

1995

# Resolving Still Unresolved Issues of Bankruptcy Law: A Fence or an Ambulance

David G. Epstein

*University of Richmond*, [depstein@richmond.edu](mailto:depstein@richmond.edu)

Follow this and additional works at: <http://scholarship.richmond.edu/law-faculty-publications>



Part of the [Bankruptcy Law Commons](#)

---

## Recommended Citation

David G. Epstein & Paul M. Baiser, *Resolving Still Unresolved Issues of Bankruptcy Law: A Fence or an Ambulance*, 69 Am. Bankr. L.J. 525 (1995).

This Article is brought to you for free and open access by the School of Law at UR Scholarship Repository. It has been accepted for inclusion in Law Faculty Publications by an authorized administrator of UR Scholarship Repository. For more information, please contact [scholarshiprepository@richmond.edu](mailto:scholarshiprepository@richmond.edu).

# Resolving Still Unresolved Issues of Bankruptcy Law: A Fence or An Ambulance

by

*Paul M. Baisier*  
and  
*David G. Epstein\**

Seventeen years after the enactment of the Bankruptcy Reform Act of 1978, many basic questions of substantive bankruptcy law remain unanswered. Stated differently, in the past seventeen years, many basic questions of substantive bankruptcy law have been answered differently by different lower courts. The existing structure for the appeal of bankruptcy decisions is responsible, at least in part, for the lack of clear, settled rules in many basic areas of substantive bankruptcy law.

Congress established a Bankruptcy Review Commission ("Commission") when it enacted the Bankruptcy Reform Act of 1994.<sup>1</sup> Although the Commission is empowered to review the Bankruptcy Code and make recommendations based upon its findings and conclusions, its focus is directed toward making suggestions that do not disturb the fundamental principles and balance of current law.<sup>2</sup> Instead, the stated purposes of the Commission are:

- (1) to investigate and study issues and problems relating to title 11, United States Code (commonly known as the "Bankruptcy Code");
- (2) to evaluate the advisability of proposals and current arrangements with respect to such issues and problems;

---

\*The authors practice in the Bankruptcy and Commercial Litigation Group at King & Spalding, Atlanta, Georgia. The topic addressed in this Article is a continually evolving one. The information contained herein is current as of early October, 1995.

<sup>1</sup>Pub. Law No. 103-394, 108 Stat. 4106 (codified as amended in scattered sections of 11 U.S.C.) [hereinafter the "1994 Amendments"].

<sup>2</sup>H.R. REP. NO. 103-835, 103d Cong., 2d Sess. 59 (1994), reprinted in 1994 U.S.C.C.A.N. 3340, 3368. The section-by-section analysis to the 1994 Amendments indicates that:

The Commission is empowered to review the Bankruptcy Code and to prepare a report based upon its findings and opinions. Although no exclusive list is set forth, the Commission should be aware that Congress is generally satisfied with the basic framework established in the current Bankruptcy Code. Therefore, the work of the Commission should be based upon reviewing, improving, and updating the Code in ways which do not disturb the fundamental tenets and balance of current law.

*Id.*

- (3) to prepare and submit to the Congress, the Chief Justice, and the President a report in accordance with section 608 [of the 1994 Amendments]; and
- (4) to solicit divergent views of all parties concerned with the operation of the bankruptcy system.<sup>3</sup>

The authors urge the Commission to consider the problem presented by the many unsettled basic questions of substantive bankruptcy law and potential solutions to that problem that involve systemic changes to the existing bankruptcy appeals process. The problem, and the possible solutions, are easy to identify and easy to understand. The problem can be seen in any issue of the *West's Bankruptcy Reporter*, and the possible solutions can be found, albeit indirectly, in "A Fence or an Ambulance,"<sup>4</sup> a poem read to third-graders in Temple, Texas in the 1950's.

## I. THE DANGEROUS CLIFF

*TWAS A DANGEROUS CLIFF, as they freely confessed,  
Though to walk near its crest was so pleasant;  
But over its terrible edge there had slipped  
A duke and full many a peasant.  
So the people said something would have to be done,  
But their projects did not at all tally;  
Some said, "Put a fence around the edge of the cliff,"  
Some, "An ambulance down in the valley."<sup>5</sup>*

### A. LACK OF SETTLED RULES

Fifty-two times a year, bankruptcy judges and bankruptcy lawyers receive the green, paperback *West's Bankruptcy Reporter*. Each week it contains forty to fifty new bankruptcy opinions. In the issues of *West's Bankruptcy Reporter* (and in the other unofficial bankruptcy case reporting services), a resourceful lawyer can easily find persuasive precedent on either side of virtually every issue that arises in a bankruptcy case.

That same resourceful lawyer will also find in *West's Bankruptcy Reporter* short articles that list conflicting decisions on basic bankruptcy law issues. For example, the July 5, 1995, issue of *West's Bankruptcy Reporter* includes a two-page article addressing whether a Chapter 11 debtor may propose a plan of reorganization which classifies an undersecured secured creditor's unsecured deficiency claim separately from other general unsecured claims.<sup>6</sup> The classifi-

<sup>3</sup>Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 603, 108 Stat. 4106, 4147.

<sup>4</sup>JOSEPH MALINS, *THE RECITER* 273 (1895), reprinted in HAZEL FELLEMAN, *BEST LOVED POEMS OF THE AMERICAN PEOPLE* 273 (1936). This poem was not read to third graders in Rochester, Illinois in the 1970's.

<sup>5</sup>*Id.*

<sup>6</sup>*West's Bankruptcy Newsletter*, at 2, 162 B.R., no. 27.

cation issue is a basic one that arises in virtually every Chapter 11 case in which real estate is a significant asset.<sup>7</sup> The article lists the seven bankruptcy court decisions, one district court decision, and one court of appeals decision since 1993 that have either allowed or required separate classification of a secured creditor's unsecured deficiency claim, and five bankruptcy court decisions, one district court decision, five court of appeals decisions, and two bankruptcy appellate panel decisions since 1991 that have prohibited the separate classification of such a deficiency claim. In other words, seventeen years after the enactment of the Bankruptcy Reform Act of 1978, there is substantial support in the decided case law for either position, and six of eleven judicial circuits have no binding precedent on this most basic question of substantive bankruptcy law.<sup>8</sup>

This conflict and lack of direction in the reported case law has considerable practical impact. Attorneys representing both debtors and creditors in the six circuits without binding precedent (and with significant authority on both sides) can and do litigate the same basic issue again and again and again.<sup>9</sup>

---

<sup>7</sup>In a typical bankruptcy case where one of the assets of the estate is an improved piece of commercial real estate, financed to a substantial extent by a lender, the value of the real estate and the nature and extent of the resulting claims of the lender are invariably at issue. If the property has a value less than the amount of the associated loan (as it often does), the lender has a secured claim for the value of the property and an unsecured claim for the balance. 11 U.S.C. § 506(a) (1994). Often, the unsecured claim of the lender is large and will dominate the class of general unsecured creditors for voting purposes, see *id.* § 1126, if it is included therein. Such domination of the unsecured creditor class would provide the lender with substantial leverage in the bankruptcy case, particularly where the debtor would otherwise rely on the unsecured creditor class to provide it with its needed accepting impaired class, see *id.* § 1129(a)(10). To avoid allowing the lender to have that leverage, the debtor often attempts to put the lender's unsecured deficiency claim in a separate class. This creates interpretive problems with the classification requirements, see *id.* § 1122. Whether such a classification is permissible has divided the courts. Compare, e.g., *In re Woodbrook Assocs.*, 19 F.3d 312 (7th Cir. 1994), with *RTC v. Swedeland Dev. Group, Inc. (In re Swedeland Dev. Group, Inc.)*, 16 F.3d 552 (3d Cir. 1994). See generally Bruce A. Markell, *Clueless on Classification: Toward Removing Artificial Limits on Chapter 11 Claim Classification*, 11 BANKR. DEV. J. 1 (1994-95); Scott F. Norberg, *Classification of Claims Under Chapter 11 of the Bankruptcy Code: The Fallacy of Interest Based Classification*, 69 AM. BANKR. L.J. 119 (1995).

<sup>8</sup>Two of the five courts of appeals decisions allowing separate classification are from the Third Circuit; hence there are six circuits without binding precedent, rather than five.

<sup>9</sup>This is only one of numerous questions that lawyers can and do litigate again and again. Currently, lawyers are litigating and relitigating questions such as: if § 553 mutuality exists for claims by and against different government agencies, compare *Westamerica Bank v. United States*, 178 B.R. 493 (Bankr. N.D. Cal. 1995) (no mutuality), with *United States v. Reed (In re Reed)*, 179 B.R. 353 (Bankr. S.D. Ga. 1995) (mutuality); whether Chapter 12 debtors can avoid trustee's fees by making direct payments to creditors, compare *Michael v. Beard (In re Beard)*, 45 F.3d 113 (6th Cir. 1995); *Wagner v. Armstrong (In re Wagner)*, 36 F.3d (8th Cir. 1994); *In re Cross*, 182 B.R. 42 (D. Neb. 1995) (permitted), with *Dunivent v. Schollett (In re Schollett)*, 980 F.2d 639 (10th Cir. 1992); *Fulkrod v. Anabele Savage (In re Fulkrod)*, 973 F.2d 801 (9th Cir. 1992); *In re C.A. Jackson Ranch Co.*, 181 B.R. 552 (Bankr. E.D. Okla. 1995) (prohibited); see generally George H. Singer, *Zeroing Out the Standing Trustee's Percentage Fee: The Eighth Circuit Approves "Outside the Plan" Payments for Chapter 12 Debtors*, 11 NORTON BANKR. L. ADVISER 7 (Nov. 1994) (for a comprehensive analysis of the issue); and when lease rejection is effective, compare *In re Thinking Machs. Corp.*, 67 F.3d 1021 (1st Cir. 1995); *In re 1 Potato 2, Inc.*, 182 B.R. 540 (Bankr. D. Minn. 1995) (on court approval), with *In re 1 Potato 2, Inc.*, 58 B.R. 752 (Bankr. D. Minn. 1986) (on filing of motion to reject).

By contrast, if a debtor's attorney knew that an unsecured deficiency claim could not be classified separately from the debtor's other general unsecured claims, counsel might well advise the debtor to negotiate a consensual resolution with the secured creditor rather than to file for bankruptcy and litigate. Similarly, if the attorney representing the secured creditor knew that a debtor could classify a secured creditor's unsecured deficiency claim separately from its other general unsecured claims, counsel would likely advise his or her client to negotiate a consensual resolution with the potential debtor rather than push that potential debtor into bankruptcy. With the existing uncertainty, each side believes that it might prevail, and litigation, rather than meaningful business negotiation, is often the chosen course of action.

As is evident, both debtors and creditors would benefit from the definitive resolution of basic legal issues and the conclusive establishment of legally binding rules. The relitigation of basic questions of substantive bankruptcy law is grossly inefficient and compounds the expense and delay inherent in the bankruptcy process. In one of the many decisions on the separate classification of unsecured deficiency claims issue, *Life Insurance Co. v. Barakat (In re Barakat)*,<sup>10</sup> United States Bankruptcy Judge Geraldine Mund acknowledges that "wide gaps exist in the areas of settled law"<sup>11</sup> which create "an inefficient and ineffective situation."<sup>12</sup> Judge Mund attributes that situation to the present bankruptcy appellate process.<sup>13</sup> The authors agree.

## B. BANKRUPTCY APPEALS PROCESS

The initial appeal of a decision by a bankruptcy court can be made either to an Article III district court or an Article I bankruptcy appellate panel,<sup>14</sup> provided that the circuit in which the appeal arises has established a bankruptcy appellate panel. To date, only the Ninth Circuit has established and retained<sup>15</sup> a bankruptcy appellate panel.<sup>16</sup>

### 1. District Court Appeals

Outside of the Ninth Circuit, bankruptcy appeals have to date been routed exclusively to the district courts. There are 94 district courts and approxi-

---

<sup>10</sup>173 B.R. 672 (Bankr. C.D. Cal. 1994).

<sup>11</sup>*Id.* at 680.

<sup>12</sup>*Id.*

<sup>13</sup>*Id.*

<sup>14</sup>28 U.S.C. § 158 (1994). The bankruptcy appellate process is based in the Article I status of bankruptcy courts. The problems with the bankruptcy appellate process have the same basis. See generally Frank R. Kennedy, *The Bankruptcy Court and Its Jurisdiction*, NORTON ANNUAL SURVEY OF BANKR. L. 485 (1995). Nevertheless, on September 19, 1995, the Judicial Conference of the United States "deleted from its Proposed Long Range Plan for the Federal Courts a recommendation that Article III status for bankruptcy courts be considered." *BNL Bankruptcy Law Daily*, September 29, 1995. See *infra* notes 39-54 and accompanying text (for a discussion of the Proposed Long Range Plan).

<sup>15</sup>The First Circuit had a Bankruptcy Appellate Panel. It was dissolved in 1984.

<sup>16</sup>As discussed in greater detail *infra* notes 20-22 and accompanying text, Congress called for the other courts of appeals to consider establishing a bankruptcy appellate panel in § 104 of the 1994 Amendments.

mately 650 district judges. None of the district judges is bound by a bankruptcy appeals decision of a district judge from one of the other 93 district courts.<sup>17</sup> For example, a district judge in the Northern District of Georgia is not bound by the bankruptcy appeals decisions of a district judge in the Southern District of New York, or by a bankruptcy appeals decision of a district judge in the Southern District of Georgia. Further, district judges in multi-judge districts are not even bound by the bankruptcy appeals decisions of other judges from that same district.<sup>18</sup> Indeed, there are reported cases holding that a bankruptcy judge is not even bound by the bankruptcy appeals decision of one of the district judges in his or her own district, if that district is a multi-judge district.<sup>19</sup> The number of district courts and the number of district judges, combined with the lack of precedential effect generally given to the decision of one district judge in the subsequent decisions of district judges (and bankruptcy judges), significantly limits the precedential effect of the bankruptcy appeals decisions of any of the district judges.

## 2. Bankruptcy Appellate Panel Appeals

In the Ninth Circuit, the appeal of a bankruptcy court decision may be had before either a district court or a bankruptcy appellate panel. The Ninth Circuit has had a bankruptcy appellate panel since 1979.<sup>20</sup> In the 1994 Amendments, Congress required the other circuits to establish a bankruptcy appellate panel, absent a finding by the judicial council for that circuit that either (i) there are insufficient bankruptcy judges in the circuit to do so, or (ii) the establishment of a bankruptcy appellate panel would result in undue delay or increased costs.<sup>21</sup> There is no statutory deadline for the other circuits to establish a bankruptcy

<sup>17</sup>See generally Note, *Bankruptcy Courts and Stare Decisis: The Need for Restructuring*, 27 MICH. J. L. REF. 313 (1994); 1B JAMES W. MOORE ET AL., MOORE'S FEDERAL PRACTICE ¶ 402[1], at I-14 & n. 20 (2d ed. 1995) ("The district courts, like courts of appeals, owe no obedience to the decisions of their counterparts in other districts . . .").

<sup>18</sup>*Compare* *Gumport v. Growth Fin. Corp.*, 121 B.R. 837, 839 (C.D. Cal. 1990), with *Miller v. Baron (In re Great Am. Mfg. & Sales, Inc.)*, 129 B.R. 633, 635 (C.D. Cal. 1990).

<sup>19</sup>E.g., *In re Shattuc Cable Corp.*, 138 B.R. 557, 565 (Bankr. N.D. Ill. 1992); *First of Am. Bank v. Gaylor (In re Gaylor)*, 123 B.R. 236, 241 (Bankr. E.D. Mich. 1991). For an in-depth and thoughtful look at precedential value and bankruptcy appeals, including cases in which bankruptcy judges have refused to follow the prior decisions of district judges in their district, see Daniel J. Bussel, *Power, Authority, and Precedent in Interpreting the Bankruptcy Code*, 41 UCLA L. REV. 1063 (1994).

<sup>20</sup>See generally Gordon Bermant & Judy B. Sloan, *Bankruptcy Appellate Panels: The Ninth Circuit's Experience*, 21 ARIZ. ST. L.J. 181 (1989).

<sup>21</sup>Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 104(c), 108 Stat. 4109-10 (amending 28 U.S.C. § 158). Section 28 U.S.C. § 158 provides in part:

(b)(1) The judicial council of a circuit shall establish a bankruptcy appellate panel service composed of bankruptcy judges of the districts in the circuit who are appointed by the judicial council . . . , to hear and determine, with the consent of all the parties, appeals . . . unless the judicial council finds that—

(A) there are insufficient judicial resources available in the circuit; or

(B) establishment of such service would result in undue delay or increased cost to parties in cases under title 11.

appellate panel or to find that they are unable to do so. None of the other circuits has yet taken any definitive action on whether or when to establish a bankruptcy appellate panel in their circuit.<sup>22</sup>

---

Not later than 90 days after making the finding, the judicial council shall submit to the Judicial Conference of the United States a report containing the factual basis of such finding.

(2)(A) A judicial council may reconsider, at any time, the finding described in paragraph (1).

....

(3) Bankruptcy judges appointed under paragraph (1) shall be appointed and be reappointed under such paragraph.

(4) If authorized by the Judicial Conference of the United States, the judicial councils of 2 or more circuits may establish a joint bankruptcy appellate panel comprised of bankruptcy judges from the districts within the circuits for which such panel is established, to hear and determine, upon the consent of all the parties, appeals under subsection (a) of this section.

(5) An appeal to be heard under this subsection shall be heard by a panel of 3 members of the bankruptcy appellate panel service, except that a member of such service may not hear an appeal originating in the district for which such member is appointed or designated under section 152 of this title.

(6) Appeals may not be heard under this subsection by a panel of the bankruptcy appellate panel service unless the district judges for the district in which the appeals occur, by majority vote, have authorized such service to hear and determine appeals originating in such district.

(c)(1) Subject to subsection (b), each appeal . . . shall be heard by a 3-judge panel of the bankruptcy appellate panel service established under subsection (b)(1) unless—

(A) the appellant elects at the time of filing the appeal; or

(B) any other party elects, not later than 30 days after service of notice of the appeal; to have such appeal heard by the district court.

....

28 U.S.C. § 158 (1994). See FED. R. BANKR. P. 8001(e).

<sup>22</sup>It has been reported that:

Almost half of the judicial districts may soon establish bankruptcy appellate panels pursuant to the 1994 Bankruptcy Reform Act, according to a poll taken by Chief Bankruptcy Judge David A. Scholl of the Eastern District of Pennsylvania. The act authorizes each circuit to establish a BAP unless there are insufficient judicial resources in the circuit or establishing the panel would result in undue delay or increased costs to parties. Scholl spoke at a seminar session on "Major Changes in the New Bankruptcy Act." Scholl reported that the First Circuit is "chugging ahead" with plans to establish a BAP, but it needs money. The Second Circuit apparently intends to implement a BAP only for the District of Connecticut, Scholl said, noting that the legislation permits judicial districts to opt out of the panel. The Third Circuit will meet soon to decide the issue; it appears that New Jersey is the only district interested in having a BAP, so the circuit may create a BAP only to hear New Jersey appeals, Scholl said. The Fourth Circuit has not decided whether to create a BAP, and the Fifth, Seventh, and Eleventh Circuits are considered unlikely to do so, Scholl continued. The Sixth and Eighth Circuits are "likely" to implement BAPs, and the Tenth Circuit may do so with Colorado opting out. There is only one bankruptcy judge in the D.C. Circuit, Scholl noted.

*BNA Bankruptcy Law Daily*, September 27, 1995. On October 18, 1995, the Circuit Council for the Eighth Circuit voted 9-3 to establish a bankruptcy appellate panel. The establishment of a BAP in the Eighth Circuit is, however, subject to the availability of funding.

Whatever arguments can be made in support of the creation of a bankruptcy appellate panel, the development of binding precedent is not one of them. Looking to the experience of the Ninth Circuit, the precedential effect of a decision of a bankruptcy appellate panel is problematic for at least the following reasons:

1. The Ninth Circuit has held that the decisions of its bankruptcy appellate panel are not binding on the district courts in the Ninth Circuit because Article III district court judges cannot constitutionally be bound by the decisions of the Article I bankruptcy court judges who sit on a bankruptcy appellate panel under 28 U.S.C. § 158(b);<sup>23</sup>
2. Since a bankruptcy appellate panel sits in lieu of a district court, its opinions may only have *stare decisis* effect within the district from which the appeal was taken;
3. If, as suggested above, district court opinions do not bind the bankruptcy courts sitting in the same district, then the opinions of the bankruptcy appellate panel (which sits in lieu of the district court) cannot bind those same bankruptcy courts, and thus bind no one; and
4. A bankruptcy appellate panel may not have the power to set precedent at all because it is an Article I court and, as such, has authority only to the extent that the parties consent to be bound by it.<sup>24</sup>

In sum, it is arguable that the result of an appeal from the bankruptcy court to a district court is an opinion that is binding precedent only on parties to the appeal and on future parties that draw *that same district judge* for the appeal of the same issue. Even stronger arguments can be made against any *stare decisis* effect at all for the opinion of a bankruptcy appellate panel.

### 3. Appeals to the Court of Appeals

If the opinion of the district court or bankruptcy appellate panel is a "final order,"<sup>25</sup> is not "moot,"<sup>26</sup> and if the parties have sufficient funds and time, fur-

---

<sup>23</sup>See *Bank of Maui v. Estate Analysis, Inc.*, 908 F.2d 470 (9th Cir. 1990). See generally Evan H. Camiker, *Why Must Inferior Courts Obey Superior Court Precedent*, 46 STAN. L. REV. 817 (1994); Honorable Kathleen P. March & Rigoberto Obregon, *Are BAP Decisions Binding on Any Court?*, 18 CAL. BANKR. J. 189 (1990); Rigoberto V. Obregon, *In re Globe Illumination: A Provocative But Flawed Theory on the Precedential Value of BAP Authority*, 21 CAL. BANKR. J. 45 (1983).

<sup>24</sup>See, e.g., 28 U.S.C. § 158(c) (1994) (allowing parties to the appeal to opt out of having an appeal heard by a bankruptcy appellate panel). See *supra* note 21.

<sup>25</sup>For discussion and criticism of the "final order" requirement, see STEPHEN E. SNYDER & LAWRENCE PONOROFF, *COMMERCIAL BANKRUPTCY LITIGATION* § 4.01 (1989); Richard B. Levin, *Bankruptcy Appeals*, 58 N.C. L. REV. 968, 982-92 (1980).

<sup>26</sup>See Bussell, *supra* note 19, at 1070 (for a discussion of the problems presented by the mootness doctrine in the context of bankruptcy).

ther appeal to the court of appeals can be had.<sup>27</sup> The statutory requirement of a final order and the bar of mootness, coupled with the practical requirements of time and money, significantly limit the number of bankruptcy court decisions subjected to a second-tier appeal to a court of appeals. A 1993 Federal Judicial Center study estimates that less than one out of every five bankruptcy appeals to the district court ultimately reaches a court of appeals.<sup>28</sup>

The time required to complete an appeal to a district court or bankruptcy appellate panel and then to a court of appeals is especially troublesome in the instance of a bankruptcy court decision that has broad commercial effect. For example, the bankruptcy court decisions in *Twist Cap, Inc. v. Southeast Bank (In re Twist Cap)*<sup>29</sup> and *Prime Motor Inns, Inc. v. First Fidelity Bank (In re Prime Motors Inns, Inc.)*,<sup>30</sup> which restrained the post-bankruptcy collection on letters of credit, affected the issuance of the billions of dollars of credit backed by letters of credit. Similarly, the decision in *In re Standard Brands Paint Company*,<sup>31</sup> which lowered the threshold for substantive consolidation and allowed such consolidation upon consent of the "major parties," impacted substantive consolidation opinions in transactions aggregating billions of dollars. More recently, the bankruptcy court opinion in *In re Harborview Development 1986 Limited Partnership*,<sup>32</sup> which held, in effect, that the right to possession was the only right protected under 11 U.S.C. § 365(h), was undoubtedly considered by lenders in deciding whether to engage in commercial real estate financings secured by ground leases.

## II. THE AMBULANCE

*But the cry for the ambulance carried the day,  
For it spread through the neighboring city;  
A fence may be useful or not, it is true,  
But each heart became brimful of pity  
For those who slipped over that dangerous cliff;  
And the dwellers in highway and alley  
Gave pounds or gave pence, not to put up a fence,  
But an ambulance down in the valley.*

*"For the cliff is all right, if you're careful," they said,  
"And, if folks even slip and are dropping,  
It isn't the slipping that hurts them so much,*

---

<sup>27</sup>28 U.S.C. § 158(d) (1994). Section 158(d) provides that: "The courts of appeals shall have jurisdiction of appeals from all final decisions, judgments, orders, and decrees . . ." *Id.*

<sup>28</sup>Fletcher Magnum, Memorandum to *The Long Range Planning Committee of The Federal Judicial Center* 19 (December 23, 1993).

<sup>29</sup>1 B.R. 284 (Bankr. M.D. Fla. 1979).

<sup>30</sup>123 B.R. 104 (Bankr. S.D. Fla. 1990).

<sup>31</sup>154 B.R. 563 (Bankr. C.D. Cal. 1993).

<sup>32</sup>152 B.R. 897 (D.S.C. 1993).

*As the shock down below when they're stopping,"  
So day after day, as these mishaps occurred,  
Quick forth would these rescuers sally  
To pick up the victims who fell off the cliff,  
With their ambulance down in the valley.*<sup>33</sup>

To date, the primary solution to the problem of unresolved issues of basic substantive bankruptcy law has been congressional legislation. The 1994 Amendments "fixed" the problem that the bankruptcy court opinion in *Harborview* created for the commercial real estate market by legislatively overruling the *Harborview* decision.<sup>34</sup> Several of the other provisions of the 1994 Amendments address problems presented by a bankruptcy court opinion or resolve a conflict in the opinions of various bankruptcy and other courts.<sup>35</sup>

Congress, with the assistance of the Bankruptcy Review Commission, can continue to serve as the "ambulance down in the valley."<sup>36</sup> The Commission

<sup>33</sup>MALINS, *supra* note 4.

<sup>34</sup>Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 205, 108 Stat. 4106, 4122-23 (amending 11 U.S.C. § 365). The amendments to 11 U.S.C. § 365(h) allow the lessee to retain its rights not only to possession but to timing and amount of rent payments, to quiet enjoyment, to subletting, to assignment and to hypothecation. See Thomas C. Homburger, Brian P. Gallagher & Kimberly K. Rubel, *Conflict Resolved: Bankruptcy Code Section 365(h) and the Contradictory Cases Requiring its Amendment*, 29 REAL PROP. & PROB. TR. J. 869 (1995).

<sup>35</sup>Examples of provisions in the 1994 Amendments which address problems resulting from an unresolved conflict in the case law, or from "mistaken" decisions, include: § 110 (whether expenses of creditors' committee members are reimbursable, see, e.g., Pullima, Yates & Brewster, *Reimbursement of Creditors' Committee Members' Costs and Expenses Under Section 503(b)*, 94 COM. L.J. 93 (1989)); § 112 (whether bankruptcy judges can conduct jury trials, compare *In re United Missouri Bank*, 901 F.2d 1449 (8th Cir. 1990) (no), with *Ben Cooper, Inc. v. Insurance Co. (In re Ben Cooper, Inc.)*, 896 F.2d 1394 (2d Cir. 1990) (yes)); § 214 (whether a creditor has an interest in postpetition rents, see 4 COLLIER ON BANKRUPTCY ¶ 552.03, at 552-17 n.9 (Lawrence P. King et al. eds., 15th ed. 1995) (outlining the conflicting views)); § 216 (whether the statute of limitations on avoidance actions runs from the filing of the case or the subsequent appointment of a trustee, see 4 COLLIER ON BANKRUPTCY ¶ 546.02, at 546-14 n.9 (Lawrence P. King et al. eds., 15th ed. 1995) (outlining the conflicting views)); § 401 (whether postpetition real property tax liens may fix notwithstanding the automatic stay, see *Makoroff v. City of Lockport*, 916 F.2d 890 (3d Cir. 1990), *cert. denied*, 499 U.S. 983 (1991); *Lincoln Sav. Bank v. Suffolk County Treasurer (In re Parr Meadows Racing Ass'n, Inc.)*, 880 F.2d 1540 (2d Cir.), *cert. denied*, 493 U.S. 1058 (1990)); and § 402 (whether municipalities may file for Chapter 9 bankruptcy without express state authorization, compare *In re City of Bridgeport*, 128 B.R. 688 (Bank. D. Conn. 1991), with *In re Carroll Township Auth.*, 119 B.R.61 (Bank. W.D. Pa. 1990)).

<sup>36</sup>Arguably, the Supreme Court is also serving as "the ambulance down in the valley." To the extent that it is, that ambulance does not appear to be picking up the most needy victims in the valley. See generally Robert K. Rasmussen, *A Study of the Cost and Benefits of Textualism: The Supreme Court's Bankruptcy Cases*, 71 WASH. U. L.Q. 535 (1993). For example, the Supreme Court has refused to review at least one case regarding the separate classification of an undersecured creditor's unsecured deficiency claim, despite its obvious importance and the split in the circuits. See, e.g., *Phoenix Mut. Life Ins. Co. v. Greystone III Joint Venture (In re Greystone III Joint Venture)*, 995 F.2d 1274 (5th Cir. 1991), *cert. denied*, 113 S. Ct. 72 (1992). See also *supra* note 7. The High Court also took under review, but then declined to decide after the parties had reached a settlement, a case that would have decided the crucial issue of whether a debtor can retain its interests while not paying senior creditors in full by contributing "new value." See *Bonner Mall Partnership v. U.S. Bancorp Mortgage Co. (In re Bonner Mall Partnership)*, 2 F.3d 899 (9th Cir. 1993), *cert. granted*, 114 S. Ct. 681, *motion to vacate denied & dismissed as moot* by 115 S. Ct. 386 (1994).

can propose and Congress can enact specific answers to basic substantive bankruptcy law questions not yet definitively answered by the courts of appeals, or for which the definitive answers provided by the courts of appeals and the lower courts have conflicted. Indeed, the legislative history seems to suggest that Congress envisioned such a role for the Bankruptcy Review Commission.<sup>37</sup> It has been the experience of the authors, however, that although Congress makes interstitial changes to the bankruptcy laws fairly often, it does not do so very well, often creating more new issues than solving old ones.

### III. THE FENCE

*To rescue the fallen is good, but "tis best  
To prevent other people from falling."  
Better close up the source of temptation and crime  
Than deliver from dungeon or galley;  
Better put a strong fence round the top of the cliff  
Than an ambulance down in the valley.*<sup>38</sup>

The authors argue that the Bankruptcy Review Commission should address the bankruptcy appeals process and propose institutional reforms to that process so that appeals from the decisions of the bankruptcy court result in the prompt and certain resolution of basic substantive bankruptcy law issues. The Committee on Long Range Planning for the Judicial Conference of the United States (the "Judicial Conference Committee") has made a similar recommendation.<sup>39</sup>

#### A. JUDICIAL CONFERENCE COMMITTEE RECOMMENDATIONS

##### 1. *Current Call for Further Study*

The Judicial Conference Committee's Proposed Long Range Plan for the Federal Courts (the "Judicial Conference Plan"), submitted to the Judicial Conference of the United States by the Judicial Conference Committee on March 15, 1995, acknowledges that the Bankruptcy Review Commission was created to study bankruptcy law and states that "examination of both existing and possible alternative mechanisms for appellate review of bankruptcy judges' orders would be a logical part of that study."<sup>40</sup> The Judicial Conference Committee is making its own study of appellate review of bankruptcy judges' orders.<sup>41</sup>

---

<sup>37</sup>See *supra* note 2. "The Blue Ribbon bankruptcy Commission established by this bill will evaluate the Code's deficiencies substantively and operationally, and make a recommendation to Congress for legislative change." 40 CONG. REC. S14,461 (daily ed. Oct. 6, 1994) (statement of Sen. Grassley).

<sup>38</sup>MALINS, *supra* note 4.

<sup>39</sup>*Proposed Long Range Plan for the Federal Courts*, March, 1995, Committee on Long Range Planning, Judicial Conference of the United States, p. 46.

<sup>40</sup>*Id.*

<sup>41</sup>*Id.* at 45.

## 2. *Prior Call for Substantial Reduction in Bankruptcy Appeals to Courts of Appeals*

A November 1994, draft of the Judicial Conference Plan proposed, in Recommendation 20, that appeals from final orders of a bankruptcy court "continue to be reviewed by Article III district judges," with any further appeal to be discretionary with the court of appeals.<sup>42</sup> Recommendation 20 appeared to have been based, at least in part, on unpublished Federal Judicial Center data compiled in 1993 that compares the duration of the pendency of bankruptcy appeals. As the text accompanying Recommendation 20 noted, "appeals were handled more expeditiously in the district courts than in the courts of appeals: an average of 145 days in the district court versus 245 days in the court of appeals."<sup>43</sup>

It is, of course, desirable to provide an expeditious resolution of the case at hand, particularly for the parties to the appeal. However, the average time required to complete an appeal is not the only relevant criteria for assessing the time-effectiveness of an appellate process. An appellate court's creation of binding precedent can result in the expeditious resolution of hundreds of cases. Adoption of Recommendation 20 would have produced the benefit of the faster end of one case at the high cost of the lack of binding precedent that might produce a substantially faster end to hundreds of cases.

Recommendation 20 also seemed to be inconsistent with Recommendation 19 in the 1994 Judicial Conference Plan, which called for an appeal of the decisions of Article I courts "ordinarily" directly to the courts of appeals.<sup>44</sup> Further, Recommendation 20 did not seem to take into account Recommendation 21 in the 1994 Judicial Conference Plan, which provided that appeals from the civil decisions of federal magistrate judges should be only to a court of appeals, because an appeal to a district court from a federal magistrate judge's decision "tends to undermine the perception of magistrate judges as fully capable judicial officers to whom the district court entrusts adjudicative functions."<sup>45</sup> Nowhere in Recommendation 20 or the text supporting Recommendation 20 is it explained why an appeal from a bankruptcy judge's decision to a district court does not similarly "tend to undermine the perception" of bankruptcy judges as "fully capable judicial officers."

Recommendation 20, which called for review by "Article III judges in the district court," also did not seem to take into account the then recently-passed 1994 Amendments, which provide for the formation of bankruptcy appellate

---

<sup>42</sup>*Proposed Long Range Plan for the Federal Courts*, November, 1994, Committee on Long Range Planning, Judicial Conference of the United States (Draft for Public Comment) [hereinafter the "1994 Judicial Conference Plan"], p. 38.

<sup>43</sup>*Id.*

<sup>44</sup>*Id.* at 37.

<sup>45</sup>*Id.* at 38-39.

panels in every circuit.<sup>46</sup> If bankruptcy appellate panels are adopted in the various circuits, appellate review will not be "by Article III judges," as required by Recommendation 20.<sup>47</sup>

### 3. *Change in Course*

After public hearings in Phoenix, Arizona; Washington, D.C.; and Chicago, Illinois, testimony regarding Recommendation 20 from Gerald Smith,<sup>48</sup> United States Bankruptcy Judge Louise D. Adler, Professor Lawrence P. King,<sup>49</sup> Robert B. Millner,<sup>50</sup> Nathan B. Feinstein,<sup>51</sup> and Robin Phelan,<sup>52</sup> and written submissions from those testifying, as well as from other bankruptcy judges and lawyers, the Judicial Conference Committee significantly changed its position on bankruptcy appeals. The Judicial Conference Committee replaced the recommendations in the 1994 Judicial Conference Plan with the following Recommendations regarding the bankruptcy appeals process in the Judicial Conference Plan:

Recommendation 22: The existing mechanism for review of dispositive orders of bankruptcy judges should be studied to determine what appellate structure will ensure prompt, inexpensive resolution of bankruptcy cases and foster coherent, consistent development of bankruptcy precedents.

Recommendation 23: Pending completion of the study of bankruptcy appellate structure recommended above, the dispositive orders of bankruptcy judges should be reviewable directly in the court of appeals in those cases where the parties stipulate,<sup>53</sup>

---

<sup>46</sup>See Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 104, 108 Stat. 4106, 4109-10 (amending 28 U.S.C. § 158). See also *supra* note 21.

<sup>47</sup>Because the bankruptcy appellate panel judges are Article I judges, appellate review of bankruptcy judges' decisions by a bankruptcy appellate panel is inconsistent not only with the language of Recommendation 20, but also with the statement regarding the 1994 Amendments by Senator Howell Heflin in the October 6, 1994, Congressional Record: "It should be recognized that the creation of a bankruptcy appellate panel service can help to establish a dependable body of case law." 140 CONG. REC. S14,463 (daily ed. Oct. 6, 1994). As long as bankruptcy judges are Article I judges, with the limitations inherent therein, an appellate court of bankruptcy judges like the bankruptcy appellate panels is not going to be able to "help to establish a dependable body of case law."

<sup>48</sup>Member, Advisory Committee on Bankruptcy Rules; Member, Business Bankruptcy Committee, Business Law Section, American Bar Association; Former Deputy Director of the Staff of the Commission on Bankruptcy Laws.

<sup>49</sup>Vice Chair, National Bankruptcy Conference; Charles Seligson Professor of Law, New York University School of Law.

<sup>50</sup>Vice Chair, American Bar Association Joint Task Force on Bankruptcy Court Structure and Insolvency Process.

<sup>51</sup>Chair, American Bar Association Joint Task Force on Bankruptcy Court Structure and Insolvency Process.

<sup>52</sup>President, American Bankruptcy Institute.

<sup>53</sup>The Committee of Bankruptcy Administration of the Judicial Conference had removed the provision contained in Recommendation 23 that allowed appeal "upon the consent of the parties" and the Judicial Conference approved the revised version at its meeting on September 19, 1995.

or the district court or bankruptcy appellate panel (BAP) certifies, that such review is needed immediately to establish legal principles on which subsequent proceedings in the case may depend.<sup>54</sup>

#### B. RECOMMENDATIONS OF APPEAL TO ARTICLE III JUDGE PANEL

Presently, in three separate articles, a distinguished professor of bankruptcy law, a nationally respected bankruptcy practitioner, and a United States Bankruptcy Judge have also publicly recommended changes to the appeals process. Professor Daniel J. Bussel, Professor of Law, U.C.L.A. Law School, Nathan B. Feinstein of the firm of Piper & Marbury, and United States Bankruptcy Judge Steven W. Rhodes, each suggests that bankruptcy appeals should go directly to a three-judge panel of an Article III appellate court.<sup>55</sup> For the reasons outlined below, the authors support that suggestion and urge both the Judicial Conference Committee and the Bankruptcy Review Commission to support it as well.

It can be argued that the present, two-tiered system of bankruptcy appeals performs adequately, if slowly, the "error correction" appellate function. But, as the current version of the Judicial Conference Plan notes, "error correction" is only one of the functions of the federal appellate process:

United States courts of appeals perform two primary functions, often described in shorthand as "error correction" and "law declaration." Review for error entails determining whether the first-level decision-maker applied the correct law to the facts of the case, and whether procedural error occurred that fatally tainted the process. Law declaration is the articulation of a rule of law; it serves to guide prospective behavior, control future cases, and ensure that all cases receive the same treatment.<sup>56</sup>

As outlined above, the present bankruptcy appeals system does not perform adequately the "law declaration" function. That function is an especially important one in bankruptcy. Bankruptcy courts are this country's most significant

---

<sup>54</sup>*Proposed Long Range Plan for the Federal Courts*, September, 1995, Committee on Long Range Planning, Judicial Conference of the United States, p. 8. These Recommendations were adopted by the American Bar Association by resolution on August 8, 1995. 3 BANKRUPTCY LITIGATION NEWSLETTER 35 (Summer 1995). The ABA resolution also stated that, as part of the interim solution, legislation should be enacted that "make[s] decisions of each bankruptcy appellate panel binding upon all bankruptcy courts in its circuit, except where contrary district court authority already exists." *Id.*

<sup>55</sup>Daniel J. Bussel, *Bankruptcy Appellate Reform: Issues and Opinions*, NORTON ANNUAL SURVEY OF BANKR. L. 257 (1995-96); Nathan B. Feinstein, *The Bankruptcy System: Proposal to Restructure the Bankruptcy Court and Bankruptcy Appellate Processes*, NORTON ANNUAL SURVEY OF BANKR. L. 517 (1995-96); Honorable Steven W. Rhodes, *Eight Statutory Causes of Delay and Expense in Chapter 11 Cases*, 67 AM. BANKR. L.J. 287, 296 (1993).

<sup>56</sup>1995 Judicial Conference Plan, p. 39.

commercial courts.<sup>57</sup> The reported decisions of bankruptcy courts have become the principal source of case law regarding commercial credit transactions. Because the commercial lending markets are national in scope, a decision by a bankruptcy judge in one state affects the practices of lenders not only in that state but throughout the country. Reforming the bankruptcy appeals process so that bankruptcy appeals are resolved initially by a three-judge panel of an Article III appellate court, with the power to bind all of the courts below it, will foster the development of bankruptcy precedent and will thus satisfy the "law declaration" function of bankruptcy appeals.

### C. SPECIALIZED APPELLATE COURT

Both the Bussel and Feinstein articles recommend consideration of the possibility of routing all bankruptcy appeals to a single Article III appellate court, either a new United States Court of Appeals for Bankruptcy or the existing United States Court of Appeals for the Federal Circuit. Although the authors join Bussel and Feinstein in urging both the Judicial Conference Committee and the Bankruptcy Review Commission to consider this possibility, the authors are concerned that the costs of a specialized bankruptcy appeals court outweigh the benefits.

The benefits of channeling all appeals dealing with the Bankruptcy Code to a single court of appeals are obvious: uniformity and efficiency. Having a single appellate court resolve all appeals from decisions of bankruptcy courts (and of district courts sitting in Title 11 matters)<sup>58</sup> is the most efficient and effective way of developing the needed body of substantive bankruptcy law. Such a specialized bankruptcy appeals court would best serve the law declaration function of an appellate court.

The current version of the Judicial Conference Plan acknowledges that specialized appellate courts offer the benefits of uniformity and efficiency but cryptically concludes that "the well-known dangers" of judicial specialization outweigh any such benefit.<sup>59</sup> A recent article by Professor Thomas E. Baker, Professor of Law, Texas Tech University Law School, and a member of the Committee on Rules of Practice and Procedure of the Judicial Conference of the United States, describes these "well-known dangers" as follows:

The arguments raised against court specialization are really two. First, a specialized appellate court . . . will prematurely end the judicial debate on any issue with its first opinion. . . .

---

<sup>57</sup>See Honorable Nancy C. Dreher, *One Judge's View of the Uniform Commercial Code in Bankruptcy Court: Why It Doesn't Work the Way You Thought it Would*, from, *Symposium: "Managing the Paper Trail": Evaluating and Reforming the Article 9 Filing System*, 79 MINN. L. REV. 777, 783 ("bankruptcy courts are the commercial courts of this country").

<sup>58</sup>So long as bankruptcy judges are Article I judges, district court judges will sit in some Title 11 matters. District courts will hear some bankruptcy proceedings in the first instance and will still review the actions of bankruptcy judges in non-core matters.

<sup>59</sup>1995 *Judicial Conference Plan*, p. 41.

Opponents of specialization argue that there is much value in "percolation" of difficult issues. . . . Second, there is a danger that specialized courts will be "captured" by one side or another. This argument dates back to the experience with the Commerce Court at the beginning of this century. That court was perceived by many as having been captured by the railroad interests and was soon dissolved by Congress.<sup>60</sup>

The authors are particularly concerned about the perception of capture. At present, the primary specialized court of appeals is the Federal Circuit.<sup>61</sup> Its jurisdiction includes patent cases.<sup>62</sup> The Federal Circuit has been criticized as being notoriously pro-patent.<sup>63</sup> Historical problems and present attitudes suggest that it is inevitable that any national bankruptcy court of appeals would be perceived as notoriously pro-debtor.

### CONCLUSION

The older of the authors remembers not only the simpler days of being in the third grade listening to Miss Robinson read poetry but also the simpler days of practicing bankruptcy law in which the *Collier* bankruptcy treatise served the law declaration function.<sup>64</sup> For all practical purposes, *Collier* was "the law" under the Bankruptcy Act of 1898.

With all due respect to *Collier*, its publishers and editors, neither *Collier* nor any other treatise can now serve the law declaration function. Today, very able lawyers apply conflicting non-binding precedent to basic and significant bankruptcy issues that arise not only in litigation but also in structuring and documenting transactions, and in counseling clients regarding troubled transactions.

As this Article and others have suggested, the present bankruptcy appellate system is not serving the law declaration function. We urge the Bankruptcy Review Commission to consider restructuring the bankruptcy appeals process to allow for direct appeals to a court of appeals, so that the bankruptcy appeals process can better perform the law declaration function.

---

<sup>60</sup>Thomas E. Baker, *Imagining the Alternative Futures of the U.S. Courts of Appeals*, 28 GA. L. REV. 913, 950 (1994).

<sup>61</sup>See generally 15A CHARLES A. WRIGHT, ARTHUR R. MILLER & EDWARD H. COOPER, FEDERAL PRACTICE AND PROCEDURE § 3903.1 (1992).

<sup>62</sup>The Federal Circuit has exclusive jurisdiction over the following subject matters: Indian claims, tax refund claims, military discharge claims, property taking claims, government contract claims, certain import law issues, patent cases, certain trademark issues, and certain federal employee issues. See Honorable Sheldon Jay Plager, *The United States Court of Appeals: The Federal Circuit, and the Non-Regional Subject Matter Concept: Reflections on the Search for a Model*, 39 AM. U. L. REV. 853 (1990).

<sup>63</sup>Eric Schmitt, *Judicial Shift in Patent Cases*, N.Y. TIMES, January 21, 1986, p. D2.

<sup>64</sup>Cf. JOSEPH SAMET, AVAILABLE RESEARCH TOOLS FOR BANKRUPTCY PRACTICE IN PRACTICING LAW INSTITUTE, THE BASICS OF BANKRUPTCY AND REORGANIZATION 241 (1989) ("the bible of bankruptcy law under the Bankruptcy Act"). The authors are convinced that Mr. Samet would hold the same opinion as to the significance of *Collier* even if Mr. Samet were not a *Collier* contributing author.

