

ABI Commission to Study Reform of Chapter 11
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I am grateful for the opportunity to testify before the Commission today. My name is James L. Patton, Jr., and I am the Chairman of Young Conaway Stargatt & Taylor, LLP. For those who are unfamiliar with Young Conaway, the firm is headquartered in Wilmington, Delaware with the vast majority of its slightly over 100 attorneys based in that office, and additional attorneys in both Georgetown and Middletown, Delaware, and New York, New York. Although Young Conaway is a full-service law firm, it has one of the largest bankruptcy departments in Wilmington, with an emphasis on chapter 11 debtor representations. I am one of the firm's bankruptcy attorneys, and was one of the attorneys on the *Continental* case. As you know, that case is regarded by many as the case that created Delaware's reputation for efficiency in chapter 11 practice.

I have had the privilege of witnessing firsthand the evolution of Delaware bankruptcy practice, and I am here to explain why I believe the current chapter 11 venue provision, 28 U.S.C. § 1408, is beneficial to distressed companies, their employees, and their residual constituencies, typically unsecured creditors, and thus should be retained.

As we all know, 28 U.S.C. § 1408 provides that a chapter 11 case may be commenced "in the district court for the district-

(1) in which the domicile, residence, principal place of business in the United States, or principal assets in the United States, of the person or entity that is the subject of such case have been located for the one hundred and eighty days immediately preceding such commencement, or for a longer portion of such one-hundred-and-eighty-day period than the domicile, residence, or principal place of business, in the United States, or principal assets in the United States, of such person were located in any other district; or

(2) in which there is pending a case under title 11 concerning such person's affiliate, general partner, or partnership."¹

It is widely accepted that a corporation's domicile is its state of incorporation or other organization.² This, of course, has spawned a number of critics of the current venue statute, who believe that venue for chapter 11 bankruptcy cases should be limited to a corporation's principal place of business or the

¹ 28 U.S.C. § 1408.

² See, e.g., *In re Del. & Hudson Ry. Co.*, 96 B.R. 467 (Bankr. D. Del. 1988).

location of its principal assets, and many who also believe that the “affiliate filing rule” set forth above should also be dispensed with.

At bottom, the criticisms of the current venue provision can be reduced to two general arguments. First, the current provision allows for a corporation to file away from its “home forum” and thereby inconveniences or prevents employees and smaller creditors from participating in a debtor’s chapter 11 case. Second, an academic criticism arising from a theory, championed most prominently by Professor Lynn M. LoPucki of UCLA School of Law but also by others, that the current venue provision has created “competition” for chapter 11 cases in a manner that has compromised the integrity of the entire bankruptcy system and led to increased failures and refilings of companies that emerge from chapter 11. As a practitioner who is not a practicing academic, I will mainly speak to the first criticism and the benefits of the current system I see as a practitioner. However, I will also very briefly speak to the academic debate today.

Clarity and Convenience

We should begin by noting that that 28 U.S.C. § 1408 is concerned primarily with clarity regarding the propriety of a court’s jurisdiction over parties, while convenience to non-debtor parties is the subject of a separate statute, 28 U.S.C. § 1412. The latter provision provides that, after a case is filed, “[a] district court may transfer a case or proceeding under title 11 to a district court for another district, in the interest of justice or for the convenience of the parties.”³ As I will explain, attempts to address convenience by altering 28 U.S.C. § 1408 will result in neither clarity nor increased convenience, thereby taking away the clarity and related benefits of current venue law without any significant increased benefits.

Venue based on state of incorporation or organization provides a clear, bright-line venue option that is easily ascertained and practically undisputable. Elimination of venue based on a company’s place of incorporation—the only venue option that is clear and easily ascertainable in advance by all parties in interest—will result in increased litigation concerning a debtor’s “principal place of business” and “principal assets.”

Proponents of restricting a debtor's venue choice to principal place of business or location of principal assets presume the venue choice is easily determinable. However, the determination of a debtor's principal place of business or location of principal assets in large chapter 11 cases often will require an intensive factual and legal inquiry and result in substantial litigation in the critical early stages of a corporation’s bankruptcy. Circuits diverge sharply on many important points of bankruptcy law that significantly affect the rights of stakeholders. No doubt, if these more amorphous venue tests were to be the only bases for venue, tactical litigation over venue will proliferate. As businesses expand into multiple states and nations, and corporate decision making becomes more and more diffuse, the concepts of “principal place of business” and “location of principal assets” each become increasingly vague.

³ 28 U.S.C. § 1412.

Ascertaining the principal place of business of a large company with diverse operations and an intricate corporate structure has never been an easy task. For nearly a century, courts have disagreed over the test to be applied in determining a corporation's principal place of business in connection with a bankruptcy case. Although in *The Hertz Corp. v. Friend*, 130 S. Ct. 1181 (2010), the Supreme Court has recently held, in the context of construing the federal diversity jurisdiction statute, that a company's principal place of business "refer[s] to the place where a corporation's officers direct, control, and coordinate the corporation's activities," it is far from clear whether this test, referred to as the "nerve center test," will control the inquiry of what is a corporation's "principal place of business" in a bankruptcy venue determination.

Even assuming the "nerve center" test set forth in *Hertz* were to be uniformly applied in the bankruptcy context, the test described in *Hertz* is a fact-intensive and time-consuming determination for many businesses, in particular large entities with dispersed operations and management, that is likely to be the subject of litigation if state of incorporation is removed as a basis for venue under the Bankruptcy Code. In today's global economy, many large companies have widely dispersed management and operations, some of which are intentionally segregated to allow for the effective control of business lines or services that have different geographic sales or manufacturing concentrations.⁴ For such entities, determining the location of their "nerve centers"—unlike the state of incorporation—is far from straightforward.

Additionally, due to technological advances that enable virtually instantaneous communication, companies are highly mobile and may move their headquarters with regularity.⁵ One recent study concluded, among other things, that (1) U.S. headquarters relocate a significant 5% a year;⁶ (2) of the 500 largest U.S. headquarters, 36 moved between 1996 and 2001, or 7.2% every five years;⁷ (3) headquarters of U.S. multi-site firms are typically disconnected from production sites;⁸ and (4) many of these moves have little to do with operations and instead are due to economic factors such as a state's offer of tax breaks or other economic incentives.⁹ If rampant forum shopping truly exists, many sophisticated companies will relocate their headquarters to jurisdictions perceived to be favorable, the effectiveness of which will almost certainly be challenged (engendering more litigation) by parties in interest.

⁴ See, e.g., Vanessa Strauss-Kahn & Xavier Vives, *Why and Where Do Headquarters Move?*, 39 *Regional Science & Urban Economics* 168, 169 (2009) (stating that the 50,000 firms in its study had an average of fifteen (15) headquarters); see also *Tosco Corp. v. Comtys. for a Better Env't*, 236 F.3d 495, 502 (9th Cir. 2001) (noting that plaintiff asserted that it had four (4) separate headquarters in different states).

⁵ See Strauss-Kahn & Vives, 39 *Regional Science & Urban Economics* at 170–71.

⁶ *Id.* at 168, 172, Table 2.

⁷ *Id.* at 172, 182, Table A7.

⁸ *Id.* at 168–69.

⁹ *Id.* at 176–79.

Like venue based on a principal place of business, the venue based on “place of principal assets” presents a fact-intensive inquiry and is likely to be litigated more frequently if state of incorporation is no longer a basis for chapter 11 venue. This is as true for companies with hard assets as it is for companies with intangible assets, but in the case of companies in which substantial value is in the form of intangible assets (such as trademarks, trade names, patents, technology, computer-related products, information systems, licenses, contracts, etc.), the term has little meaning. In these cases, “place of principal assets” is a far less “real” contact than state of incorporation, and it is a great deal more difficult to determine. Even with respect to debtors whose value is in the form of “hard assets,” like inventory, equipment, owned or leased wholesale and retail locations, and other non-movable assets, the place of “principal assets” is not easily ascertained. National and regional retailers and restaurants, by way of common examples, have stores in several states. As should be clear, determining venue based on the location of “principal assets” in these cases can be expensive and time-consuming and, if anything, points out the need to expand rather than limit venue choices so as to reduce litigation, uncertainty, and expense.

Recent experience under the Bankruptcy Code confirms that these new venue tests will be difficult to apply. The availability of “state of incorporation” as a venue choice has freed corporate chapter 11 debtors from the burden, expense, and distraction of venue litigation for decades. However, since 2005, one chapter of the Bankruptcy Code has required bankruptcy courts to apply a venue test similar to the venue tests that will be applicable to corporate chapter 11 debtors if state of incorporation ceases to be a clear, unequivocal basis for chapter 11 venue. Under chapter 15 of the Bankruptcy Code, the bankruptcy court must make a determination whether a foreign debtor’s foreign proceeding is a “main” or “non-main” proceeding. To be a “foreign main proceeding,” the proceeding must be a foreign proceeding “pending in the country where the debtor has the center of its main interests” or “COMI.”¹⁰ The bankruptcy courts have now had eight years’ experience with litigating COMI issues, and the results are unsettling.

Like the phrases “principal place of business” and “principal assets,” the phrase “center of main interests” is not fully defined in the Bankruptcy Code.¹¹ Judge Allan L. Gropper, a leading bankruptcy jurist, recently observed that “[t]he factors that go into the determination of COMI have been formulated and reformulated by the courts.”¹² Courts have considered numerous and varied factors including: the location of the debtor’s headquarters; the location of the managers; the location of the principal assets; the location of the majority of the debtor’s creditors; and the jurisdiction whose law

¹⁰ 11 U.S.C. § 1502(4).

¹¹ Unlike the general bankruptcy venue statute, chapter 15 does provide some guidance about the meaning of the phrase “center of main interest.” Section 1516 states: “[i]n the absence of evidence to the contrary, the debtor’s registered office, or habitual residence in the case of an individual, is presumed to be the center of the debtor’s main interest.” 11 U.S.C. § 1516. This is essentially a default rule that applies where the issue of COMI is not contested. *In re Artimm, S.R.L.*, 335 B.R. 149, 159 (Bankr. C.D. Cal. 2005).

¹² Hon. Allan L. Gropper, *The Model Law after Five Years: The U.S. Experience with COMI*, 2011 Norton Ann. Rev. of Int’l Insolvency 13, text at n.20 (2011).

would apply to most disputes.¹³ Judge Gropper’s grim assessment of the effects of COMI litigation is that “[t]he requirement that there be a COMI determination has, in too many cases, complicated and confused the process of recognition [of foreign proceedings].”¹⁴ He is not alone in expressing frustration about the burden COMI litigation puts on foreign debtors and the courts at the outset of chapter 15 cases.¹⁵

In light of the challenges that courts and parties have had in making fact-intensive venue determinations in chapter 15 cases, it is truly puzzling why the proponents of venue alteration would want to inject more uncertainty and opportunities for costly and burdensome litigation into the determination of venue for corporate debtors in chapter 11 cases. The venue choices that would remain will be increasingly difficult to apply, but ultimately less meaningful in large cases, as businesses continue to expand into multiple states and corporate decision-making becomes more diffuse. A chapter 11 debtor’s state of incorporation is the single venue option that can be conclusively and indisputably determined and, unlike principal place of business or location of principal assets, is never subject to challenge.

It is not surprising that the clarity afforded under the current venue provision is generally consistent with the rest of federal law. Federal statutes and case law repeatedly have found a corporation’s state of incorporation to be appropriate for venue purposes. Prior to the 1948 enactment of the federal provision that presently, generally governs venue, 28 U.S.C. § 1391, when a federal general venue statute laid venue in the district where one of the parties resided, a corporation was deemed to reside, and venue accordingly was proper, only in its state of incorporation.¹⁶ After the passage of 28 U.S.C. § 1391, when venue was laid where a party resided, venue was proper with respect to a corporation in its state of incorporation.¹⁷ The amendment of section 1391(c) in 1988 generally effected a substantial

¹³ *In re Bear Stearns High Grade Structured Credit Strategies Master Fund, Ltd.*, 389 B.R. 325, 336 (S.D.N.Y. 2008), *aff’ing* 374 B.R. 122 (Bankr. S.D.N.Y. 2007); *In re British Am. Ins. Co. Ltd.*, 425 B.R. 884, 908–09 (Bankr. S.D. Fla. 2010); *In re Betcorp Ltd.*, 400 B.R. 266, 290 (Bankr. D. Nev. 2009); *In re SphinX Ltd.*, 351 B.R. Bankr. S.D.N.Y. 2006), *aff’d* by 371 B.R. 10 (S.D.N.Y. 2007). *See also* Mark Lightner, *Determining the Center of Main Interests under Chapter 15*, 18 Norton J. of Bankr. L. & Practice 519, 521 (2009).

¹⁴ Gropper, *supra* note 12, text at n.27.

¹⁵ *See, e.g.*, Edward J. Janger, *Virtual Territoriality*, 48 Colum. J. Transnat’l L. 401, 410 (2010) (“At the moment, determining a debtor’s COMI is the most hotly litigated issue in international insolvency.”); Christopher J. Redmond, *COMI: In Search of Predictability*, 2010 Norton Ann. Rev. of Int’l Insolvency 14, 14 (2010) (“[I]n complex international cross-border insolvency proceedings . . . the location of the COMI of the debtor is often highly litigated and as a result less predictable. This lack of predictability and the lack of clearly discernable criteria by which a determination as to the COMI of a company is an issue which must be addressed and resolved.”); Susan Power Johnston, *2007 Developments in Chapter 15*, 2008 Ann. Surv. of Bankr. L. Part III § 22 (Aug. 2008) (“It is also quite possible to conceive of situations in which COMI could be hotly contested for a variety of legitimate reasons, in which case its determination would require development of a complex factual record with all the attendant delay that such disputes can engender, with the risk of concomitant harm to the estate.”).

¹⁶ *See Shaw v. Quincy Mining Co.*, 145 U.S. 444, 449-50 (1892).

¹⁷ *See Denver & R.G.W.R. Co. v. Bhd. of R.R. Trainmen*, 387 U.S. 556, 558-59 (1967).

expansion of venue choices for plaintiffs suing corporations, but did not remove the corporation's state of incorporation as a proper venue.¹⁸

Furthermore, a corporation's state of incorporation is appropriate venue pursuant to specific venue provisions governing various federal actions including, but not limited to: (1) patent infringement, 28 U.S.C. § 1400(b); (2) antitrust matters, 15 U.S.C. § 22; (3) CERCLA, 42 U.S.C. § 9613(b); (4) Securities Act of 1933, 15 U.S.C. § 77v; (5) Securities Exchange Act of 1934, 15 U.S.C. § 78aa; (6) Investment Advisors Act, 15 U.S.C. § 80b-14; (7) review of orders of federal agencies, 28 U.S.C. § 2343; (8) civil RICO claims, 18 U.S.C. § 1965; and (9) actions against automobile manufacturers brought by dealers regarding termination of franchise agreements, 15 U.S.C. § 1222. In *State of Delaware v. State of New York*, 507 U.S. 490 (1993), the Supreme Court rejected the notion that the principal place of business rather than state of incorporation should control escheat rights. Acknowledging the propriety of venue based on state of incorporation, Senator John Cornyn of Texas, as we all know one of the primary proponents of amending the current venue provision, opposed any change to a similar venue provision for patent infringement suits based on the state of incorporation of either the plaintiff or defendant in his opposition to a proposed amendment to the Patent Reform Act of 2007. When faced with an amendment that would limit venue choice and likely remove venue from the Eastern District of Texas, a popular venue for patent infringement lawsuits, Senator Cornyn stated that the amendment "unnecessarily makes waste of the experience and expertise that several federal judges in the EDTX have developed in the highly complex area of patent litigation."¹⁹

Stated simply, removing state of incorporation from the venue choices for corporations seeking chapter 11 protection would be an anomaly in the federal system, no doubt in large part as a result of the clarity provided by such an option (as well as other jurisdictional concerns, of course), and should be rejected. In the absence of a clear venue option, creditor groups may strategically commence value-destroying fights to move cases to jurisdictions perceived to be more favorable by alleging a case was filed in an improper venue; cases may be determined to have been filed in an improper (not just inconvenient) venue, resulting in further litigation regarding whether such cases should be dismissed or only transferred, and the possible dismissal (as opposed to transfer) of these cases in accordance with Bankruptcy Rule 1014(a)(2).²⁰ Any such dismissal could be disastrous to a debtor's estate, potentially

¹⁸ As enacted in 1948, section 1391(c) provided that "[a] corporation may be sued in any judicial district in which it is incorporated or licensed to do business or doing business, and such judicial district shall be regarded as the residence of such corporation for venue purposes." 28 U.S.C. § 1391(c) (1948). As amended in 1988, section 1391(c) now provides in pertinent part that, "[f]or purposes of venue under this chapter, a defendant that is a corporation shall be deemed to reside in any judicial district in which it is subject to personal jurisdiction at the time the action is commenced." This would include state of incorporation for any corporate entity.

¹⁹ See July 13, 2007 press release regarding the Patent Reform Act of 2007.

²⁰ Bankruptcy Rule 1014(a) states:

(a) Dismissal and Transfer of Cases.

(1) *Cases Filed in Proper District.* If a petition is filed in the proper district, the court, on the timely motion of a party in interest or on its own motion, and after hearing on notice to the petitioners, the United States trustee, and other entities as directed by the court, may transfer the

resulting in the forfeiture of preference recoveries and other avoidance actions tied to a petition date that would cease to be operative, and the quintessential “race to a courthouse” before a case could be re-filed.

But these points only speak to clarity and certainty of a court’s jurisdiction—what of convenience?

Access for parties in interest will not be materially improved in most large chapter 11 cases by limiting a debtor’s choice of forum to exclude a debtor’s state of incorporation. Creditors are often widely dispersed and located throughout the country, if not the world. In this global economy, it is simply not true that creditors are located near a debtor’s headquarters, and as a result, limiting venue to a debtor’s principal place of business, or the location of its principal assets, does not necessarily increase a creditor’s access to a bankruptcy court. No evidence exists, empirical or otherwise, supporting the blanket assertion that altering the venue rules will actually increase accessibility for or participation by creditors or other parties in interest. Similarly, most large debtors have substantial operations spread throughout the country. It is not uncommon for the majority of a company’s employees to be located in states other than where the principal place of business is located. Examples that spring immediately to mind are those where a debtor has retail operations or multiple manufacturing plants. Limiting a debtor’s venue to its principal place of business or principle assets would not meaningfully enhance the ability of such employees to participate in the process.

Moreover, in recent years, parties in interest have benefited from increasingly greater access to bankruptcy courts in other states as a result of substantial advances in technology and revised local rules of bankruptcy procedure. In 1991, at the beginning of the contemporary venue debate, Professor LoPucki and his colleague and co-author William C. Whitford acknowledged that large and complex corporate restructurings would likely always have issues with stakeholder access to bankruptcy proceedings—this stems from the fact that such companies often have stakeholders both across the nation and around the world.²¹ LoPucki and Whitford also acknowledged, however, that this burden on participation could be greatly reduced by the implementation and expansion of information technologies.²²

In recent years, advances in technology have provided immediate global public access to court dockets and pleadings in the federal court system generally and, as discussed in this testimony *infra*, the

case to any other district if the court determines that the transfer is in the interest of justice or for the convenience of the parties.

(2) *Cases Filed in Improper District.* If a petition is filed in an improper district, the court, on the timely motion of a party in interest or on its own motion, and after hearing on notice to the petitioners, the United States trustee, and other entities as directed by the court, may dismiss the case or transfer it to any other district if the court determines that transfer is in the interest of justice or for the convenience of the parties.

²¹ See Lynn M. LoPucki and William C. Whitford, *Venue Choice and Forum Shopping in the Bankruptcy Reorganization of Large, Publicly Held Companies*, 1991 Wis. L. Rev. 11, 48.

²² See *id.* at 49.

Delaware and Southern District of New York bankruptcy courts specifically. These advances have all but eliminated geographic hurdles to creditor participation and provided uniform access to the federal courts. Since 2000, the Administrative Office of U.S. Courts has worked to implement an electronic filing and case management system, the CM/ECF, which provides for electronic filing and access to documents. The CM/ECF System is in use in all bankruptcy courts, district courts and circuit courts of appeal. More than 41 million cases and 500 million documents are now accessible online through CM/ECF. Over 700,000 attorneys throughout the country have e-filed documents using CM/ECF.²³

Additionally, independent internet websites, such as those operated by corporate debtors, court-appointed claims agents, and other professionals, also provide access to critical case information, such as deadlines, forms, case dockets and status reports. The Delaware and Southern District of New York bankruptcy courts, among others, also have invested in videoconferencing and teleconferencing technology and support staff to allow parties to participate remotely in the judicial process. In many matters, participation in bankruptcy court hearings via video or teleconference has become a standard practice that often eliminates the need to be physically present in order to participate in the bankruptcy process. Both the Delaware and Southern District of New York bankruptcy courts, and over 30 other bankruptcy court districts across the country, utilize CourtCall, a vendor specializing in facilitation of telephonic and video courtroom conferencing, to supply advanced teleconferencing and/or videoconferencing capabilities.²⁴

These technological changes do not occur in a vacuum. In order to promote access for smaller stakeholders located around the country, bankruptcy courts have also modified their local rules to permit creditors and other parties to take advantage of these technological developments. For instance, the Delaware bankruptcy court has implemented local procedural rules to relax local counsel requirements and allow for greater remote creditor participation in bankruptcy proceedings.

In Delaware, creditors and shareholders, or their out-of-state counsel, are not required to associate with local counsel when addressing issues related to the filing of a proof of claim or interest and responding to any objection to such a proof of claim or interest.²⁵ Furthermore, such claimants may participate pro se and telephonically at any hearing related to the filing of a proof of claim or interest.²⁶ Government attorneys, such as attorneys for any state or local government or the Pension Benefit Guaranty Corporation, also do not need local counsel to appear in the Delaware bankruptcy court.²⁷ And in all other situations, parties have 30 days from the filing of their first pleading with the bankruptcy court to

²³ See <http://www.uscourts.gov/FederalCourts/CMECF/FAQs.aspx> (last visited October 17, 2013) for all CM/ECF figures set forth herein.

²⁴ See http://www.courtcall.com/ccallp/public_displaypage?pagename=Courts%20List (last visited October 17, 2013).

²⁵ See Del. Bankr. LR 9010-1(e).

²⁶ See Del. Bankr. LR 3007-1(g).

²⁷ See Del. Bankr. LR 9010-1(e).

affiliate with local counsel.²⁸ Often, issues raised by such a party can be heard and resolved by the court before the local counsel requirement even arises.

In conjunction with the technological advancements in the bankruptcy court, these local rules have expanded court access to numerous parties seeking to make their voices heard in large corporate reorganizations, significantly lessening the inconvenience to parties in interest of protecting their rights in a bankruptcy court such as Delaware's.

Even ignoring these sociological, technological and local developments, however, current statutory law, in and of itself, ensures that chapter 11 cases filed in truly inconvenient jurisdictions will be transferred. Once a chapter 11 case or other bankruptcy case is filed it may be transferred to another district in the interest of justice or for the convenience of the parties, pursuant to 28 U.S.C. § 1412 and Bankruptcy Rule 1014.²⁹ The statute applies to cases filed in the proper venue, as well as those cases filed in an improper venue.³⁰ Further, any party-in-interest in a bankruptcy case, including employees and creditors, may seek to transfer venue pursuant to 28 U.S.C. § 1412 and Bankruptcy Rule 1014.

By way of example, the Delaware bankruptcy court analyzes the following four factors when applying the "convenience of the parties" and "interest of justice" standards of Bankruptcy Rule 1014(a): (a) the proximity of the bankruptcy court to the interested parties; (b) the location of the debtor's assets; (c) the bankruptcy court's ability to administer the estate more economically; and (d) the relative economic harm to the debtor and the other interested parties by the transfer.³¹ These are among the same factors considered by bankruptcy courts in other jurisdictions, such as in Texas, Massachusetts, California, Florida and others, when deciding whether to grant a motion to transfer venue.³²

The Delaware bankruptcy court has specifically expressed its concern for the interests of creditors and other parties when considering venue motions. For example, Judge Walsh, United States Bankruptcy

²⁸ See Del. Bankr. LR 9010-1(d); D. Del. LR 83.5(e).

²⁹ See 28 U.S.C. § 1412.

³⁰ Compare 28 U.S.C. §§ 1404(a) and 1406(a). See also Fed. R. Bankr. P. 1014(a) and (b).

³¹ See *In re Infolink Grp. Inc.*, No. 10-10891, at 44-46 (Bankr. D. Del. June 2, 2010) (Transcript); *First New England Dental Ctrs., Inc.*, No. 98-347, letter op. at 4-5 (Bankr. D. Del. Mar. 20, 1998); *In re Ernst Home Ctr., Inc.*, Nos. 96-1088 and 1099, bench ruling at 2-3 (Bankr. D. Del. Mar. 8, 1996) (Transcript); see also *Jumara v. State Farm Ins. Co.*, 55 F.3d 873, 879-80 (3d Cir. 1995); *Son v. Coal Equity, Inc. (In re Centennial Coal, Inc.)*, 282 B.R. 140, 144 (Bankr. D. Del. 2002); *In re Del. & Hudson Ry. Co.*, 96 B.R. 467, 486 (Bankr. D. Del. 1988); *In re Ocean Props. of Del., Inc.*, 95 B.R. 304, 305 (Bankr. D. Del. 1988); *In re Racing Servs., Inc.*, No. 04-10349, at 54:9-25 – 55:1-16 (Bankr. D. Del. Feb. 11, 2004) (Transcript); See *In re Innovative Comm'n Co., LLC*, 358 B.R. 120, 126-8 (Bankr. D. Del. 2006).

³² See *Gulf States Exploration Co. v. Manville Forest Prods. Corp. (In re Manville Forest Prods. Corp.)*, 896 F.2d 1384, 1391 (2d Cir. 1990); *In re Donald*, 328 B.R. 192, 204 (B.A.P. 9th Cir. 2005); *Puerto Rico v. Commonwealth Oil Ref. Co. (In re Commonwealth Oil Ref. Co.)*, 596 F.2d 1239, 1247 (5th Cir. 1979); *In re Dunmore Homes, Inc.*, 380 B.R. 663, 672 (Bankr. S.D.N.Y. 2008); *In re MacDonald*, 73 B.R. 254 (Bankr. N.D. Ohio 1987); *In re Baltimore Food Sys. Inc.*, 71 B.R. 795 (Bankr. D.S.C. 1986); *In re Walter*, 47 B.R. 240 (Bankr. M.D. Fla. 1985); *In re Almeida*, 37 B.R. 186 (Bankr. E.D. Pa. 1984).

Court Judge for the District of Delaware, in *USM Corp.*, granted a motion to transfer venue to protect the rights of retirees and stated “it gives these people some comfort to be able to firsthand observe what is going on and undertake whatever efforts they believe to protect their interest, they can do it at the Boston location rather than here.”³³ This case is an example of the propensity of the Delaware bankruptcy court to give full consideration to the interests of retirees seeking to transfer venue, and illustrates that such motions will be granted when pursued by interested parties. Yet another example of the Delaware bankruptcy court’s balanced approach to venue transfer motions is demonstrated by Judge Walsh’s comments in the *Hawaiian Telecom* case:

Let me comment on the venue issue. And quite frankly it’s troubling me. And the reason it’s troubling me is aside from electricity, this is a utility that has a significant impact probably on 99% of the population of the state ... And I am concerned that if something bad happens, then they’re going to say it’s because it was on somebody else’s court. Namely this one. Not where it should have been with the appropriate consideration for the population in general.³⁴

Likewise, in *Qualteq, Inc.*, Judge Kevin J. Carey granted a motion to transfer venue to the Northern District of Illinois in 2012 where one of the debtors’ stated reasons for filing in Delaware was to file in a forum away from large, ongoing litigation in Illinois and where, among other things, approximately 45.5% of the creditors listed on the debtors’ creditor matrix contained an Illinois address, and 77% of the debtors’ scheduled indebtedness was listed as owed to creditors with an Illinois address.³⁵ In so ruling, Judge Carey stated bluntly: “the Debtors’ obvious attempt to ‘escape’ the forum best suited for administration of these chapter 11 cases should not be condoned.”³⁶

It is a common misconception that venue transfer motions are not granted. From 2006 through 2012, however, motions to transfer venue out of the Delaware bankruptcy court were ruled upon by the bankruptcy court in 13 different non-affiliated chapter 11 cases. In nine of these thirteen different chapter 11 cases, or roughly 69.2%, the Delaware bankruptcy court transferred venue. This is not an anomaly; historically, dating back over 20 years, the Delaware bankruptcy court has consistently granted approximately 60% of such motions. Further, on at least three different occasions during the period from 2003 through 2012, judges of the Delaware Bankruptcy Court on their own raised the issue of transferring venue and in all three cases, the court transferred the pending chapter 11 cases out of

³³ *In re USM Corp.*, No. 05-10272, at 26:4-8 (Bankr. D. Del. Feb. 3, 2005, Judge Peter J. Walsh) (Transcript).

³⁴ *In re Hawaiian Telecom Communications, Inc.*, No. 08-13086, at 8:5-14 (Bankr. D. Del. Dec. 2, 2008, Judge Peter J. Walsh) (Transcript).

³⁵ See Memorandum and Order Transferring Venue, *In re Qualteq, Inc.*, No. 11-12572, (Bankr. D. Del. Feb. 16, 2012, Judge Kevin J. Carey), ECF Nos. 106 & 732.

³⁶ *See id.*

Delaware.³⁷ (The Court has also transferred certain adversary proceedings. This statistic does not include the many adversary matters that have been transferred by the Delaware Bankruptcy Court.)³⁸

Some have argued that bankruptcy courts do not consider motions to transfer venue until a month or two after the case was filed, thus causing a delay that could inconvenience everyone involved. However, on multiple occasions the Delaware bankruptcy courts has recognized the importance of granting motions to transfer venue within the first thirty days of the case, in addition to granting the other relief necessary to stabilize the debtor, in order to ensure that the matter is quickly before the proper court.³⁹

Current statutory law provides the best of both worlds—a venue provision that provides at least one clear venue choice in nearly every case, and a separate provision that allows a case to be transferred when truly more inconvenient than other permissible locations for the majority of parties in interest. Both provisions work well to achieve their important goals. Therefore, I submit the current venue statute should not be altered in the name of convenience.

The Efficiency of Delaware and the Academic Debate

From my perspective as a bankruptcy practitioner, it is obvious that removing state of incorporation as a basis for venue will lead to an overall increase in the cost of corporate reorganization that will ultimately harm employees, creditors and the market generally. It is axiomatic that increasing the costs of and delay attendant to a corporate reorganization will result in fewer assets being available to satisfy employees, creditors and other stakeholders, and a higher likelihood of non-going-concern liquidations, which destroy jobs. The existing venue provision has fostered the development of highly experienced courts in complex business bankruptcies, resulting in quicker trips through reorganization. Although the debate among academics rages on as to the reasons why, as discussed below, this was true in 2006 when Professors Kenneth Ayotte and David A. Skeel, Jr. analyzed a broad sampling of bankruptcy cases

³⁷ See Order Requiring Debtor to Appear and Show Cause Why Case Should Not be Transferred and Order Transferring Case, *In re Dr. Barnes' Eyecenter, Inc.*, No. 04-10784 (Bankr. D. Del. Mar. 10, 2004, Judge Mary F. Walrath), ECF Nos. 9 & 15; Order Transferring Ch. 11 Case Pursuant to Bankr. R. 1014(a)(1) and Transcript regarding Hearing, *In re Three S Delaware, Inc.*, No. 08-13068 (Bankr. D. Del. Dec. 10, 2008, Judge Peter J. Walsh), ECF Nos. 20 & 24; Order Transferring Cases and Adversary Proceedings sand Transcript regarding Hearing, *In re RC Sooner Holdings, LLC, et al.*, No. 10-10528 (Bankr. D. Del. June 14, 2010, Judge Brendan Linehan Shannon), ECF Nos. 204 & 211.

³⁸ All statistics set forth in this paragraph are on file with the Officer of the Clerk of the United States Bankruptcy Court for the District of Delaware. Information not available for period of October 1996 through 1997. A grouping of affiliated cases is treated as a single case for purposes of these statistics.

³⁹ See, e.g., *In re Racing Servs., Inc.*, No. 04-10349, at 55:12-16 (Bankr. D. Del. Feb 11, 2004, Judge Mary F. Walrath) (Transcript) (“I think it’s more important to transfer it now rather than to wait, because of the necessity to address the serious issue raised with respect to Section 543 on whether the receiver can be excused from turning over the assets of the debtor to the debtor’s estate.”); *In re USM Corp.*, No. 05-10272, at 26:24-5 – 26:1 (Bankr. D. Del. Feb. 3, 2005, Judge Peter J. Walsh) (Transcript) (“And I think it is appropriate to do it earlier rather than later. And for those reasons, I will grant the [venue] motion.”); *In re CHA Hawaii LLC*, No. 08-12027, at 9:17-18 (Bankr. D. Del. Sept. 19, 2008, Judge Peter J. Walsh) (Transcript) (granting motion to transfer venue at Second Day Hearing).

to “confirm the general perception and other researchers’ findings that the Delaware bankruptcy judges handled cases appreciably faster than the judges in other districts.”⁴⁰

While there may not be a direct correlation between shorter case duration and lower professional fees in every case, a shorter case duration should tend on the whole to reduce the overall costs associated with a bankruptcy reorganization case. Indeed, the recent successful restructuring and sale of General Motors in the Southern District of New York bankruptcy court demonstrates the value of speed in keeping professional fees and other reorganization costs in check. Prior to the GM bankruptcy case, Professor LoPucki forecast that the massive GM bankruptcy case would produce professional fees nearing \$1 billion.⁴¹ However, the case proceeded quickly and efficiently, with substantially all of GM’s assets being sold in the initial 40 days of the bankruptcy case and a liquidating chapter 11 plan being consummated less than nine months later. As a result of these and other efficiencies, total professional fees in the chapter 11 case topped out at approximately \$110 million. Even Professor LoPucki was forced to concede that the GM bankruptcy was “unusually inexpensive” for its size.⁴²

Furthermore, the benefits of speedy reorganizations extend beyond keeping professional fees in check. In general, a quick trip through bankruptcy means a quicker dividend to creditors on their claims. It also means less uncertainty to employees, vendors and other parties that interact with corporate debtors. If a corporation exits bankruptcy sooner, it allows all those parties to plan for the future.

Another critical factor in considering state-of-incorporation venue is the willingness of lenders to extend bankruptcy loans in jurisdictions without an established record of effectively or quickly handling large chapter 11 cases. It has been true for some time that most companies that file for bankruptcy in Delaware have very significant levels of secured debt. Further logic and practical experience teach that a company’s secured lenders have significant input in its choice of venue for a bankruptcy filing. The reality for many over-leveraged companies is that, to successfully reorganize, they will need debtor-in-possession financing from their existing secured lenders or, at minimum, the consent of their secured lenders to the company’s use of cash after the company files bankruptcy. This gives secured lenders, who effectively hold the company’s purse strings, significant leverage over venue choice. Both the Delaware and Southern District of New York bankruptcy courts have well-developed precedent and procedures governing DIP financing transactions and other aspects of bankruptcy reorganizations, which provides lenders and debtors with a measure of certainty as to what can and cannot be accomplished. A change in venue laws specifically designed to remove venue based on state of incorporation will upset this paradigm and is apt to cause many lenders to rethink their willingness to lend to distressed businesses in chapter 11 cases, resulting in more chapter 7 non-going-concern liquidations. And those

⁴⁰ See Kenneth Ayotte and David A. Skeel, Jr., *An Efficiency-Based Explanation For Current Corporate Reorganization Practice*, 73 U. Chi. L. Rev. 425, 461 (Winter 2006) (“[W]e find that Delaware cases are 168 days faster than cases elsewhere, a speed effect that is statistically significant.”).

⁴¹ See Eric Morath, GM Bankruptcy Case ‘Unusually Inexpensive’, The Wall Street Journal Bankruptcy Beat Blog (Posted July 26, 2011, at 4:08 p.m. ET).

⁴² See *id.*

lenders that are still willing to extend credit to chapter 11 debtors may do so only at a significantly higher cost of capital than that which currently prevails in bankruptcy cases in Delaware and Southern District of New York. This, in turn, will create a greater risk that reorganizations will fail, resulting in the loss of jobs and greater inefficiency in the redeployment of the assets of bankrupt companies.

Changing the venue rules would likely result in increased costs to taxpayers as well. In addition to having substantial experience in large and complex reorganizations, the bankruptcy courts and the Office of the United States Trustee in Delaware and the Southern District of New York have the infrastructure in place to handle such cases. In a time when the nation is facing large government deficits and funding issues, amendments to the venue rules will require substantial investment in infrastructure and personnel in courts around the country that are already overburdened with consumer bankruptcies.

Indeed, over the last two decades, the Delaware bankruptcy court has put in place a robust information technology backbone required by the volume of filings such cases generate, including servers, back up servers and additional IT staff. Additionally, in 2005-2006, the Delaware bankruptcy court added additional courtrooms, expanded the size of most of its courtrooms and added videoconferencing and teleconferencing capabilities in all of its courtrooms. These investments were principally directed at meeting the demands of the large corporate reorganization cases that frequently file in Delaware. Most other bankruptcy courts, in contrast, have not had the occasion of Delaware and the Southern District of New York to make such infrastructure investments and likely would be challenged in the near term to provide creditors and other interested parties with the same level of access—both in person and remotely—to court proceedings in mega bankruptcy cases. Furthermore, the Delaware bankruptcy court maintains a help desk designed to respond to inquiries from the thousands of creditors and other interested parties that frequently call the court for information about mega bankruptcy cases.

It is also my understanding that the Delaware and Southern District of New York bankruptcy courts are permanently staffed at levels necessary to service large chapter 11 cases, while other bankruptcy courts often have to request supplementary staffing assistance from the Administrative Office of the United States Courts when a mega case files in their jurisdiction. The Administrative Office then assigns one or more temporary staffers to the court for the anticipated duration of the case, and, as a result, must incur the salary and benefits for the newly added temporary court personnel. If venue is restricted in a way that reduces the concentration of large corporate chapter 11 cases in Delaware and Southern District of New York, it can be expected that the frequency of such staffing requests to the Administrative Office will increase dramatically. The aggregate cost of adding temporary court personnel in many jurisdictions throughout the country is likely to far outstrip the cost to have additional personnel permanently on staff in a few locations such as Delaware and the Southern District of New York. Permanent personnel changes following a venue amendment would likewise will be problematic; this additional investment necessarily will be inefficient because it will have to be made in many of the bankruptcy courts across the country, as removing state of incorporation eliminates a predictable venue option in favor of a system in which it will be more difficult to predict where cases will file. There is, therefore, significant risk that money will be required to be spent in a great number of

bankruptcy jurisdictions even though there surely will be no material increase in the number of chapter 11 cases filed in many of those jurisdictions.

It should also be noted that proposed venue amendments often include provisions removing or severely restricting the ability of affiliated corporations with different principal places of business or location of assets from filing together. This will lead to increased costs of reorganization due to the loss of savings from joint administration of related cases.

That is the perspective of this practitioner. That said, I recognize the academic debate that has raged over the last 20 years regarding whether the concentration of large chapter 11 cases in Delaware and the Southern District has produced better, or worse, results in chapter 11 practice. And I recognize the debate continues and further replies may be forthcoming by Professor LoPucki and others. That said, from my admittedly non-academic perspective, it seems a few points are in order regarding this debate.

First, it seems that when Professors LoPucki and Whitford first surfaced with modern criticism of current venue rules in 1991, it was alleged debtors would forum shop to where exclusivity would be extended the longest—the Southern District of New York—so that debtors could use the threat of lingering in bankruptcy to exact extra leverage over creditors.⁴³ Indeed, a number of non-venue articles from this time spoke of chapter 11 confirmations increasingly taking longer and longer, so much that wholesale replacement of chapter 11 with other means of maximizing value of and/or reorganizing failed firms were all the rage.⁴⁴

The argument that debtors would shop for a forum where they could long-term park in chapter 11 was soon abandoned, however, when the predominant large chapter 11 venue became Delaware, which even critics of the current venue statute acknowledged confirmed cases quicker than other jurisdictions.⁴⁵ The critique of “venue shopping” then became that it encouraged courts to rubber-stamp unfeasible chapter 11 plans in the interest of pleasing debtors with quicker exits from chapter 11, which led to higher re-filing rates and business failures after emergence from chapter 11.⁴⁶ When Delaware re-filing rates went down slightly and other districts went up to become roughly equal, the argument championed by critics of the current venue provision then became that this was because the

⁴³ See *supra* note 21 at 30-32, 35-36, 48 & 57-58.

⁴⁴ See, e.g., Lynn M. LoPucki, *The Trouble with Chapter 11*, 1993 Wis. L. Rev. 729 (discussing this problem and collecting prior articles making this observation in note 3 and elsewhere).

⁴⁵ See, e.g., Lynn M. LoPucki & Joseph Doherty, *Why Are Delaware and New York Bankruptcy Reorganizations Failing?*, 55 Vand. L. Rev. 1933, 1984-1985 (2002). Of course, after the shift to Delaware occurred, section 1121 of the Bankruptcy Code was also amended to limit the amount of time a debtor’s exclusivity may be extended.

⁴⁶ See, e.g., *id.* (“Several other factors suggest that the Delaware reorganization process is less thorough than that of Other Courts. Our data show that the Delaware process is quicker. Unpublished data show that the Delaware process is slightly less expensive than that of Other Courts - even though professionals appear to be paid at higher rates in Delaware and Delaware requires local counsel in every case. Some bankruptcy lawyers and judges have told us that the Delaware Bankruptcy Court discourages adversary proceedings and objections to claims.”).

Delaware contagion had spread through other courts adopting Delaware's procedures—and that the period of Delaware's ascendancy, 1991-1996, was thus the only relevant period to review.⁴⁷

In my opinion (and not necessarily that of my firm, any of my partners, or anyone else) the shifts in the academic theory seem to show that if you are looking for a witch, you will find a witch—the manifestation of the problem has evolved to fit the theory that there is a problem. The tail is seemingly wagging the dog.

Moreover, academic commentaries have showed that the venue critics' data and conclusions regarding Delaware's period of ascendancy and the spread of its "contagion" are flawed. Specifically:

Professors Douglas G. Baird and Robert K. Rasmussen have noted that the data analyzing the chapter 11 cases confirmed in Delaware during its "period of ascendancy" (1991-1996) inappropriately lumps prepackaged and traditional cases, inappropriately skewing the numbers against Delaware and its large number of prepackaged cases during this time, which involve less substantial reorganization and debt reduction given their consensual nature.⁴⁸

In a separate article from his joint work with Professor Baird, Professor Rasmussen has noted that there were only nine traditional confirmed chapter 11 reorganization cases included in the study by Professor LoPucki that gave rise to his theory that large public Delaware chapter 11 cases were more likely to refile within five years during Delaware's "period of ascendancy." Professor Rasmussen detailed the three refilings among these nine traditional confirmed chapter 11 cases from Delaware's "period of ascendancy," and concluded these three cases refiled because of events beyond any control of the bankruptcy court. Specifically, first, Harvard Industries re-filed over four and a half years after its emergence because of a failed acquisition that took place after it emerged from bankruptcy and that was overseen by a CEO installed after the bankruptcy emergence. Second, United Merchants and Manufacturers filed over four and a half years after its emergence as a result of the inability of a subsidiary that was not part of the first filing to manage its debt service. Third, and finally, TWA re-filed—something not uncommon in this decidedly troubled industry, as Continental

⁴⁷ See Lynn M. LoPucki, *Courting Failure: How Competition for Big Cases Is Corrupting the Bankruptcy Courts* (Michigan 2005); see also Lynn M. LoPucki & Joseph W. Doherty, *Delaware Bankruptcy: Failure in the Ascendancy*, 73 U. Chi. L. Rev. 1387 (2006); Lynn M. LoPucki, *Where Do You Get Off, A Reply to Courting Failure's Critics*, 54 Buff. L. Rev. 511, 517-18 (2006).

⁴⁸ See Douglas G. Baird & Robert K. Rasmussen, *Beyond Recidivism*, 54 Buff. L. Rev. 343 (2006).

demonstrated when it filed in Houston before later re-filing in Delaware.⁴⁹

Professor Melissa B. Jacoby has noted that the anecdotal evidence in support of this “contagion” beginning in 1997 relies on anecdotal examples of policy changes that took place only in 1997 or later, undermining this theory (but I will note this has been responded to by a claim that some official changes took place in early 1997, and unofficial changes allegedly may have taken place sooner).⁵⁰

Recent empirical work by Professor Stephen J. Lubben shows other factors, such as general interest rates at time of emergence, are far better predictors of a re-filing, and that inclusion of bankruptcy court actually decreased the predictability of his model.⁵¹

Judges from districts that are not widely viewed as benefitting from the current venue rules have criticized the thesis that bankruptcy judges would compete for prestige through large chapter 11 cases.⁵²

Of course, the academic debate continues. I trust responses—and further counter-responses—will continue to come in due course.⁵³

In closing, I again thank you for allowing me to testify regarding this issue. I welcome your questions.

⁴⁹ See Robert K. Rasmussen, *Empirically Bankrupt*, 2007 Colum. Bus. L. Rev. 179, 217-245 (2007).

⁵⁰ See Melissa B. Jacoby, *Fast, Cheap, and Creditor-Controlled: Is Corporate Reorganization Failing?*, 54 Buff. L. Rev. 401 (2006). For response to this and other criticisms, including Baird and Rasmussen, see LoPucki, *Where Do You Get Off*, *supra* note 45.

⁵¹ See Stephen J. Lubben, *Delaware's Irrelevance*, 16 Am. Bankr. Inst. L. Rev. 267 (2008).

⁵² See, e.g., Hon. Robert D. Martin, *Courting Failure? The Effects of Venue Choice on Big Bankruptcies*, 54 Buff. L. Rev. 503 (2006).

⁵³ Indeed, a forthcoming article that will soon be published in the Connecticut Law Review raises a new argument against allowing state of incorporation as a basis for venue. Examining the percentage of large, publicly filed chapter 11 cases filed in either Delaware or the Southern District of New York, it theorizes that the current venue rule is destroying the proper evolution of bankruptcy law by concentrating chapter 11 decisional law in Delaware and the Southern District of New York, rather than nationwide. See Samir D. Parikh, *Modern Forum Shopping in Bankruptcy*, Conn. L. Rev. (forthcoming 2013).

This argument overlooks, among other things, the fact that smaller chapter 11 cases are filing outside of Delaware and the Southern District of New York in droves. Of the 1,170,324 bankruptcy cases filed in the United States in the twelve-month period ending March 31, 2013, 8,413 were cases where a company sought to reorganize under chapter 11 of the Bankruptcy Code. Of those 8,413 business reorganization cases, 596 filed in the District of Delaware and 616 filed in the Southern District of New York. In other words, approximately 85.6% of chapter 11 corporate cases filed somewhere other than the Southern District of New York or Delaware. See <http://www.uscourts.gov/Statistics/BankruptcyStatistics/12-month-period-ending-march.aspx> (last visited October 17, 2013).