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THE BANKRUPTCY AMENDMENTS AND FEDERAL JUDGESHIP ACT OF 1984: A STEP BACKWARD IN REDUCING JURISDICTIONAL DELAY

The entire history of bankruptcy law is shrouded in attempts to define the parameters of the bankruptcy tribunal's jurisdiction.[1] Federalism and separation of powers priniciples merge to render a precise definition of the appropriate scope of bankruptcy law theoretically complex.[2] These theoretical difficulties directly translate into burdensome jurisdictional delays in bankruptcy proceedings which are detrimental to debtors and creditors alike. The theoretical confusion would be simplified and the resulting delays alleviated if Congress established bankruptcy courts pursuant to the judicial power provided for in Article III of the United States Constitution.[3] Congress has steadfastly refused to grant bankruptcy courts Article III status, however, choosing instead to establish them pursuant to the congressional power contained in Article I.[4]

The Bankruptcy Amendments and Federal Judgeship Act of 1984[5] (Bankruptcy Amendments) represents Congress' most recent attempt to resolve the jurisdictional problems which impede the progress of bankruptcy proceedings pursuant to its power under Article I. Unfortunately, the Bankruptcy Amendments not only add to the theoretical confusion, but also provide new opportunities for litigants to object to bankruptcy proceedings on jurisdictional grounds, thereby fostering further delay. In addition, the jurisdiction granted federal district courts under the Bankruptcy Amendments may exceed the constitutional scope of federal subject matter jurisdiction.[6] The time has come, therefore, to re-examine Congress' persistent refusal to grant bankruptcy courts Article III status and to evaluate

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1. One author has noted that every volume of the Federal Reporter through 1940 contains opinions resolving objections to the bankruptcy tribunal's jurisdiction. MacLachlan, *Scope of the Summary Jurisdiction of the Bankruptcy Court*, 40 COLUM. L. REV. 489, 490 n.2 (1940).

2. *See* Northern Pipeline Constr. Co. v. Marathon Pipeline Co., 458 U.S. 50 (1982).

3. U.S. CONST. art. III, § 1.

4. U.S. CONST. art. I, § 1. Among Congress' enumerated powers is the power to establish uniform laws on the subject of bankruptcy. *Id.* § 8, cl. 4.

5. Pub. L. No. 98-353, 98 Stat. 330 (codified in scattered sections of Titles 11 & 28 of the United States Code).

6. The Constitution limits the jurisdiction of federal courts to cases involving federal subject matter. *See* U.S. CONST. art. III, § 2.

the wisdom of continuing to determine the scope of bankruptcy jurisdiction within the ill-defined confines of Article I.

The jurisdiction of bankruptcy courts is necessarily dependent upon the constitutional source of their authority. Courts established pursuant to the judicial power contained in Article III may exercise jurisdiction over cases arising under federal law and all cases between citizens of diverse citizenship.[7] The Constitution also requires that Article III judges must be given life tenure and protection against salary diminution.[8] An Article III court's exercise of jurisdiction is subject to objections based upon federalism principles. Litigants often object, for example, to the jurisdiction of federal district courts on the ground that federal subject matter is lacking and, therefore, the court's exercise of jurisdiction would infringe upon the province of state courts. An entire body of law has evolved in response to these objections, thereby adding certainty to the appropriate scope of an Article III court's jurisdiction.[9]

In contrast to Article III courts, Article I judges are not constitutionally granted life tenure or given protection against salary diminution. Moreover, the jurisdiction of courts established pursuant to the congressional power contained in Article I is ill-defined.[10] In addition to the federalism objections which confront Article III courts, an Article I court's exercise of jurisdiction is subject to objections based upon separation of powers principles. An Article I court's exercise of jurisdiction is not only subject to the objection that federal subject matter is lacking, but also to the objection that the court is exercising jurisdiction over a controversy which can only be heard constitutionally in an Article III court.[11] It is this separation of powers problem, between Congress' power under Article I and the judicial power under Article III, which has, in large part, been responsible for the jurisdictional delays which have historically plagued bankruptcy proceedings. This separation of powers problem first manifested itself in the burdensome, bifurcated system of adjudication which existed under traditional bankruptcy laws.

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7. *Id.* Federal courts have constitutional authority to exercise jurisdiction over other specific types of cases unrelated to bankruptcy, such as cases involving admiralty law. *Id.*

8. *Id.* § 1.

9. *See, e.g.*, United Mine Workers v. Gibbs, 383 U.S. 715 (1966) (ancillary and pendent jurisdiction); Osborn v. Bank of the United States, 22 U.S. (9 Wheat.) 738 (1824) ("arising under" jurisdiction); Strawbridge v. Curtiss, 7 U.S. (3 Cranch) 267 (1806) (diversity jurisdiction). *See also* H. HART & H. WECHSLER, THE FEDERAL COURTS AND THE FEDERAL SYSTEM 12-18 (2d ed. 1973) (general discussion of the scope of federal court jurisdiction).

10. *See, e.g.*, National Mut. Ins. Co. v. Tidewater Transfer Co., 337 U.S. 582 (1949) (holding unclear).

11. *See* Northern Pipeline Constr. Co. v. Marathon Pipeline Co., 458 U.S. 50 (1982) (plurality opinion).

Traditionally, jurisdiction over all bankruptcy proceedings resided in the federal district courts.[12] The district courts referred certain types of proceedings to bankruptcy "referees."[13] Because referees were not Article III judges their jurisdiction only extended over what were termed "summary proceedings."[14] Summary proceedings were limited to those controversies where the property in dispute was in the actual or constructive possession of the bankruptcy trustee.[15] Those controversies which fell outside the referee's summary jurisdiction were termed "plenary proceedings"[16] and could only be heard in the district court or in a state court.[17]

The distinction between summary and plenary proceedings was merely a manifestation of the underlying separation of powers problem. The limited scope of the bankruptcy referee's jurisdiction was necessitated by the fact that they were not Article III judges. It was the limited scope of the bankruptcy referee's jurisdiction which, in turn, necessitated a bifurcated system of adjudication. The procedures which existed under the referee approach to bankruptcy proceedings eventually proved unworkable. Attorneys frequently objected to the referee's jurisdiction on the ground that the property at issue was not in the actual or constructive possession of the bankruptcy trustee. Delays resulted not only from objections to the referee's exercise of jurisdiction, but also from the bifurcated system of procedure itself.[18] Litigating summary proceedings before the bankruptcy referee and litigating plenary proceedings before the district or state courts was cumbersome.[19] Bankruptcy proceedings were

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12. Act of July 1, 1898, § 2, 30 Stat. 544-66 (repealed 1978).

13. *Id.* § 33, 30 Stat. at 573. Referees were re-designated bankruptcy "judges" in 1973. BANK. PROC. R. 901(7).

14. Originally, summary proceedings were limited to those matters related to the administration of the debtor's estate. *See generally* MacLachen, *Scope of the Summary Jurisdiction of the Bankruptcy Court*, 40 COLUM. L. REV. 489 (1940); Reed, Sagar & Granoff, *Subject Matter Jurisdiction, Abstention and Removal Under the New Federal Bankruptcy Law*, 56 AM. BANKR. L.J. 121 (1982). The duties of the bankruptcy referee gradually expanded until Congress enacted the Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2672 (codified as amended in scattered sections of Titles 11 & 28 of the United States Code). For a list of the referee's duties prior to the passage of the Reform Act, see COMMISSION ON THE BANKRUPTCY LAWS OF THE UNITED STATES, REPORT H.R. DOC. NO. 93-137, 93rd Cong., 1st Sess., pt. 1, 88-92 (1973), *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 6005-09 [hereinafter cited as COMMISSION REPORT].

15. Murphy v. John Hufman Co., 211 U.S. 562 (1909).

16. Plenary proceedings included actions brought by the bankruptcy trustee to recover preferences or fraudulent transfers. *See* Reed, Sagar, & Granoff, *supra* note 14, at 124-25 n.6.

17. The district court's jurisdiction over plenary proceedings was concurrent with state courts. 2 COLLIER ON BANKRUPTCY ¶ 23.15 (J. Moore 14th ed. 1978).

18. *See* COMMISSION REPORT, *supra* note 14, at 43-52, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 6005-12; Kennedy, *The Bankruptcy Court Under the New Bankruptcy Law: Its Structure and Jurisdiction*, 55 AM. BANKR. L.J. 63, 85-86 (1981).

19. *See* COMMISSION REPORT, *supra* note 14, at 43-52, *reprinted in* 1978 U.S.

delayed while the district and state courts attempted to adjudicate plenary proceedings on their already overcrowded dockets.[20] This jurisdictional dilemma reached critical proportions when this country's courts experienced an unprecedented rise in bankruptcy petitions.[21]

In response to the jurisdictional crisis created under traditional bankruptcy procedure, Congress enacted the Bankruptcy Reform Act of 1978[22] [Reform Act]. The Reform Act abolished the bifurcated method of adjudication in place under the referee system. Bankruptcy judges, whose jurisdiction remained dependent upon Congress' power under Article I, were granted broad jurisdiction over all proceedings "related to" bankruptcy cases.[23] While the term "related to" was not defined in the Reform Act,[24] it is clear that Congress intended to abolish the distinction between plenary and summary proceedings, placing jurisdiction over both in the bankruptcy judge.[25] Although the Reform Act changed the form of procedure, it did not address the underlying substance of the objections which had created the need for the distinction between summary and plenary proceedings. Congress had simply changed the procedure without addressing the federalism and separation of power problems which were the true cause of the delays. This attempt to place form over substance was not destined to withstand constitutional attack.

The constitutionality of the broad jurisdiction granted bankruptcy courts under the Reform Act was tested in *Northern Pipeline Construction Company v. Marathon Pipeline Company*.[26] The

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CODE CONG. & AD. NEWS 6005-12.

20. The delays associated with the district courts' adjudication of plenary proceedings were exacerbated by the fact that district courts must give priority to criminal cases. Speedy Trial Act, Pub. L. No. 93-619, 88 Stat. 2076 (1975). *See* H.R. REP. No. 595, 95th Cong., 2d Sess. 14, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 5975.

21. Bankruptcy filings increased from 10,000 to over 240,000 in the 30 years preceding enactment of the Reform Act. *Hearings on H.R. 31 and H.R. 32 Before the Subcomm. on Civil and Constitutional Rights of the House Comm. on the Judiciary*, 94th Cong., 1st & 2d Sess., pt. 1 at 37 (1975-76).

22. Pub. L. No. 95-598, 92 Stat. 2672 (amended 1982).

23. 28 U.S.C. § 1471(b) (1982) (amended 1984) (current version to be codified at 28 U.S.C. § 1334(b)). Actually, section 1471(b) of the Reform Act granted "related to" jurisdiction to the district courts, but the bankruptcy judge was given power to exercise all of the district court's jurisdiction in section 1471(c). 28 U.S.C. § 1471(c) (1982) (repealed 1984).

24. For varying formulations of the possible scope of the bankruptcy court's jurisdiction over "related to" cases, see 1 COLLIER ON BANKRUPTCY ¶ 3.01, 3.49 (I. King 15th ed. 1980); Kennedy, *supra* note 18, at 86 n.102; Reed, Sagar & Granoff, *supra* note 14, at 130-35.

25. *See* H.R. REP. No. 595, 95th Cong., 2d Sess. 48-49, *reprinted in* 1978 U.S. CODE CONG. & AD. NEWS 5963, 6010.

26. 458 U.S. 50 (1982).

dispute, which allegedly fell within the bankruptcy court's "related to" jurisdiction, was between parties of diverse citizenship and was based upon purely state law causes of action.[27] In a plurality opinion, a sharply divided United States Supreme Court declared the jurisdictional provisions of the Reform Act unconstitutional.[28] The three separate opinions revealed great disparity among the justices concerning the appropriate scope of bankruptcy court jurisdiction. More importantly, the opinions revealed and relied upon the substance of the jurisdictional objections which Congress had ignored when it enacted the Reform Act.

The plurality opinion in *Northern Pipeline* found that Congress' expansion of the bankruptcy court's jurisdiction over all proceedings "related to" bankruptcy cases violated separation of powers principles.[29] The fact that the bankruptcy courts were established pursuant to Article I, rather than Article III, was decisive. Actions such as Northern's, formerly referred to as plenary proceedings, were reserved for adjudication in Article III court's. The grant of jurisdiction over all "related to" proceedings required the exercise of Article III power which the bankruptcy court could not constitutionally exercise without violating the separation of congressional and judicial power.[30] The dissenting opinion was also based upon separation of powers principles. The dissenters balanced the need to have all proceedings "related to" bankruptcy cases heard in an Article I court against the interest in preserving the values promoted by Article III.[31] In sharp contrast to the plurality, the dissenters concluded that the jurisdictional provisions of the Reform Act did not unconstitutionally infringe upon Article III values.[32]

Unlike the plurality and dissenting opinions, the decisive concurring opinion was based upon federalism principles. The concurring justices concluded that jurisdiction over proceedings based upon purely state law causes of action could not constitutionally be granted to courts established under Article I.[33] The diverse citizenship of the litigants in *Northern Pipeline* could establish federal subject matter jurisdiction in an Article III court, but could not provide the basis for an Article I court's exercise of jurisdiction. The

27. The action was based upon breach of contract, breach of warranty, misrepresentation, coercion and duress. *Id.* at 56.

28. *Id.* at 87.

29. *Id.* at 50-89.

30. *Id.* at 87.

31. *Id.* at 113-18.

32. *Id.*

33. The concurring opinion stated that the causes of action in *Northern Pipeline* were "the stuff of the traditional actions at common law tried by the courts at Westminister in 1789." *Id.* at 90. The concurring justices expressed the federalism concern that no federal rule of decision applied to the issues in the case because the claims arose "entirely under state law." *Id.*

separation of powers principles asserted by the plurality and the federalism principles relied upon by the concurring justices, thus combined to render the jurisdictional provisions of the Reform Act unconstitutional.

The Supreme Court temporarily stayed enforcement of its judgment in *Northern Pipeline* to allow Congress the opportunity to cure the Reform Act's constitutional infirmities.[34] Congress did not, however, respond before the judgment went into effect, necessitating the adoption of an interim rule to govern bankruptcy proceedings. The interim rule only fostered further delay and confusion and it was in response to this new jurisdictional crisis that Congress finally passed the Bankruptcy Amendments.[35]

Congress cured the constitutional infirmities of the Reform Act when it enacted the Bankruptcy Amendments. Its persistent refusal to grant bankruptcy courts Article III status,[36] however, necessitated the creation of a procedural morass which makes even the procedures in place prior to the Reform Act appear routine. Under the Bankruptcy Amendments, all cases "related to" bankruptcy are referred to the bankruptcy court.[37] The bankruptcy judge is empowered to determine whether a controversy is a "core proceeding" or is "otherwise related to" a bankruptcy case.[38] A non-exclusive list of core proceedings is provided which includes controversies which probably would have fallen within the referees jurisdiction over "summary proceedings" prior to the Reform Act.[39] The bankruptcy judge is permitted to enter final judgments and orders in core proceedings.[40] In cases determined to be otherwise related to a bankruptcy case, the bankruptcy judge is limited to the entry of findings of fact and conclusions of law which are subject to *de novo* review in the district court.[41] Providing for district court *de novo* review of

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34. *Id.* at 88.

35. *See* Countryman, *Emergency Rule Compounds Emergency*, 57 AM. BANKR. L.J. 1 (1984).

36. The bankruptcy judges are granted 14 year terms. Bankruptcy Amendments, Pub. L. No. 98-353, § 104(a), 98 Stat. 330, 336 (to be codified at 28 U.S.C. § 152(a)(1)). Their salaries are subject to the Federal Salary Act of 1967, 2 U.S.C. §§ 351-361 (1982). Pub. L. No. 98-353, § 104(a), 98 Stat. 330, 338-39 (to be codified at 28 U.S.C. § 153(a)).

37. Pub. L. No. 98-353, § 104(a), 98 Stat. 330, 340 (to be codified at 28 U.S.C. § 157(a)).

38. *Id.* § 104(a), 98 Stat. 330, 340-41 (to be codified at 28 U.S.C. § 157(b)(3)). The section also provides that a proceeding shall not be determined to be a non-core proceeding "solely on the basis that its resolution may be affected by state law." *Id.*

39. *Id.* § 104(a), 98 Stat. 330, 340 (to be codified at 28 U.S.C. § 157(b)(2)). For a discussion of the scope of the referee's jurisdiction over summary proceedings, see *supra* note 14.

40. Pub. L. No. 98-353, § 104(a), 98 Stat. 330, 340 (to be codified at 28 U.S.C. § 157(b)(1)).

41. *Id.* § 104(a), 98 Stat. at 341 (to be codified at 28 U.S.C. § 157(c)(1)).

cases otherwise related to a bankruptcy case answers the constitutional objection based upon separation of powers principles enunciated in *Northern Pipeline* to the effect that such cases must be heard in an Article III court.[42]

Although the Bankruptcy Amendments cure the separation of powers objection to the procedures established under the Reform Act, they also represent a step backward into the bifurcated procedures[43] which the Reform Act sought to abolish.[44] Cases otherwise related to bankruptcy cases must be reviewed *de novo* in the district court. Bankruptcy proceedings will, therefore, once again be delayed while the district courts attempt to adjudicate these cases on their over-crowded dockets. Litigants will object to the bankruptcy judge's characterization of their controversies as either core proceedings or as proceedings otherwise related to bankruptcy. The procedures established under the Bankruptcy Amendments are essentially the same as those which existed under pre-Reform Act law. The major difference between the two systems is purely semantic. Summary proceedings are now termed core proceedings and plenary proceedings are now referred to as proceedings otherwise related to a bankruptcy case. Congress has, thus, once again, changed the terms which will constitute the form of jurisdictional objections, but has left the substance of the underlying jurisdictional problems unresolved and the delays associated with those problems intact. Delay is certain to result from this return to pre-Reform Act bankruptcy procedures.[45]

Establishing bankruptcy courts pursuant to the judicial power contained in Article III would eleminate the separation of power problems which originally necessitated the bifurcated procedures.[46] Objections based upon the constitutional requirement that certain cases must be heard in an Article III court would disappear because the bankruptcy court would, itself, exercise Article III power. The need for a bifurcated system of adjudication would likewise disappear because the bankruptcy court's jurisdiction would be co-extensive with that of the district courts. Granting bankruptcy courts Article III status would, therefore, reduce theoretical complexity and

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42. *See supra* text accompanying note 30.

43. *See supra* notes 12-17 and accompanying text.

44. *See supra* note 25 and accompanying text.

45. *See* W. NORTON, BANKRUPTCY LAW & PRACTICE (Monograph 1985—No. 1)(author suggests that procedure under Bankruptcy Amendments "may become the most inefficient and time-consuming system to date"). For a more definitive discussion of the bankruptcy procedures employed under the new Act, see generally Kamp, *Court Structure Under the Bankruptcy Code*, 90 COM. L.J. 203 (1985).

46. The suggested House bill would have granted bankruptcy judges Article III status under the Bankruptcy Amendments. H.R. 6978, 97th Cong., 2d Sess., 128 Cong. Rec. H5871 (daily ed. Aug. 12, 1982).

jurisdictional delay.

The Bankruptcy Amendments are not only inadequate in their response to separation of powers problems, but are also subject to objection based upon federalism principles. Under the Bankruptcy Amendments, the district court may hear all "civil proceedings related to" bankruptcy cases.[47] The constitutional scope of the district court's jurisdiction is limited, however, to cases arising under federal law and cases where the parties are of diverse citizenship.[48] Civil proceedings which are related to a bankruptcy case, yet are lacking in some other basis for the exercise of federal subject matter jurisdiction could not be constitutionally heard in the district courts, or in any other federal court, for that matter. A case such as *Northern Pipeline*, for example, would not present any constitutional difficulty because the parties were of diverse citizenship.[49] A case based upon a purely state law cause of action in which diversity did not exist, however, would raise serious constitutional problems. The only basis for a federal court's exercise of jurisdiction over such a case would be the fact that one of the parties to the litigation had filed a bankruptcy petition. It is doubtful that this would be enough to transform the case into one arising under federal law.[50] The jurisdiction granted to district courts may, therefore, exceed the constitutional scope of federal subject matter jurisdiction. The term "related to" could, of course, be interpreted as being co-extensive with the requirements of federal subject matter jurisdiction to save the provision from being declared unconstitutional. This would, however, necessitate defining the term "related to" on a case-by-case basis to determine whether federal subject matter provides the basis for the district court's exercise of jurisdiction.

Granting bankruptcy courts Article III status would obviate the need to determine whether a civil proceeding "related to" a bankruptcy case could constitutionally be heard in a bankruptcy court. The bankruptcy court's jurisdiction would be defined by established law governing federal subject matter jurisdiction and the need to de-

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47. Bankruptcy Amendments, Pub. L. No. 98-353, § 101, 98 Stat. 330, 333 (to be codified at 28 U.S.C. § 1334(b)). The district court may, but is not required to, abstain from hearing cases in the interest of comity or out of respect for state law. *Id.* § 101(a), 98 Stat. 330, 333 (to be codified at 28 U.S.C. § 1334(c)(2)). The new section 1334(b)(2) of Title 28 also addresses the federalism problem but it, too, is not mandatory. It provides that the district court shall abstain from hearing proceedings "with respect to which an action could not have been commenced in a court of the United States . . . *if an action is commenced, and can be timely adjudicated* in a state court of appropriate jurisdiction." *Id.* § 101(a), 98 Stat. 330, 333 (to be codified at 28 U.S.C. § 1334(b)(2)) (emphasis added).

48. *See supra* notes 6 & 7 and accompanying text.

49. *See supra* note 27 and accompanying text.

50. *See* 130 CONG. REC. 8891 (daily ed. June 29, 1984), *reprinted in* 1984 U.S. CODE CONG. & AD. NEWS 590, 595 (statement of Senator Hutch).

fine the term "related to" would disappear. The bankruptcy court's jurisdiction would depend upon whether the case arose under federal law, was between parties of diverse citizenship, or was pendent or ancillary to another case properly before the bankruptcy court. Granting bankruptcy courts Article III status, therefore, would render the bankruptcy court's jurisdiction more certain according to the body of law which has already been developed to define the appropriate scope of federal subject matter jurisdiction.[51]

Any attempt to resolve the jurisdictional problems which have historically plagued bankruptcy proceedings must be evaluated according to the extent to which it addresses the interests of litigants in reducing delays and creating certainty. The Bankruptcy Amendments fail to properly address these interests and thus, are productive of further delays, greater theoretical confusion, and are perhaps unconstitutional. Establishing bankruptcy courts under Article III would not only minimize delays and theoretical confusion, but would also render the existence of the bankruptcy court's jurisdiction more certain. Congress should not await yet another jurisdictional crisis to cure the deficiencies of the present law. Bankruptcy litigants cannot afford to suffer the delays which inevitably accompany congressional attempts to change the form of jurisdictional objections without resolving their substance. Congress should respond to the needs of bankruptcy litigants and finally grant bankruptcy courts Article III status.

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51. *See supra* note 9 and accompanying text.