization that referenced the previous proposed sale of the property, but also noted that the property sale had not yet closed due to various environmental issues. Sometime later, the debtor and his co-owner apparently agreed to sell the ROFR Property to a third party. Eventually, a dispute arose under which the Purchaser claimed that the debtor had failed to honor the right of first refusal in its original contract, and sought specific performance as well as certain monetary damages. By then, the bankruptcy case had been closed, but the debtor reopened the case and asked the bankruptcy court to assert jurisdiction over the dispute because of its effect on the earlier sale order in the case. The bankruptcy court reluctantly asserted jurisdiction and denied the Purchaser's claims.

On appeal, the Ninth Circuit reviewed the issue of whether the bankruptcy court had jurisdiction to make any determination on the Purchaser's claim. The court first found that the Purchaser's state court action did not arise under or arise in the bankruptcy case, but rather was a simple breach of contract action under Washington state law. The claim was created under state law rather than as a part of the bankruptcy proceeding, and thus those bases for jurisdiction did not exist. The Ninth Circuit further rejected the assertion of "related-to" jurisdiction because the contract action did not bear any close nexus to the bankruptcy case. The bankruptcy case had concluded and the assets had been distributed, and thus the outcome of the breach of contract action would have no effect on the bankruptcy case. As such, the breach of contract action was not related to the chapter 11 case, so the bankruptcy court did not have jurisdiction to hear it.

4. *In re Farmland Industries, Inc.*, 567 F.3d 1010 (8th Cir. 2010).

This case involved a post-sale challenge (after a § 363 sale) brought by a failed bidder alleging, among other things, conspiracy and intentional interference with the bankruptcy sale process. The claim was asserted against certain individual former officers of the debtor, as well as other parties. The liquidating trustee of the debtor's estate was under an obligation to indemnify the former officers concerning the performance of their duties to the estate, and as a part of that obligation, the liquidating trustee was paying the legal fees incurred to defend individuals from the present dispute. The Eighth Circuit ultimately determined that the bankruptcy court did not have "arising in" or "arising under" jurisdiction to hear the failed bidder's complaint. However, the claim was "related to" the chapter 11 case because the estate was actually paying legal fees of the non-debtor defendants under the estate's indemnification obligations. The court did not have to speculate about whether the estate's indemnification claims could conceivably arise in the future, because they were already in existence and costing the estate money. Accordingly, the bankruptcy court had jurisdiction to hear the dispute. *See also Buffets, Inc. v. Leischow*, 732 F.3d 889 (8th Cir. 2013) (related-to jurisdiction existed where bankruptcy estate was obligated to indemnify non-debtor defendants for attorney's fees and other amounts).

IV. Disputes Between Non-Debtors

A. Introduction

As noted above, there is no question that Congress' grant of "related to" subject matter jurisdiction under 28 U.S.C. §1334(b) is very broad and includes a claim that "portends a mere contingent or tangential effect on a debtor's estate." *In re Titan Energy*, 837 F.2d 325, 330 (8th

Cir. 1988). The statutory grant of subject matter jurisdiction contained in the "related to" provision is not unbounded. As the Seventh Circuit has noted, common sense cautions against an open reading of "related to" jurisdiction under 28 U.S.C. §1334(b) given the modern economic climate where "everything is related to everything else." *In re FedPack Sys, Inc.*, 90 F.3d 207, 214 (7th Cir. 1995). Rather, a cause of action is related to the bankruptcy case under 28 U.S.C. § 1334(b) only if its outcome could conceivably affect the amount of property available for distribution or the allocation of property among the unsecured creditors. *In re Reeves*, 65 F.3d 670, 675 (8th Cir. 1995).

The Fifth Circuit has held that in the non-debtor versus non-debtor context, the court's "related to" jurisdiction under §1334(b) is limited to those actions where the subject of the dispute is property of the estate or where the dispute over the asset in question would have an effect upon the debtor's estate. *Feld v. Nat'l Union Fire Ins. Co. (In re Zale Corp.)*, 62 F.3d 746, 753 (5th Cir. 1995). The Fifth Circuit also noted that judicial economy or the facilitation of a settlement of a dispute within the bankruptcy case cannot provide the basis of "related to" jurisdiction with respect to claims involving third parties. *Id*. For example in *Zale Corp.*, the debtor attempted to settle a claim with its insurers by including a provision in the settlement agreement whereby third parties would be enjoined from bringing any bad faith claims against the insurers. *Id*. at 750. The Fifth Circuit held that the bankruptcy court did not have "related to" jurisdiction under § 1334(b) to approve the settlement as it related to the injunction in favor of the insurers on the bad faith claims because the potential bad faith claims against the insurers simply did not involve any asset of the estate nor could those claims in any way effect the estate. *Id*. at 753-54. The Fifth Circuit specifically rejected the argument that because the bankruptcy court had subject matter jurisdiction over the debtor's attempt to settle its dispute with its

insurer, the court had jurisdiction over the discrete claims embodied in the dispute and each of those claims shared common facts. *Id*. Rather, each of the claims must separately involve an asset of the estate or involve a dispute over an asset that would have an effect upon the estate. *Id*.

B. Procedural Issues.

There are a number of procedural issues that will affect the analysis of whether the bankruptcy court possesses related-to jurisdiction over a claim involving non-debtors.

1. Application of the well-pleaded complaint rule to cases removed under 28 U.S.C. § 1452(a)

First, the well-pleaded complaint rule applies to cases removed to bankruptcy court under 28 U.S.C. § 1452(a), the bankruptcy removal statute. *Rivet v. Regions Bank of Louisiana*, 522 U.S. 470, 477 (1998). Thus, a court may only review the well-pleaded allegations contained in the complaint itself, and not the answer, to determine if the court has related-to jurisdiction over the action under § 1334(b) so that removal was proper under § 1452(a). *Yangming Marine Transp. Corp. v. Electri-Flex Co.*, 682 F.Supp. 368, 370 (N.D. Ill 1988).

For example in *Electri-Flex*, the plaintiff brought a state law breach of contract claim against defendant. Defendant removed the action under § 1452(a), arguing that the plaintiff's contact was with a third party that had filed a petition for relief in Texas. The district court held that under the well-pleaded complaint rule, its review of whether it had related-to jurisdiction under § 1334(b) for removal purposes under § 1452(a) was limited to only the face of the plaintiff's complaint. Accordingly, because the plaintiff had merely asserted a state law breach of contract claim, the district court held that it lacked related-to jurisdiction under § 1334(b) and the matter should be remanded to the state court.

It should be noted that there is small minority of courts that hold that the well-pleaded complaint rule applies only to actions based on the general federal-question jurisdiction statute contained in 28 U.S.C. § 1331, and that it does not apply to cases removed under §1452 based on the court's related-to jurisdiction under § 1334(b). *See e.g. Meritage Homes Corp. v. JP Morgan Chase Bank, N.A.*, 474 B.R. 526, 562 n.37 (Bankr. S.D. Ohio 2012). This line of cases, however, ignores the fact that in *Rivet*, the Supreme Court held that a defendant's removal of a state law claim based on its defense that the claim had been disposed of in its prior bankruptcy was subject to the well-pleaded complaint rule. *Rivet*, 522 U.S. at 477. Further, the Supreme Court has noted that the underlying principle of the well-pleaded complaint rule is to promote a "consistent application of a system of statutes conferring original federal court jurisdiction." *Franchise Tax Bd. Of State of California v. Constr. Laborers Vacation Trust*, 463 U.S. 1, 27 (1983). Thus, the vast majority of courts that have addressed the issue have held that the well-pleaded complaint rule applies in cases removed under § 1452(a) based on related-to jurisdiction under § 1334(b). *See Conseco, Inc. v. Adams (In re Conseco, Inc)*, 318 B.R. 425, 430 (Bankr. N.D. Ill. 2004).

2. The party invoking the court's related-to jurisdiction under 28 U.S.C. § 1334(b) has the burden of proof on the issue.

An often overlooked point is that just as with any other jurisdictional statute, the party invoking the court's related-to jurisdiction has the burden of proof on the issue. *Cardinalli v. Superior Court of Cal. For Monterey*, 2013 U.S. Dist. LEXIS 160687, *14 (N.D. Cal. Nov. 7, 2013); *Schafer v. Nextiraone Fed., LLC*, 2012 U.S. Dist. LEXIS 83737 (M.D.N.C. June 18, 2012). Thus, the party invoking the court's related-to jurisdiction under § 1334(b) must adduce evidence showing that the resolution of the dispute between the non-parties either involves an asset of the estate or that the resolution of the dispute will have a direct impact on the

administration of the estate. *In re Combustion Eng'r, Inc.*, 391 F.3d 190, 232-33 (3d Cir. 2004). For example in *Combusion Eng'r*, the Third Circuit held that a non-debtor party failed to establish that a dispute between it and the debtor's insurer was related to the debtor's case based on shared insurance policies when the record on appeal failed to include the terms and operations of those policies. *Id*. at 232.

3. The determination whether the court has subject matter jurisdiction over the claims based on the related-to provision of § 1334(b) must be made at the time its jurisdiction is invoked.

A determination whether a court has related-to jurisdiction over a claim involving non-debtor parties must be made at the outset of the dispute. *Zale Corp.*, 62 F.3d at 759. Thus for example, in *Meritage Homes*, a dispute involving two non-debtors was removed to the bankruptcy court under § 1452(a) based on the bankruptcy court's related-to jurisdiction under § 1334(b). *Meritage Homes*, 474 B.R. at 559. At the time of the removal, the outcome of the action could have had a significant impact on the debtors' ability to formulate a confirmable plan. While the removed action was pending, the constituent groups reached an agreement on a plan, which the bankruptcy court confirmed. The plaintiff then filed a motion to remand the case, contending the bankruptcy court no longer had related-to jurisdiction over the matter because the confirmation issues had been resolved. The bankruptcy court rejected this argument and held that because it had related-to jurisdiction over the removed action under § 1334(b) on the removal date, the subsequent resolution of the plan confirmation issues did not divest it of that jurisdiction. *Id*. at 560.

4. Specific situations involving non-debtor disputes

a. Disputes between non-debtors that affect the debtor's ability to reorganize.

The Supreme Court observed in *Celotex* that a court's related-to jurisdiction under 28 U.S.C. § 1334(b) is broader in a Chapter 11 context than in a liquidation under Chapter 7. *Celotex*, 514 U.S. at 310. The Court noted that a broader range of disputes between non-debtors will likely be implicated when an ongoing business is attempting to reorganize its debt and capital structure under Chapter 11. *Id*. at 310-11.

For example in *Celotex*, tort victims obtained a judgment against the debtor prepetition in the United States District Court for the Northern District of Texas. The debtor's insurer issued a surety bond to stay execution under Rule 64. The Fifth Circuit affirmed the judgment in favor of the tort victims. The same day that the Fifth Circuit issued its opinion, the debtor filed its petition for relief under Chapter 11 in the United States Bankruptcy Court for the Middle District of Florida.

The tort victims then filed a motion with the district court to enforce the surety bond under Rule 65.1 against the debtor's insurer. The debtor filed an adversary proceeding seeking an order from the bankruptcy court under §105(a) to enjoin the tort victims from prosecuting their action against the debtor's insurer on the surety bond. The debtor argued, *inter alia*, that the bankruptcy court had subject matter jurisdiction over its claim to enjoin the tort victims from prosecuting their claim against the non-debtor insurer because the debtor had agreed that the insurer could reduce the amount that it owed the debtor under a settlement agreement by the amount that the insurer had to pay to the tort victim on the surety bond.

The bankruptcy court granted the debtor's request for temporary and preliminary

injunctive relief. The tort victims, however, ignored the bankruptcy court's order and continued to prosecute their claim on the surety bond against the insurer in the district court. Both the district court and the Fifth Circuit held that the bankruptcy court's order was invalid because it did not have the power under § 105(a) to enjoin an action between non-debtors that did not involve property of the bankruptcy estate.

The Supreme Court reversed. The Court noted with respect to the subject matter jurisdiction question that the related-to provision of § 1334(b) was a dramatic departure from the 1898 Bankruptcy Act, which premised jurisdiction solely on possession of the *res* of the estate or consent. *Id*. at 308. The Court agreed with the Third Circuit's observation in *Pacor* that the related-to provision of § 1334(b) was a Congressional grant of authority sufficient to allow the district court to deal efficiently and expeditiously with all matters concerning the administration of the estate, not just the possession of property. *Id*. Further, although the Court did not expressly adopt the *Pacor* test, it strongly suggested that that "conceivable effect" test was proper under § 1334(b).

The Court observed that allowing the judgment creditor to execute on the surety bond issued by the debtor's insurer, along with the potential for similar actions against 227 other surety bonds, could significantly impede the debtor's ability to reorganize. This result flowed from the prepetition settlement agreement, which would allow the insurer to reduce the cash it was to pay the debtor under the settlement agreement by the amount it paid on the bonds.

It should be noted that the Court's opinion in *Celotex* is not premised on the debtor's derivative liability to the insurer on the surety bond. Rather, the Court's holding that the bankruptcy court had subject matter jurisdiction over the debtor's request to enjoin the tort creditors' action was premised solely on the fact that the debtor's ability to reorganize would be

significantly hampered by the reduction of the cash the debtor would receive under the settlement agreement. Thus, it is highly likely that if *Celotex* had filed a Chapter 7 or even a liquidating Chapter 11, the tort creditors' claim against the insurer on the surety bond would not have been "related to" Celotex's bankruptcy under § 1334(b).

b. Disputes involving the debtor's insurer.

Courts have readily found that disputes between a third party and the debtor's insurer were related to the debtor's bankruptcy case under § 1334(b) provided the outcome of the dispute would affect the estate's liability to the third party. In *Titan Energy*, the debtor's insurer refused to pay a claim asserted by an entity that had purchased an ethanol plant from the debtor. *In re Titan Energy*, 837 F.2d 325, 326 (8th Cir. 1988). The purchaser filed a claim in a Louisiana state court against the insurer on the insurance policy. The debtor then filed a petition for relief in the United States Bankruptcy Court for the Western District of Missouri. The insurer then filed a declaratory judgment action in the bankruptcy court asking the bankruptcy court to declare that the insurer had no liability to the purchaser under the policy and to stay the state court action.

The bankruptcy court dismissed the insurer's declaratory judgment action for lack of subject matter jurisdiction, finding that the dispute involved "strangers" to the bankruptcy estate, but the Eighth Circuit reversed. The Circuit first noted that the insurance policies themselves were property of Titan's estate under § 541(a), although any payment on the purchaser's claim would flow directly to the purchaser and not through the estate. *Id*. at 329. The Circuit also observed that if the purchaser prevailed on its claims against the insurer then it would not have a claim against the debtor's estate. *Id*. On the other hand, if the insurer prevailed, then the purchaser would become a general unsecured creditor, which would reduce the distributions to

the other creditors. *Id*. Relying on *Pacor*, the Circuit held that because the purchaser's claim against the insurer had the potential to affect the amount of cash that would be distributed to each unsecured creditor of the debtor's estate, that claim was related to the debtor's bankruptcy case under § 1334(b). *Id*. at 330.

The Sixth Circuit in *Dow Corning* addressed the question whether claims by tort creditors against non-debtors who were co-insureds with the debtor were related to the debtor's estate under § 1334(b). *Lindsey v. O'Brien (In re Dow Corning Corp.)*, 86 F.3d 482, 494 (6th Cir. 1996). The insurance policies had a combined limit of $1 billion in coverage, and the insurers had already paid approximately $400,000,000 to Dow Corning. Further, the Sixth Circuit noted that if the tort victims were allowed to collect against the non-debtors, the non-debtors' claims on the joint insurance policies would likely consume the remaining $600,000,000 of coverage. Thus, if the tort victims were to recover against the non-debtors, the Circuit found that a possibility existed that the insurance policy would not cover the remaining claims against the debtor's estate. Thus, the Circuit held that the claims against the non-debtors were related to Dow Corning's estate under § 1334(b) and the *Pacor* conceivable effect test. *Id*.

A third-party claim against a debtor's insurer, however, still must directly affect the administration of the debtor's estate in order for that claim to be "related to" the debtor's case under § 1334(b). For example in *Zale*, the debtor and its insurer reached a settlement agreement with respect to the insurer's liability to the debtor on an insurance policy. *In re Zale*, 62 F.3d 746, 749 (5th Cir. 1995). The settlement agreement contained an injunction prohibiting any party from asserting claims against the insurer relating to the policy in question. The settlement agreement also required the debtor to indemnify the insurer for any liability it incurred in defending against claims made against it.

A third party objected to the settlement, contending that the bankruptcy court did not have subject matter jurisdiction to enjoin its claims against the non-debtor insurer. Specifically, the third party intended to file both a bad faith claim sounding in tort and a breach of contract claim against the debtor's insurer. The Fifth Circuit held that the third party's potential bad faith claim against the insurer was not related to the debtor's bankruptcy case for purposes of § 1334(b). *Id*. at 755. The Circuit first noted that the proceeds of any bad faith claim against the insurer could not affect the estate because the proceeds of that claim would not pass to the estate. Further, the Circuit held that because the bad faith claim against the insurer was not premised on the debtor's conduct, the indemnification provision in the settlement agreement could not provide the bankruptcy court with related-to jurisdiction over the claim that it would not otherwise have. *Id*. at 756.

c. Indemnification and contribution claims.

Perhaps the most litigated issue involving a bankruptcy court's related-to jurisdiction over claims between non-debtors concern the scope of the debtor's derivative liability on such claims under the doctrines of contribution and indemnification. The Third Circuit's seminal opinion in *Pacor* itself addressed this issue directly. In *Pacor*, the Circuit found that a claim against a non-debtor for damages caused by asbestos supplied by the debtor was not sufficient to provide the bankruptcy court with related-to jurisdiction over the claim. *Pacor*, 743 F.2d at 995. The Third Circuit's holding was premised on the fact that the claim against the non-debtor would not establish the debtor's liability on the contribution or indemnification claim. *Id*.

The Third Circuit continues to reject related-to jurisdiction over disputes between non-debtors that do not directly result in the debtor's derivative liability under theories of indemnification and contribution. *See W.R. Grace & Co. v. Chakarian (In re W.R. Grace & Co)*,

591 F.3d 164, 173 (3d Cir. 2009). At least one district court within the Eighth Circuit has adopted the Third Circuit's view that disputes between non-debtors are not within the ambit of a court's related-to jurisdiction under § 1334(b) if the debtor's derivative liability must be determined in a subsequent action. *Transamerican Finan. Life Ins. Co. v. Merrill Lynch & Co. Inc.*, 302 B.R. 620, 626 (N.D. Iowa 2003).

The Sixth Circuit, however, has adopted a much broader view of the court's related-to jurisdiction over claims between non-debtors based on the debtor's potential derivative liability. In *Dow Corning*, the Sixth Circuit held that Dow Corning's potential common-law derivative contribution and indemnification liability stemming from tort claims asserted against entities to which it had supplied silicone for silicone breast implants was sufficient to provide related-to jurisdiction over those claims under § 1334(b). *Dow Corning*, 86 F.3d at 494. The Circuit did note, however, that unlike *Pacor*, the tort claims at issue were large in both number and liability. *Id*. Thus, the debtor's contingent indemnification and contribution liability stemming from the non-debtor litigation significantly threatened the debtor's ability to effectively reorganize. *Id*.

The Fifth Circuit has held that a court has related-to jurisdiction over litigation between non-debtors when the debtor's obligation to indemnify one of the parties to the litigation is contractually based. *In re El Paso Refinery*, 302 F.3d 343, 349 (5th Cir. 2002). This results even if there are several parties and contracts that must be linked together in order to establish the debtor's indemnification liability. *Id*.

V. Related-To Jurisdiction in Consumer Cases

A. Introduction

Questions about related-to jurisdiction don't come up very often in consumer cases, but

they are raised occasionally. Perhaps the most common situation where they are raised is when a creditor takes some action against the debtor after the debtor has received a discharge, and the debtor returns to the bankruptcy court to sue the creditor for violating a federal or state consumer protection law of some kind, as well as the discharge injunction (§ 524 of the Bankruptcy Code). Courts typically rule that they have jurisdiction of the claim based on the discharge injunction because it arises under the Bankruptcy Code, but that a claim under a consumer protection law is not related to the debtor's bankruptcy case because it can have no effect on the bankruptcy estate, so the court has no related-to jurisdiction over it. As stated earlier, bankruptcy courts generally rule that they cannot exercise supplemental jurisdiction under 28 U.S.C. § 1367, so they conclude they must dismiss the consumer protection law claim even though it is based on a "common nucleus of operative fact" with the debtor's claim under the discharge injunction.

Another situation in consumer cases where bankruptcy courts are likely to find they don't have related-to jurisdiction is when a dispute involves parties other than the debtor, such as third-party complaints for indemnity or contribution. Of course, like most areas of bankruptcy, there are occasional cases where the court reached the opposite result, concluding it did have related-to jurisdiction of such a dispute.

Many dischargeability complaints are filed in consumer cases. Some courts have questioned bankruptcy courts' jurisdiction to enter a money judgment specifying the amount of the debt they determined was excepted from the debtor's discharge. However, both the 8th and 10th Circuits have now ruled that bankruptcy courts do have such jurisdiction. *See Islamov v. Ungar (In re Ungar)*, 633 F.3d 675, 679-80 (8th Cir. 2011); *Johnson v. Riebesell (In re Riebesell)*, 586 F.3d 782, 792-94 (10th Cir. 2009).

Bankruptcy jurisdiction can be so confusing that in at least one published decision, a

bankruptcy court ruled that a garnishment proceeding to enforce the court's own judgment did not fall within the court's arising-in or arising-under jurisdiction, and was not even related to the debtor's bankruptcy case, so the court had no jurisdiction over it at all.

B. Consumer cases finding no related-to jurisdiction

1. Claims arising after the debtor gets a discharge, or the case is dismissed

a. *Educ. Credit Mgmt. Corp. v. Kirkland (In re Kirkland)*, 600 F.3d 310, 316-18 (4th Cir. 2010)

A Chapter 13 debtor completed a confirmed plan that provided for full payment of three student loan debts. However, due to errors made by the Chapter 13 trustee, two of the claims received overpayments, which were refunded to the debtor, and the other received no payments, leaving the full principal still owed. The holder of the third student loan tried collect from the debtor, and eventually, she filed a complaint seeking a determination that her obligation on the third debt had been discharged, although she conceded she still owed any postpetition interest that had accrued while she was making her plan payments. The bankruptcy court ruled the debtor still owed the debt, and went on to determine the amount of postpetition interest she owed, and denied the creditor's claim for collection costs based on a lack of proof. On appeal, the creditor questioned the bankruptcy court's subject matter jurisdiction over the postpetition interest and collection costs the creditor was entitled to as the result of a default on the student loan that occurred after the Chapter 13 estate was closed and the debtor was discharged, but the district court affirmed. On further appeal, the Fourth Circuit reversed, finding the bankruptcy court had no subject matter jurisdiction of the postpetition interest and collection costs. The circuit said for related-to jurisdiction to exist after confirmation, a claim must affect an integral

aspect of the bankruptcy process, and involve a close nexus to the bankruptcy plan or proceeding. The creditor's claims for postpetition interest and post-default collection costs did not meet this test because (1) the creditor could not have included postpetition interest in its proof of claim and the trustee could not have paid such interest, and (2) the claim for collection costs did not arise until the debtor defaulted on the debt and that did not happen until after the debtor had completed her plan and been discharged.

b. *Vienneau v. Saxon Capital, Inc. (In re Vienneau)*, 410 B.R. 329, 333-37 (Bankr. D. Mass. 2009)

The Chapter 7 debtors filed an adversary complaint against various defendants, claiming their postpetition actions violated (1) the automatic stay, (2) the discharge injunction, (3) the Fair Debt Collection Practices Act, and (4) a state version of the fair debt collection practices act, (5) breached the covenant of good faith and fair dealing, (6) intentionally or negligently inflicted emotional distress, and (7) violated another state statute. The defendants sought dismissal of all but the first two claims. The court agreed it did not have related-to subject-matter jurisdiction of the other claims because the actions complained of all occurred postpetition, and resolution of the claims would not meet the *Pacor* test of affecting the debtors' estates. The court also followed its prior ruling that bankruptcy courts cannot exercise supplemental jurisdiction under 28 U.S.C. § 1367, but gave the debtors the opportunity to ask the district court to withdraw the reference of the proceeding to the bankruptcy court and determine whether it had subject-matter jurisdiction of the claims.

c. *Vogt v. Dynamic Recovery Servs. (In re Vogt)*, 257 B.R. 65, 68 (Bankr. D. Colo. 2000)

Long after the Chapter 7 debtors' discharges were entered and their case was closed, they

alleged a creditor refused to amend a credit report that showed they still owed it a debt unless they paid the debt, and failed to amend the report even after they paid the debt. They sued in bankruptcy court, claiming the creditor's actions violated the Fair Debt Collection Practices Act and the discharge injunction. The court noted that to the extent the creditor's actions involved the debtors' discharges, the actions would have related to, if not arisen out of, the bankruptcy case, but ruled that the court did not have jurisdiction over their claim under the FDCPA even though it arose from the same set of facts. The court found it did have related-to jurisdiction of their claim for violating the discharge injunction.

d. *Goldstein v. Marine Midland Bank, N.A. (In re Goldstein)*, 201 B.R. 1, 3-7 (Bankr. D. Me. 1996)

According to a complaint filed by a Chapter 7 debtor, a creditor continued to demand payment from him after he filed bankruptcy and even after he received a discharge. The debtor sued for violations of the automatic stay and the discharge injunction, and for postpetition violations of the Fair Debt Collection Practices Act. The court ruled its jurisdiction under § 1334 and § 157 did not extend to the FDCPA claims because any recovery the debtor made on them would belong to him, not his bankruptcy estate, and could therefore have no impact on the handling and administration of the estate. The court went on to concede that the federal district court might have supplemental jurisdiction under 28 U.S.C. § 1367, but ruled the bankruptcy jurisdiction referred to the bankruptcy court under § 157 did not include jurisdiction under § 1367.

e. *Irwin v. Olson & Bearden (In re Irwin)*, 325 B.R. 22, 25-28 (Bankr. M.D. Fla. 2005)

After a Chapter 7 debtor received a discharge and his bankruptcy case was closed, he

sued attorneys who had been representing him pre-bankruptcy in a divorce action for legal malpractice, and the attorneys removed the case to the bankruptcy court. That court ruled the debtor's claim was not property of his bankruptcy estate because the divorce action had not been concluded and, under Florida law, no malpractice claim would exist until a judgment in the divorce action had been entered against him. Consequently, the debtor's malpractice cause of action was not related to his bankruptcy case, and the bankruptcy court had no jurisdiction over it. The court remanded the suit to state court.

f. *Kline v. Deutsche Bank Nat'l Trust Co. (In re Kline)*, 420 B.R. 541, 552-53 (Bankr. D.N.M. 2009)

More than three years after her Chapter 13 case was dismissed, the debtor sued her mortgage creditor and its attorney, alleging that the creditor had violated the automatic stay in a state-court foreclosure action, and that the attorney had violated a New Mexico statute barring attorneys from engaging in deceit or collusion. With respect to the claim against the attorney, the bankruptcy court ruled it had no jurisdiction because the claim was governed entirely by nonbankruptcy law and existed independently of the bankruptcy case, and resolution of the claim would have no conceivable effect on the bankruptcy estate, so the claim was not one arising under title 11 or arising in or related to a case under title 11.

g. *Russell v. Chase Bank USA (In re Russell)*, 378 B.R. 735, 738-39 (Bankr. E.D.N.Y. 2007)

After a Chapter 7 debtor received a discharge, he tried to get a credit card company to correct information provided to the credit reporting agencies to show his debt to the company had been discharged in bankruptcy and was no longer due and owing. When the company refused to do so, the debtor brought an adversary proceeding, contending the creditor's refusal

violated the discharge injunction (§ 524 of the Bankruptcy Code), violated the Fair Credit Reporting Act, and constituted defamation. On the creditor's motion to dismiss, the bankruptcy court concluded that it had subject matter jurisdiction of the § 524 claim, and that the alleged FCRA violation could affect the § 524 claim (the debtor sought no separate relief under the FCRA). However, the court ruled it did not have subject matter jurisdiction of the defamation claim because it could not have any conceivable effect on the bankruptcy estate; instead, any damages awarded on that claim would go to the debtor alone. The court also declared that it had no authority to exercise supplemental jurisdiction to hear the defamation claim because § 157 did not authorize the district court to refer its supplemental jurisdiction to the bankruptcy court.

h. *Torres v. Chase Bank USA (In re Torres)*, 367 B.R. 478, 481-82 (Bankr. S.D.N.Y. 2007)

After Chapter 7 debtors received discharges, they tried to get a credit card company to correct information provided to the credit reporting agencies to show their debts to the company had been discharged in bankruptcy and were no longer due and owing. When the company refused to do so, the debtors brought an adversary proceeding, contending the creditor's refusal violated the discharge injunction (§ 524 of the Bankruptcy Code), violated the Fair Credit Reporting Act, and constituted defamation. The bankruptcy court concluded it had subject matter jurisdiction of the § 524 claims, but not of the claims for the FCRA violation and for defamation. The debtors had received discharges and their estates had been fully administered, so they were seeking damages for themselves, not their estates, and those claims did not fall within the court's related-to jurisdiction under *Pacor*.

i. *In re Timmons*, Case No. 11-20513-7, 2012 WL 4435522, *6-9 (Bankr. D. Kan. Sept. 24, 2012) (Somers, J.)

After a Chapter 7 debtor received a discharge and her case was closed, her student loan creditor notified her that she was in default and her debt had been accelerated, allegedly because she had filed bankruptcy. The debtor claimed she had timely made all the required payments on the loan. She filed a motion asking the bankruptcy court to find the creditor in contempt for violating either the automatic stay or the discharge injunction, depending on when the acceleration was done. She also contended the acceleration constituted illegal consumer abuse under a state statute. After concluding the debtor had identified nothing in the Bankruptcy Code that barred the creditor's action, the court then determined it had no subject matter jurisdiction over the debtor's state law claim because, applying the *Pacor* test, resolution of the claim could have no effect on her bankruptcy case because the case was over and done before the creditor notified her of the default and acceleration. The court said the allegation the default was declared because the debtor filed bankruptcy did give the claim a relationship to her bankruptcy case, but concluded that relationship was too tenuous to bring the claim within the court's related-to jurisdiction.

2. Claims arising after a Chapter 13 debtor completes a plan and gets a discharge

a. *Porter v. NationsCredit Consumer Discount Co. (In re Porter)*, 295 B.R. 529, 538-42 (Bankr. E.D. Pa. 2003)

After completing her Chapter 13 plan and receiving a discharge, the debtor brought an adversary proceeding against her mortgage lender and a credit insurance company, asserting claims under the Truth in Lending Act and the Racketeer Influenced and Corrupt Organizations

Act. She sought certification of a class of plaintiffs comprised of all borrowers who were enrolled in insurance with the same company as part of a loan transaction with the same lender, without specifying that any class member had to be a debtor in either a pending or a completed bankruptcy case. The defendants contested the bankruptcy court's subject matter jurisdiction over the putative class, and the court agreed with them. There was no arising-in or arising-under jurisdiction because the TILA and RICO claims were not created by the Bankruptcy Code, did not arise from the administration of a bankruptcy case, and existed independently of bankruptcy cases and could be brought in non-bankruptcy courts. The debtor's own claims were related to her bankruptcy case because they were property of the estate and disposition of the claims could conceivably affect the assets of the estate. However, the claims of the proposed class members belonged to them, and disposition of the claims could have no conceivable effect on the debtor's case. Courts are divided about whether bankruptcy court jurisdiction over class claims is limited to claims in cases pending in the court's own district or could extend to cases pending nationwide. But the claims of the proposed class in this case were not related to any bankruptcy case because the class was not limited to current or former debtors in bankruptcy cases. The possibility the claims might involve common factual or legal issues was not enough to make them related to this debtor's bankruptcy case.

3. Claims asserted by the debtor's spouse or other co-owner or co-obligor who has not filed bankruptcy

a. *Fietz v. Great Western Savings (In re Fietz)*, 852 F.2d 455, 457-58 (9th Cir. 1988)

The Chapter 13 debtor and his estranged wife owned a house subject to a mortgage. After default, the debtor found a buyer for the house but the mortgagee sunk the deal by insisting

on enforcement of a due-on-sale clause in the mortgage. The debtor filed bankruptcy and obtained confirmation of a plan. Then the debtor sued the mortgagee, seeking damages for the mortgagee's failure to agree to the house sale, and joining his wife as a defendant. The wife filed a cross-claim against the mortgagee, asserting a claim identical to the debtor's. The 9th Circuit adopted the *Pacor* test for related-to jurisdiction, and concluded the district court (and therefore the bankruptcy court) did not have jurisdiction over the wife's cross-claim. Even assuming the cross-claim was community property that became property of the bankruptcy estate, the circuit said, resolution of the cross-claim could have no conceivable effect on the administration of the bankruptcy estate because confirmation of the debtor's plan had vested all the estate property in him and his creditors could not assert any interests other than those provided for them by the plan. At the relevant time, § 1329 did not permit creditors to seek post-confirmation modification of the plan.

b. *Ostrander v. Surprise (In re Surprise)*, 443 B.R. 258, 262 (Bankr. D. Mass. 2011)

Several years before the debtor filed a Chapter 7 bankruptcy, he and his wife separated and, contemplating a divorce, he transferred his interest in their home to her in exchange for her waiver of her interest in his retirement plan. Later, they reconciled and did not divide their other assets. After the debtor filed bankruptcy, the trustee sued the wife, seeking to recover the debtor's transfer of his interest in the home under state law as a constructively fraudulent transfer. The debtor's wife filed a third-party complaint against the debtor's attorneys, alleging malpractice and breach of contract in failing to fulfill the debtor's expressed desire that his bankruptcy should not affect his wife or the home. When the attorneys moved to dismiss that complaint, the bankruptcy court raised the question of its jurisdiction *sua sponte*. The court said

the wife's claims did not arise under title 11 or arise in the debtor's bankruptcy case because they occurred prepetition, derived from state law, and could be brought in state courts. Then the court said the claims were not property of the debtor's bankruptcy estate, any recovery on them would go to the wife alone, no rights would be created for the estate, and the claims would have no impact on the claims against the estate. Therefore, the court had no related-to jurisdiction over the third-party complaint.

c. *Rhiel v. Central Mortgage Co. (In re Kebe)*, 444 B.R. 871, 875-78 (Bankr. S.D. Ohio 2011)

The Chapter 7 debtor was a co-owner of mortgaged real property, and the trustee sued the mortgagee and the debtor's co-owner, seeking under state law to avoid the mortgage on the debtor's interest as defective, and then to sell both the debtor's and the co-owner's interests. The co-owner filed a third-party complaint against the title company that had conducted the closing when he and the debtor bought the property, alleging that company's negligence created the problem the trustee's claim was based on. Applying the *Pacor* test as adopted by the Sixth Circuit, the bankruptcy court concluded it did not have subject matter jurisdiction of the co-owner's complaint because the co-owner failed to show how the disposition of that complaint would have any effect on the trustee's right to sell the real property, or how it would conceivably have any effect on the trustee's administration of the bankruptcy estate. The court went on (444 B.R. at 878-83) to note a split of authority over the question whether bankruptcy courts can exercise supplemental jurisdiction under 28 U.S.C. § 1367, which gives federal district courts jurisdiction over claims that are so related to a claim within their original jurisdiction that they form a part of the same case or controversy under Article III of the U.S. Constitution. The court ruled, however, that it would be appropriate to decline supplemental jurisdiction over the third-

party complaint in any event because it raised a novel issue of state law, and deciding it would not necessarily adequately serve the interests of judicial economy or the convenience of the parties.

4. Claims asserted for the debtor's personal benefit, not for the benefit of the bankruptcy estate

a. *Lambert v. Schwab (In re Lambert)*, 438 B.R. 523, 526-27 (Bankr. M.D. Pa. 2010)

The Chapter 7 debtors sued the trustee for their case based on his alleged effort to collect a debt they owed to another debtor he was the trustee for, claiming violations of the automatic stay, the Fair Debt Collection Practices Act and the Pennsylvania Fair Credit Extension Uniformity Act. The court ruled that it had jurisdiction of the alleged stay violations, but that the other claims were not related to the bankruptcy case because they could have "virtually no impact" on the bankruptcy estate. The court said if the debtors recovered from the trustee, they would retain the proceeds, and if they lost, the estate would not be impacted.

b. *Harris v. HSBC Bank USA (In re Harris)*, 450 B.R. 324, 333-35 (Bankr. D. Mass. 2011)

Through two adversary proceedings and objections to stay relief motions, a *pro se* Chapter 7 debtor sought a determination that a bank was not the holder of a note and mortgage on his home. The bankruptcy court said the dispute did not arise under the Bankruptcy Code or arise in the bankruptcy case because the rights asserted by both parties would exist outside of title 11. Then the court gave some examples of situations where a dispute like the one the debtor was raising could be related to the bankruptcy case because the dispute could potentially have some effect on the bankruptcy estate or the administration of the estate: (1) if voiding or

reducing the asserted security interest would make nonexempt equity available for distribution to unsecured creditors, (2) if the debtor had affirmative prepetition claims against the mortgagee, so the trustee could pursue recovery on the claims for the benefit of unsecured creditors, (3) if the purported mortgagee filed a proof of claim which turned out to be undersecured, then the mortgagee would be entitled to share in any dividend payable to unsecured creditors, and (4) if the purported mortgagee asked for stay relief to pursue a foreclosure action in state court, the bankruptcy court could consider the mortgagee's standing (but only to determine whether it had a colorable claim). But, the court ruled, none of those circumstances were present. The debtor had exempted the property that was subject to the mortgage, the trustee had chosen not to pursue the claims the debtor was asserting, the mortgagee had not filed a proof of claim, and the validity of any filed claim would be irrelevant anyway because there were no asserts to distribute, and the mortgagee had withdrawn its motion for stay relief.

5. Garnishment action to enforce a bankruptcy court judgment finding a debt to be nondischargeable

1. *In re Miller*, 248 B.R. 198, 201 (Bankr. M.D. Fla. 2000)

A creditor that obtained a nondischargebility judgment from the bankruptcy court in a Chapter 7 brought a garnishment action in that court to enforce the judgment. The court said the garnishment was not a core proceeding and was also not a related proceeding, so the court said it "chooses not to exercise jurisdiction" over it. 248 B.R. at 201.

C. Consumer cases finding related-to jurisdiction

1. Claim arising before plan confirmation

a. *Bartock v. Bae Systems Survivability Systems, Inc. (In re Bartock)*, 398 B.R. 135, 149-53 Bankr. W.D. Pa. 2008)

Before filing bankruptcy, the individual Chapter 11 debtor had signed an agreement not to compete with an employer for two years after his employment ended. After he left that job, the former employer sued him in state court for violating the non-compete provision. The state court enjoined the debtor from continuing to work for a competing company. The state court ruled the debtor had violated the non-compete clause, but the debtor filed his Chapter 11 petition before a trial to determine damages could be held. The debtor soon filed an adversary proceeding seeking a determination that his obligations for breaching the non-compete clause were dischargeable, and that with the passage of time, he was free to seek competing employment. The parties reached a settlement of that proceeding, and eventually submitted an order approving their settlement. The court found the order was deficient, and directed the parties to revise it. The parties failed to do that, though, and when the former employer's competitor sought confirmation of the debtor's assertion that it was free to hire him, the former employer disagreed. The debtor then filed an emergency motion to enforce the parties' settlement. The court rejected the former employer's assertion the court did not have subject matter jurisdiction of the debtor's motion, concluding the dispute was at least related to the debtor's case because the debtor's ability to obtain employment despite the non-compete clause would have a significant effect on the bankruptcy estate and in fact determine whether the debtor could propose a feasible plan. The court pointed out that whether the dispute was core or non-core was not relevant to the question of the bankruptcy court's subject matter jurisdiction.

2. Third-party complaints

a. *Allstate Ins. Co. v. Harris (In re Harris)*, 474 B.R. 816, 820-21 (Bankr. E.D. Mich. 2012)

When an insurance company brought a complaint contending its judgment against the Chapter 7 debtors was nondischargeable, the debtors filed a third-party complaint against an attorney who had been involved in the defense of the insurance company's suit against them. The debtors contended a specified dollar amount of their claim against the attorney was exempt, but valued the claim at more than that amount, and by agreement, the trustee and other parties could still object to the debtors' asserted exemption. Under these facts, the court found the claim against the attorney came within the court's related-to jurisdiction because the estate could conceivably recover money on the claim that the trustee could use to pay creditors.

b. *Holmes v. Deutsche Bank Nat'l Trust Co. (In re Holmes)*, 387 B.R. 591, 598-602 (Bankr. D. Minn. 2008)

Chapter 7 debtors sued their mortgagee, seeking to void its mortgage under state law on the ground the signature of one of them on the mortgage was forged. The mortgagee filed a third-party complaint for contribution or indemnity against the closing agent, alleging the agent was responsible for any defect that would allow the debtors to void the mortgage. The bankruptcy court found it had related-to jurisdiction over the debtors' complaint because if they won, their bankruptcy estate would retain certain assets that could provide a distribution to creditors, but if they lost, they could amend their exemptions in such a way that the estate would lose those assets. The court found it also had related-to jurisdiction over the mortgagee's complaint against the closing agent because any recovery it obtained would indirectly affect the bankruptcy estate by reducing the mortgagee's claim against the estate and giving other creditors

a greater share of the estate's assets. However, the court decided to exercise its discretion to abstain from deciding the third-party complaint.

3. Claim to avoid government setoff

a. *U.S. Dept. of Agriculture v. Huff (In re Huff)*, 343 B.R. 136, 139-41 (W.D. Pa. 2006)

After the federal government offset a tax refund the Chapter 7 debtor had claimed as exempt, she sued contending the offset was improper. On appeal, the district court rejected the government's argument that the bankruptcy court had no jurisdiction because the debtor's claim was not property of the estate, concluding the bankruptcy court had related-to jurisdiction of the claim. Related-to jurisdiction extends not only to property of the estate but also to property of the debtor and to any proceeding that could alter the debtor's rights, liabilities, options, or freedom of action in any way. The court went on to conclude the debtor's suit was a core proceeding under the catch-all provision of 28 U.S.C. § 157(b)(2)(O) because it affected the adjustment of the debtor-creditor relationship.

4. Claim covered by arising-in, arising-under, and related-to jurisdiction

a. *DaimlerChrysler Fin. Servs. Americas LLC v. Jones (In re Jones)*, 397 B.R. 775, 780-82 (S.D. W. Va. 2008)

A husband and wife bought a car financed by a creditor and then the husband alone filed a Chapter 7 bankruptcy. The couple were current on their payments to the creditor, and had maintained all necessary insurance on the car. The debtor filed a statement of intention that said he would "continue payments" on the car, but did not say whether he intended to redeem the car or reaffirm the debt; he was relying on a "ride-through" option that had been recognized by the

circuit in which the bankruptcy case had been filed. After obtaining stay relief, the creditor repossessed the car without giving the debtor and his wife a notice allegedly required by state law that they had a right to cure their default on the debt (apparently the only default was the debtor's having filed for bankruptcy). The couple filed an adversary proceeding against the creditor, contending the repossession was improper and seeking return of the car and money damages. The bankruptcy court ruled in favor of the couple, but on appeal, the district court reversed. As a preliminary matter, the district court rejected the creditor's argument that the bankruptcy court did not have subject matter jurisdiction of the proceeding. It ruled the bankruptcy court had both arising-under and arising-in jurisdiction because the couple were relying on the bankruptcy common-law "ride-through" option. It ruled there was related-to jurisdiction under the applicable circuit's version of the *Pacor* test because the proceeding would impact the couple's (and therefore the debtor's) ability to retain and use the car, and if they could exercise the "ride-through" option, their continued payments on the car would affect the couple's (and therefore the debtor's) cash flow, thereby conceivably affecting the bankruptcy estate if the ongoing payments reduced the assets that were available for distribution to the estate's creditors [Not clear how this could be so in a Chapter 7 case]. The court ultimately ruled against the debtors, though, finding that the ride-through option had been eliminated by 2005 amendments to the Bankruptcy Code and that state law did not require the right-to-cure notice under the circumstances of the case.

5. Claim involving the non-debtor spouse of the debtor

a. *Sharif v. IndyMac Bank (In re Sharif)*, 411 B.R. 276, 279-82 (Bankr. E.D. Va. 2008)

After a Chapter 7 debtor received a discharge and the estate's interest in real property he

and his non-debtor wife owned was abandoned, the debtor brought an adversary proceeding against a creditor, seeking a declaration that its lien on the property was not valid because the property was held in tenancy by the entirety and the wife had not signed the creditor's deed of trust. The bankruptcy court said the subject-matter-jurisdiction question was difficult, but concluded it had related-to jurisdiction of the proceeding because the bankruptcy estate was still open, and the outcome could affect who would receive distributions from the estate and how much they would receive. The court also required adding the debtor's wife as a party to the proceeding.

VI. What Is Related If the Plan Is Confirmed?

A. Introduction

Other sections of these materials have explained how broad the bankruptcy courts' "related to" jurisdiction can be under the any-conceivable-effect test set forth in *Pacor, Inc., v. Higgins,* 743 F.2d 984, 994 (3d Cir. 1984). Those sections have analyzed some of the doctrines courts have used to prevent that vague provision from becoming an almost boundless jurisdictional grant. While broad related-to jurisdiction is needed to further the single forum concept and aid in the reorganization of troubled enterprises, it may not be necessary or appropriate after the reorganization has been completed by the consummation of a confirmed plan. Indeed the majority of circuits adopt the view that the bankruptcy courts' related-to jurisdiction shrinks upon confirmation (or consummation) of the plan.

B. Defining the proceedings that are post-confirmation

1. Continuing Jurisdiction over Pending Actions.

Post-confirmation related-to jurisdiction should be distinguished from the court's

retention of jurisdiction over matters that already were pending at the time of confirmation. Since jurisdiction is determined at the time of filing, the normal related-to doctrines apply to actions instituted before confirmation. However, although the bankruptcy court retains jurisdiction of pending related-to proceedings, as a general rule, related-to proceedings should be dismissed when the underlying bankruptcy case is terminated. *See In re Porges,* 44 F.3d 159, 162-63 (2d Cir. 1995) (involving dismissal of underlying bankruptcy case). Dismissal is not automatic, but is vested in the sound discretion of the bankruptcy court based on four factors: (1) judicial economy; (2) convenience of the parties; (3) fairness; and (4) comity. This doctrine is typically applied when the underlying bankruptcy case has been dismissed. Limited research did not uncover reported decisions discussing whether it should apply when the case is terminated by formal closing or terminated, as a practical matter, by plan confirmation.

2. What Date Determines Whether a Proceeding is Post-Confirmation?

Many of the reported cases that raise the issue whether related-to jurisdiction is more restricted post-confirmation involve causes of action that accrued after the plan of reorganization had been confirmed. These proceedings are post-confirmation both in terms of their substance and of the date they were instituted. The Third Circuit has held that the more limited interpretation of related-to jurisdiction is triggered by the date of filing, and does not turn on the time the conduct that gave rise to the action occurred. *See In re Seven Fields Devel. Corp.,* 505 F.3d 237, 264-65 (3d Cir. 2007).

C. Theoretical approaches to post-confirmation jurisdiction

1. No Change under the Statutory Language.

The statutory language of 28 U.S.C. § 1334(b) provides for "original but not exclusive jurisdiction of all civil proceedings … related to cases under title 11." This language makes no

distinction between civil proceedings instituted before or after plan confirmation, at least as long as the case remains pending. This supports the view that there is no change in the test for related-to jurisdiction post-confirmation, a position articulated by early scholarship. *See* Frank Kennedy & Gerald Smith, *Postconfirmation Issues: The Effects of Confirmation and Postconfirmation Proceedings,* 44 S.C. L. Rev. 621, 743 (1993). However, the courts have not adopted that view. A possible exception is the Seventh Circuit. Its test for related to jurisdiction in the pre-confirmation context is much narrower than the majority *Pacor* test. Arguably the Seventh Circuit's test is as narrow as the more restrictive test that *Pacor* jurisdictions apply post-confirmation. Thus, the test in the Seventh Circuit may be the same for both pre-confirmation and post-confirmation proceedings.

Note that even if the legal test remains the same, plan confirmation should change the scope of related-to jurisdiction because the plan will change the factual context to which the test will be applied. In general, the plan will narrow the range of matters that the bankruptcy case involves, thereby reducing the number of civil proceedings that might relate to the case.

2. No Jurisdiction under the *Pacor* and *Celetex* Language.

While the statutory language might support the extreme position that confirmation changes nothing, at the other extreme is the view that plan confirmation completely eliminates the basis for related-to jurisdiction. *See* Rhett Campbell, *Issues in Litigation: Postconfirmation Jurisdiction,* 1 J. Bankr. L. & Prac. 94, 97 (1991). This view is based on the *Pacor* test for related-to jurisdiction, which was quoted approvingly by the Supreme Court in *Celotex.* The *Pacor* test finds related-to jurisdiction to hear a proceeding if "the outcome of that proceeding could conceivably have any effect on the estate being administered in bankruptcy". *Pacor,* 743 F.2d at 994. The Supreme Court, in its only indication of the scope of related-to jurisdiction,

picked up on the *Pacor* language and stated that "bankruptcy courts have no jurisdiction over proceedings that have no effect on the estate of the debtor." *Celotex Corp. v. Edwards,* 514 U.S. 300, 308 n. 6 (1995). If these statements are accepted as the test for related-to jurisdiction, then related-to jurisdiction should lapse upon confirmation in most cases. This is because the property of the estate typically revests in the debtor upon confirmation and the estate ceases to exist. *See* 11 U.S.C. § 1141(b). Although the Third Circuit made this point in its seminal post-confirmation jurisdiction case of *In re Resorts Int'l, Inc.,* 372 F.3d 154, 165 (2004), it rejected this "literal" view, as have other courts.

It is not clear why there should be any related-to jurisdiction post-confirmation in cases where all property revests in the debtor. Continuing bankruptcy court jurisdiction over related-to proceedings might well be convenient for the parties and desirable to some of them, but the related-to jurisdictional grant is an exceeding broad one. It was designed to enhance the courts' ability to effectively restructure the business. That process concludes with the substantial consummation of a confirmed plan. While continuing jurisdiction over the case, interpretation and enforcement of the confirmation order, and jurisdiction over post-petition actions arising under bankruptcy law may be necessary to wrap up the case, related-to actions are tangential proceedings. They are not based on bankruptcy law and do not arise out of the bankruptcy case. It is not clear why those actions should be heard in bankruptcy court simply because they may affect an entity that *previously* was the subject of a successfully-concluded bankruptcy proceeding when similar actions involving entities that have not been debtors are heard elsewhere.

3. The Policy Considerations Supporting a Restrictive View of Post-Confirmation Jurisdiction.

While no circuits have clearly adopted either of the extreme views of post-confirmation jurisdiction, most courts recognize that the scope of related-to jurisdiction shrinks upon confirmation of the plan. The cases articulate several reasons for restricting post-confirmation related-to jurisdiction. The most common is that the related-to jurisdiction is very broad and should not continue indefinitely. A related consideration is based on the idea that the bankruptcy reorganization process is supposed to restructure the debtor so that it can re-enter the marketplace in its reincarnated form. Once the debtor has re-entered the market, it should be treated just like other entities and no longer have the special advantage of funneling virtually all litigation affecting it to a single federal forum.

D. Varying circuit court views of post-confirmation jurisdiction

1. Is there Confusion or Convergence?

A review of the reported decisions at the circuit court level suggests that there may be several different approaches to the post-confirmation jurisdiction issue, with a split in the courts. However, the apparent disagreement among the circuits may have more to do with timing. The seminal Third Circuit decision in *Resorts* in 2004 appears to have focused the issue in a way that had not previously been done. Indeed, prior to *Resorts*, even cases decided by the Third Circuit articulated a variety of different approaches. Since *Resorts* was decided, other circuits have been adopting its approach. Thus some of the apparent disagreement may reflect nothing more than the fact that the opinions articulating a different approach pre-dated *Resorts.* If asked to revisit their pre-*Resorts* opinions, these courts might also adopt the *Resorts* approach. The exception is the Seventh Circuit. The Seventh Circuit is unique because it never adopted the expansive *Pacor*

view of related-to jurisdiction. However, in the post-confirmation area, its general approach to related-to jurisdiction may be narrow enough to be almost identical to the *Resorts* interpretation.

2. The Majority View Requires a Close Nexus.

The modern era of post-confirmation jurisdiction jurisprudence dates to the Third Circuit's 2004 opinion in *Resorts.*

a. The *Resorts* Approach

The Third Circuit was the source of the popular *Pacor* test for related-to jurisdiction and, in *Resorts,* had to consider how that test applied after confirmation. The *Pacor* test had two salient features. First, it adopted a very minimal threshold for jurisdiction by holding that the degree of relationship needed in order for a proceeding to be related to the bankruptcy case was whether it had any conceivable effect. The second requirement was that the effect had to be an effect on the estate being administered in bankruptcy. In *Resorts,* the Third Circuit restricted the first requirement but relaxed the second for post-confirmation proceedings. As noted above, the Third Circuit rejected the view that *Pacor's* requirement of an effect on the estate eliminated post-confirmation jurisdiction entirely. The Third Circuit stated, "[T]hough the scope of bankruptcy court jurisdiction diminishes with plan confirmation, bankruptcy court jurisdiction does not disappear entirely." *Resorts,* 372 F.3d at 165. Since there generally will be no "estate" post-confirmation, the *Resorts* court instead focused on the bankruptcy plan and the bankruptcy proceeding. The necessary relationship between the relevant related proceeding and the bankruptcy plan or proceeding shrunk from any conceivable effect to a "close nexus." *Resorts,* 372 F.2d at 166. The court noted that, "Matters that affect the interpretation, implementation, consummation, execution, or administration of the confirmed plan will typically have the requisite close nexus." *Resorts,* 372 F.3d at 167. As the court restated the test, "[W]here there is

a close nexus to the bankruptcy plan or proceeding, as when a matter affects the interpretation, implementation, consummation, execution, or administration of a confirmed plan or incorporated trust agreement, retention of post-confirmation bankruptcy court jurisdiction is normally appropriate." *Resorts,* 372 F.3d at 168-69. Other circuits have adopted this view. *See, e.g., In re Boston Reg'l Med. Ctr., Inc.,* 410 F.3d 100, 106 (1st Cir. 2005); V*alley Historic Ltd. v. Bank of New York,* 486 F.3d 831, 837 (4th Cir. 2007); *In re Pegasus Gold Corp.,* 394 F.3d 1189, 1193-94 (9th Cir. 2005).

b. Post-Confirmation Trusts.

It is common in many reorganization plans to create either a litigation trust or a liquidating trust and to transfer claims that the estate may have against third parties to those trusts for post-confirmation resolution, with the creditors becoming the beneficiaries of the trusts and sharing in any recovery. The argument that such a trust is a new entity and that there should be no related-to jurisdiction over claims asserted by it was rejected by the Third Circuit in *Resorts.* The court reasoned that the use of such trusts "by their nature maintain a connection to the bankruptcy even after the plan has been confirmed." *Resorts,* 372 F.3d at 167. Indeed, the court's articulation of its test expressly refers to trust agreements incorporated in a confirmed plan.

c. Jurisdiction Might Not Shrink in Liquidating Plans.

Where the plan provides for liquidation instead of reorganization, some courts take the view that the bankruptcy courts' related-to jurisdiction does not shrink upon plan confirmation. A liquidating plan does not present the policy concerns that the *Resorts* court relied upon to restrict post-confirmation jurisdiction. In a liquidation context, the debtor has not reentered the marketplace and the risk of unending jurisdiction is small because the debtor is being wound up.

For these reasons, the First Circuit has held that "when a debtor (or trustee acting to the debtor's behoof) commences litigation designed to marshal the debtor's assets for the benefit of its creditors pursuant to a liquidating plan of reorganization, the compass of related to jurisdiction persists undiminished after plan confirmation." *Boston Reg'l Med. Ctr.,* 410 F.3d at 107.

d. Retention of Jurisdiction Provisions in the Plan.

It is clear that the plan cannot confer subject matter jurisdiction on the bankruptcy courts. Thus the inclusion of a broad retention of jurisdiction provision should not expand the reach of post-confirmation related-to jurisdiction. *See, e.g., Resorts,* 372 F.3d at 161. However, the Second Circuit apparently requires not only that there be a close nexus but that the plan also contain a retention of jurisdiction provision that retains jurisdiction over the matter. *See In re Residential Capital,* 527 B.R. 865, 871 (S.D.N.Y. 2014) (also noting that the Second Circuit has not yet adopted the close nexus test). Some other courts also adopt this position. *See, e.g., In re Baur,* 433 B.R. 898, 900 (Bankr. M.D. Fla. 2010). It is unclear why this is a requirement. Section 1334 should by itself be sufficient to confer the full range of post-confirmation related-to jurisdiction in the absence of any retention of jurisdiction provision. Possibly the courts mean to say that a retention of jurisdiction provision in the plan that is narrower than section 1334 operates as a contractual agreement to limit jurisdiction.

3. Other Circuit Court Views.

The Seventh Circuit is the only circuit to explicitly reject the broad *Pacor* test for "related to" jurisdiction. Instead it follows a much narrower approach that recognizes related-to jurisdiction only if the dispute "affects the amount of property available for distribution [i.e., the debtor's estate] or the allocation of property among creditors." *In re Fed Pak Systems, Inc.,* 80 F.3d 207, 213-14 (7th Cir. 1996) (reaffirming narrow view notwithstanding Supreme Court's

apparent preference for the broad view in *Celotex*). Since the Seventh Circuit's test is so narrow already, it does not shrink further upon plan confirmation.

The Fifth Circuit might also be an outlier, but this may only be a reflection of its failure to carefully consider *Resorts*. In the pre-*Resorts* case of *In re Craig's Stores of Texas, Inc.,* 266 F.3d 388 (2001), it adopted a test for post-confirmation related-to jurisdiction that has been interpreted by lower courts to involve a six-factor analysis. *See Timothy Davis, Comment, Defining the Close Nexus: An Analysis of a Bankruptcy Court's Chapter 11 Postconfirmation Jurisdiction*, 28 Emory. Bankr. Dev. J. 419, 447-53 (2012). The *Craig* test was relaxed in *In re Enron Corp. Securities,* 535 F.3d 325, 335 (5th Cir. 2008), where only three factors were emphasized. While *Enron* was a post-*Resorts* decision, that case did not involve the post-confirmation jurisdiction issue addressed by *Resorts*. Instead, the question was whether plan confirmation divested the court of jurisdiction over a matter that had properly been removed to the bankruptcy court prior to confirmation. *Enron* did not mention *Resorts* or engage in any analysis of that issue, so the opinion may not reflect the approach the Fifth Circuit would take if squarely presented with the *Resorts* analysis.