Venue Reform Unlikely for Chapter 11 Bankruptcy Cases

Joshua Gadharf | Friday, February 20, 2015

Once a company elects to file for chapter 11 bankruptcy protection, the venue where the company will file its case is usually one of the first and most important decisions the company must make.

Businesses usually have several venue options. Pursuant to 28 U.S.C. § 1408, a debtor may file for bankruptcy in the district where it is domiciled, where it has its principal place of business, or where its principal assets are located. A company's domicile is generally viewed as its state of incorporation. Therefore, because many companies incorporate themselves in Delaware or New York, those two jurisdictions are often viable venue options. In other words, a company who has its principal place of business in New Mexico and does all of its business on the west coast may nonetheless file for bankruptcy in Delaware if it incorporated itself in that state.

The venue decision is often critical because courts in different districts do not uniformly interpret all provisions of the Bankruptcy Code and often have different procedural rules. For example, a company may prefer to file in a specific district because of favorable appellate court rulings on issues important to the prospective debtor (e.g., standards for rejecting a collective bargaining agreement, or for cutting off product liability claims against successors to debtor, such as a purchaser or reorganized debtor). Appellate court decisions are binding on bankruptcy courts in such appeals court's respective jurisdiction. This very issue caused several weeks of litigation in the Delaware and Illinois bankruptcy courts when Caesars Entertainment Corp. put its largest unit into chapter 11 in Chicago, despite a pending involuntary bankruptcy filing made against Caesars in Delaware.

Many bankruptcy practitioners and scholars have long pushed for venue reform. They view the ability of a company to file bankruptcy in its state of incorporation, regardless of such company's principal place of

business, as inherently unfair to parties in interest in the bankruptcy case, such as creditors who did business with the debtor in the debtor's principal place of business, which could be thousands of miles from the debtor's chosen bankruptcy venue.

The American Bankruptcy Institute Commission to Study the Reform of Chapter 11 recently declined to recommend any changes to the venue rules in chapter 11 cases. According to the Commission: "[it] engaged in extensive deliberations concerning the existing venue statute, the merits of the venue debate, and the potential advantages and disadvantages to reforming the statute [and] found these issues among some of the most difficult and divisive issues considered during the Commission project. Although all Commissioners appreciated and understood the various perspectives represented in the debate, they were unable to reach a consensus regarding whether reform of the venue statute was necessary or what potential reform might best serve the diverse interests in chapter 11 cases."

This decision, or lack thereof, irked many in the industry including Judge Steven Rhodes, who recently presided over the City of Detroit bankruptcy case and who has long been an advocate of venue reform. According to Judge Rhodes, "[t]he current bankruptcy venue law is the single most significant source of injustice in chapter 11 bankruptcy cases."

Despite Judge Rhodes's and others' strong disagreement with the Commission's refusal to recommend venue reform, it now appears unlikely that Congress will consider venue reform anytime soon.

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