



## Kriss Worthington

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### CONSENT CALENDAR

10/31/2017

To: Honorable Mayor and Members of the City Council  
 From: Councilmembers Kriss Worthington and Kate Harrison  
 Subject: Reforming Current Venue Laws of United States Code

### RECOMMENDATION

Adopt a Resolution and send a letter to the California Legislature asking them to support reforming the current venue laws in section 1408 of title 28 of the United States Code to better serve the community of taxpayers, consumers and small business owners.

### BACKGROUND:

Current federal bankruptcy venue laws allow corporations filing Ch. 11 reorganization cases to forum shop for preferential districts. In California, from 2004 through 2012 California companies representing \$47,244,306,682 in assets and \$52,210,750,411 in liabilities have filed for Ch. 11 reorganization in the foreign districts of Delaware and Southern New York. In particular to the Bay Area, from 2004 through 2012, 17 companies from the Bay Area have filed Ch. 11 reorganization cases in Delaware and New York. To convey some sense of the magnitude of the estimated amount at issue, CLLA estimated in 2015 that the economic boost to Wilmington, Del., from all the bankruptcy cases is around \$100 million each year. These \$100 million each year combine many expenses associated with corporate cases including everything from court and lawyer fees to money spent on accommodations at hotels and restaurants. The concentration of Chapter 11 cases in one or two jurisdictions deprives local hospitality and service providers of California from sharing in the economic activity that surrounds these cases. This activity includes not just local lawyers or court fees, but also hotels, restaurants, cabs and copy centers, to name a few. The purpose of this resolution is to protect California's economy by revising current venue laws in a way that enforce corporations to file Ch. 11 reorganization in their place of business or primary location of assets.

Permitting these cases to be filed in the preferential districts not only significantly affects the local economy, but also disenfranchises many of the employees, retirees, consumers, land-owners, communities, and small business owners who will be most heavily impacted by the outcome of the case. Unlike large corporations, most people lack the resources to participate in a trial that is occurring on the other side of the

country. As a result, many employees, retirees, consumers, communities, landowners, and small business owners are deprived of their right to participate in case proceedings. This is particularly troubling because the effects of corporate reorganization are felt most at the local level. The entire process not only harms California's economy but it also erodes public confidence in the bankruptcy system and heavily ignores local interests.

A 2015 GAO Report on Corporate Bankruptcy – Stakeholders Have Mixed Views on Attorneys; Fee Guidelines and Venue Selection for Large Chapter 11 Cases (GAO-15-839) confirmed that since 2009 nearly 2/3 of large companies (assets and liabilities of \$50 million or more) filed their chapter 11 cases in venues outside of the district where their principal place of business or principal assets are located. And approximately 90 percent of those companies filed in the District of Delaware or the Southern District of New York. In addition to this, 2014 Commercial Law League of America (CLLA) study indicates that 70% of the public companies filed Chapter 11 outside of their district. These cases involved approximately \$1 trillion in assets, \$2 trillion in debt, 5.3 million creditors and more than 2 million employees, all having their rights administered by courts having no meaningful connection with the subject debtors.

In the wake of significant California state court budget cuts, keeping this money in the local system would provide a significant resource for both the courts and the support industries involved in the cases. In addition to protecting California's economy, preventing forum shopping would prevent Californians from being disenfranchised. The purpose of the law as stated by the Congress is "to disclose a common theme and objective [underlying the reorganization provisions]: avoidance of the consequences of economic dismemberment and liquidation, and the preservation of ongoing values in a manner which does equity and is fair to rights and interests of the parties affected." The code provides for a national bankruptcy system and supports principles of federalism, and yet the proceedings for Chapter 11 cases is largely concentrated in a duopoly manner.

As stated by the CLLA, "the Bankruptcy Code is not purely economic legislation, and the bankruptcy court is not merely a commercial court; the law is socioeconomic, and courts are required to balance the interests of many different parties." Venue laws must exist to ensure that cases are held in a location that is convenient and fair to all stakeholders, and allowing corporations to file in foreign districts subverts this purpose. The proposal outlined in this item strikes towards the right balance between protecting debtor's right to economic dismemberment and returning bankruptcy to its foundational principles.

The current Chapter 11 venue laws provide corporations with four choices for where they can file a bankruptcy case: (1) state of; (2) location of primary assets; (3) primary place of business; and (4) where an affiliate has a pending case. Revising the law to

ensure that corporations file for reorganization in their place of business or primary location of assets would protect Californians' right to due process, protect California's economy, and comply with the purpose of venue laws. Therefore, it is important for the City of Berkeley to send a letter to the California Legislature asking them to support reforming the current venue laws.<sup>1</sup>

FINANCIAL IMPLICATIONS

None.

CONTACT PERSON

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Attachment:

1. Resolution to California Legislature and California Congressional delegation

RESOLUTION NO. ##,###-N.S.

SUPPORTING FEDERAL BANKRUPTCY VENUE LAW REFORM

WHEREAS, California loses a large sum of potential revenue to companies opting to file Ch. 11 reorganization cases in out-of-state districts such as Delaware or the Southern District of New York, which adversely affects California's economy, courts, businesses and workers; the forum shopping that occurs in California and other states nets a \$100,000,000 yearly profit for Delaware; and (no source for this number)

WHEREAS, small businesses are hit particularly hard, as many small-scale companies depend on a single large-scale company for business, and allowing these large corporations to take their cases out of state adds an unnecessary and heavy burden to an already laden California middle class; and

WHEREAS, the current venue laws in section 1408 of title 28 of the United States Code allow companies filing a Ch. 11 bankruptcy case to forum shop by providing them with four options for filing their case: 1) the district of incorporation, 2) the district where the primary assets of the company are located, 3) the district in which the company principally conducts its business, or 4) any district in which the company's affiliate has a pending case; and

WHEREAS, filing bankruptcy cases in foreign districts disenfranchises all stakeholders in the case that do not operate on a budget large enough to participate in a trial taking place in a different state or coast, including retirees whose pension may be affected, locals who are employed by the company or are seeking employment, small business owners who offer services that depend on the company, and landowners; and

WHEREAS, excluding these stakeholders from participating in case proceedings by filing in foreign districts means that bankruptcy cases are decided less equitably, because out-of-state judges are both more likely to overlook or ignore the interest of creditors if they are not present during the proceedings and are less invested in local issues, which is particularly important because the impact of a corporation going out of business is felt primarily at the local level; and

WHEREAS, additionally, allowing out of state judges to rule on bankruptcy cases compromises the ability of our judicial system to produce the most accurate case decisions because out-of-state judges must decide these cases with access to less information; when judges hear cases that originate hundreds or thousands of miles away they not only lack knowledge of the local contexts and dynamics, but are also deprived of potentially critical information that excluded parties provide; and

WHEREAS, allowing out-of-state judges to decide Ch. 11 reorganization cases has resulted in less successful outcomes than when these cases were filed locally; instead of successful reorganization it has become more common for businesses to sell their assets - an issue that leads to more repeat filings and inefficiency, but that can be

resolved by corporations filing reorganization cases in their home districts where the presiding judges are invested in preserving local business instead of quick 363 asset sales; and

WHEREAS, contrary to the notion that the judges of Delaware and Southern New York have developed an expertise in bankruptcy law that allows them to handle bigger cases more efficiently, bigger cases are not necessarily more complex, and California bankruptcy judges have shown the ability to effectively and efficiently deliver decisions on highly involved and intricate cases; and

WHEREAS, venue laws exist in order to ensure that cases are tried in a location that is convenient and fair to all the parties involved in the case, yet by allowing debtors to forum shop and file for reorganization in distant districts the current laws undermine their own purpose, allowing one party to protect and advocate for their own interests at the expense not only of the other parties in the case, but also of the state in which they are most involved; and

WHEREAS, the current laws allow creditors to challenge the location that the debtor has chosen to file the case on the grounds that the location is inconvenient or unfair, it is extremely difficult to win this type of challenge, as challenges are very expensive and the strong legal presumption that the debtor chose the correct venue poses a significant obstacle; additionally, it is often too risky for a creditor to challenge the venue choice because the same court that handles the motion to overrule the debtor's choice of venue will also, in the probable event of the motion failing, be the court that decides the case itself; and

WHEREAS, the US' judicial system is structured such that the evolution of the law benefits from and is driven by input from judges of many districts and so that the people have direct access to the courts, yet the current system violates these principles of federalism and citizen access by turning over control of an entire area of law to only two states, both stunting the healthy growth of the law and restricting access to the courts; and

WHEREAS, admitting forum shopping and allowing debtors to take their cases to districts where particular outcomes are essentially known and ensured because the same judges hear nearly all the cases compromises the equity of the judicial process, because the system relies on balanced bargaining power and uncertain outcomes to drive a fair bargaining process.

NOW THEREFORE BE IT RESOLVED, by the Council of the City of Berkeley that the Council requests that the Assembly and the senate of the State of California both adopt a position in support of reforming section 1408 of title 28 of the United States Code to prohibit debtors from filing Ch. 11 reorganization cases in their district of incorporation, or in a district in which an affiliate that directly or indirectly holds, controls, or owns less than 50% of the outstanding voting securities of the company, has a pending case.

BE IT FURTHER RESOLVED, that the Berkeley City Council urge the California Congressional Delegation to adopt this position as well.