

# Bankruptcy Judges Handle Much More Than Bankruptcy Matters

By Randall Newsome

**M**uch of what goes on in bankruptcy court has little to do with bankruptcy laws or rules. Commercial lawyers and litigators seeking a suitable ADR specialist to help resolve their disputes may want to consider a retired bankruptcy judge.

Most general practitioners, and indeed many commercial litigators, shudder at the thought of having to handle bankruptcy matters or appear in bankruptcy court. They view it as an arcane, mystifying corner of the law best left to bankruptcy specialists. The fact that bankruptcy rules largely track the Federal Rules of Civil Procedure, and that bankruptcy courts have made a concerted effort to look and act like any other trial court, seems to have done little to assuage these fears.

But what many lawyers may not know is that many issues arising in bankruptcy cases have little or nothing to do with bankruptcy law. The U.S. Supreme Court has customarily directed bankruptcy courts to look to state or general federal law to resolve property rights. And while the Supreme Court has narrowed the jurisdiction of bankruptcy judges to finally decide nonbankruptcy law issues, they still have jurisdiction to enter a judgment on any matter that relates to a bankruptcy case if the parties consent, or to make a report and recommendation to a district court if they don't consent. They are also routinely called upon to decide ancillary nonbankruptcy matters that arise in bankruptcy cases. For those

seeking an arbitrator, it's important to remember that virtually all disputes in bankruptcy court are decided by bench trials, not jury trials, which means that bankruptcy judges are accustomed to preparing findings of fact and conclusions of law.

Bankruptcy judges are often confronted with nonbankruptcy issues from the very beginning of a case. Chapter 11 cases, which generally involve business reorganizations, require the appointment of professionals to represent the debtor and other constituencies. These professionals are required to be "disinterested," as that term is defined in the bankruptcy code, but they also cannot have any conflicts of interest under general rules of practice. Bankruptcy judges are also often required to decide these difficult qualification issues at the outset of a case.

Once a professional is appointed, his or her compensation must be set by the bankruptcy judge. Although there are specific bankruptcy provisions that guide this inquiry, the judge must follow general federal jurisprudence governing compensation of professionals, such as the lodestar method and the 12-factor test used by some courts. Bankruptcy judges deal with compensation issues more often than any other judicial officer, with the possible exception of probate court judges.

The same holds true for valuation issues. Bankruptcy judges are constantly called upon to decide nettlesome issues



U.S. Bankruptcy Judge Randall Newsome (Ret.) who is now a neutral at JAMS

of valuation: Is the value of the debtor's property less than the amount of debt that encumbers it, thus justifying the lifting of the bankruptcy automatic stay to allow it to be foreclosed upon? Will a Chapter 11 plan pay creditors more than they would have received in a liquidation? Is a secured creditor receiving the "indubitable equivalent" of its claim? Will secured creditors receive deferred cash payments equal to the present value of their claims?

The issues regarding secured claims don't end with valuation. The validity and priority of secured claims under Uniform Commercial Code (UCC) Article 9 and other state laws frequently arise in bankruptcy court. Other parts of the UCC also come into play, such as Article

2 and Article 3. State law issues regarding contracts are decided routinely in the process of determining the validity of bankruptcy claims.

Almost every conceivable commercial and financial issue arises in the course of a Chapter 11 case. Over time, the complexity of financial failures has steadily increased, and sometimes contributes to the debtor's demise. Witness the Baldwin-United bankruptcy, which I presided over as a young judge. The tax arbitrage schemes, the Byzantine corporate holdings, and the blizzard of inter-company transfers used to prop up the insurance reserves for the company's multi-billion-dollar annuity business were challenging enough, but they pale in comparison to what Enron and Lehman Brothers were doing. All of the state law issues that emerge during the dissolution of business organizations, from partnerships and corporations to limited liability companies to business trusts, are dealt with in bankruptcy courts.

Corporate governance issues also frequently arise in large Chapter 11 cases. For example, should a shareholder's demand for a shareholders' meeting be granted in the midst of a Chapter 11? Should a company honor its obligation to indemnify officers and directors for their costs and damages in lawsuits filed against them? Are the directors who rode the company into bankruptcy too conflicted to remain on the board? These issues often implicate directors and officers insurance. Suing for coverage under these policies has become routine in Chapter 11 cases. I have conducted a number of mediations involving these claims, which can be tricky to pursue, as any suggestion of fraud by the corporate officers may jeopardize coverage. Alleged breaches of fiduciary duty arise in this and many other contexts in bankruptcy cases.

Unfortunately, bankruptcy judges frequently are called upon to determine all types of fraud issues. Claims of fraudulent transfer under both state and federal laws are equally common.

One of the principal ways of maximizing the value of a debtor or bankruptcy estate is by selling property and assuming and assigning executory contracts and leases. Indeed, filing a Chapter 11 petition and obtaining bankruptcy court approval of a sale with all its attendant protections is often a prerequisite for the acquisition of a troubled company. Bankruptcy judges thus become familiar with the acquisition and divestiture process and pitfalls. Because information technology and biotech companies are frequent visitors to bankruptcy court, bankruptcy judges also gain familiarity with intellectual property, particularly patent licenses and their assignability. The subject of trade secret theft also crops up on occasion.

Restaurants, automobile dealerships and other franchisees are also frequent visitors, and present issues regarding franchise agreements, including their assignability and validity. Retail chains and other brick-and-mortar businesses raise a myriad of landlord-tenant issues. Shopping center leases bring their own peculiar issues in the bankruptcy context. Therefore, bankruptcy judges deal with the whole range of real and personal property law in the course of performing their duties.

Not surprisingly, Chapter 11 debtors frequently have environmental problems, from leaky tanks at gas stations to massive Superfund liabilities. The Tronox bankruptcy offers just one example of how extensive those liabilities can be. Tronox was spun off from a major oil company and burdened with all kinds of legacy toxic assets. A fraudulent transfer lawsuit (in which I served as a mock judge) led to exhaustive findings of lia-

bility by the bankruptcy judge, resulting in a settlement in which the defendants paid over \$5 billion.

The topics highlighted above do not represent a complete catalog of all of the state and federal law issues that bankruptcy judges confront on a daily basis. Because all bankruptcy judges handle every kind of bankruptcy—from the no-asset Chapter 7 case to the largest Chapter 11 mega-case—the range of civil legal issues they confront equals or exceeds that of many judges who serve on courts of general jurisdiction. If you have a business or commercial problem that might benefit from an early neutral evaluation, mediation or mock trial, or that requires resolution through arbitration, a retired bankruptcy judge might be the right person to turn to.

*Judge Randall Newsome (Ret.) is a neutral at JAMS where he serves as a mediator, arbitrator and discovery master for disputes in a variety of areas including bankruptcy, business/commercial, employment, government, securities and professional liability. Previously, he spent 28 years as a settlement and bankruptcy judge, most recently as chief judge of the U.S. Bankruptcy Court, Northern District of California.*

