Litigating Fraudulent Transfer Claims to Final Judgment In and Out of Bankruptcy Court:

All Is Well in the Wake of *Stern*

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When the Supreme Court issued its seminal decision in *Stern v. Marshall*,[1] bankruptcy practitioners, trustees, judges, and many others, justifiably were concerned that, in the words of Justice Breyer, "Congress' constitutionally based effort to create an efficient, effective federal bankruptcy system" could be jeopardized.[2]

In *Stern*, the Court held that Article III of the constitution prohibits a bankruptcy court from exercising the authority to finally adjudicate a "state law counterclaim that is not resolved in the process of ruling on a creditor's proof of claim."[3] For the first time since the revisions to the Bankruptcy Code that followed the Supreme Court's 1982 ruling in *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*,[4] the authority of bankruptcy courts to hear and decide many cases routinely handled by bankruptcy judges was thrown into doubt.

Of particular importance were the many questions raised with respect to the proper court to hear—and the procedures to be followed in deciding—fraudulent transfer claims. Fraudulent transfer claims have long been a key tool available to bankruptcy estates and trustees to recover assets (1) transferred by debtors to hinder, delay, or defraud creditors or (2) transferred for insufficient consideration at a time when the transferor was insolvent. Fraudulent transfer claims can be brought based on transfers that are actually fraudulent under Section 548(a)(1)(A) of the U.S. Bankruptcy Code[5] for transfers that are constructively fraudulent under § 548(a)(1)(B) and under state law fraudulent transfer provisions through the authority provided by § 544(b)(1).[6] After *Stern*, fraudulent transfer defendants frequently attempted to remove such claims from the bankruptcy court to the district court in light of the uncertain scope of the *Stern* decision.[7] With the Supreme Court's recent decision last term in *Wellness International Network Ltd. v. Sharif*,[8] which upheld the authority of bankruptcy courts to enter final judgments in actions where the parties consent, and its 2014 decision in *Executive Benefits Insurance Agency v. Arkison*,[9] which confirmed that bankruptcy courts can hear and make proposed findings of fact and conclusions of law as to so-called "*Stern* claims" ("unconstitutional core claims"),[10] determining the proper forum to hear fraudulent transfer claims, and the procedures to be followed, now should be far more certain.

The *Stern/Executive Benefits/Wellness* trilogy of cases provides a solid framework for deciding where fraudulent transfer claims should be heard and how such decisions should be reviewed. As asserted below, first, as to fraudulent transfer claims brought by a trustee or estate in bankruptcy against a creditor that has filed a proof of claim, bankruptcy courts retain the constitutional and statutory authority to hear and enter a final judgment. In addition, there is no jury-trial right for a fraudulent transfer action brought against a creditor that has filed a proof of claim, so the bankruptcy court can decide the action as the trier of fact. Moreover, final judgments entered by a bankruptcy court in such cases should be reviewed on appeal by district courts or bankruptcy appellate panels under the standard rules that apply to appeals from bankruptcy courts.

Second, with respect to fraudulent transfer claims brought against parties that have not filed a proof of claim (and are thus not part of the claims resolution process), while *Executive Benefits* establishes that a final judgment cannot be entered on such claims by a bankruptcy court, *Wellness* holds that parties may consent to letting the bankruptcy court hear those claims and enter a final judgment. Furthermore, the *Stern/Executive Benefits/Wellness* trilogy, and post-*Stern* case law from both district courts and circuit courts, should remove most doubt that, absent unusual circumstances, bankruptcy courts are the proper forum to initially litigate fraudulent transfer claims.

In cases where there is no right to a jury trial, the bankruptcy court should hear and initially determine fraudulent transfer claims and submit proposed findings of fact and conclusions of law to the district court to be reviewed in accordance with Federal Rule of Bankruptcy Procedure 9033. Where there is a right to a jury trial, fraudulent transfer claims should remain in the bankruptcy court until discovery is complete, any dispositive motions are initially determined, and the case is ready for trial. If case dispositive motions (i.e., motions for summary judgment) are granted, the bankruptcy judge should submit proposed findings of fact and conclusions of law to be reviewed de novo under Federal Rule of Bankruptcy Procedure 9033. Finally, as argued below, when the case is certified as ready for trial and the reference is withdrawn to the district court for a jury trial, the district court should have broad discretion to decide which, if any, nondispositive rulings it should review under the Rule 9033 procedures before a jury is impaneled.

Third, the clarity provided by the *Executive Benefits* and *Wellness* decisions should pave the way for implementation of a number of procedural rule changes that will provide greater guidance and predictability for practitioners, litigants, and judges in the wake of the initial chaos that followed *Stern*.

Fraudulent Transfer Claims Brought Against a Creditor Who Has Filed a Proof of Claim

In *Executive Benefits*, the Supreme Court left undisturbed the Ninth Circuit's holding that "Article III does not permit a bankruptcy court to enter final judgment on a fraudulent conveyance claim against a noncreditor unless the parties consent."[11] The Ninth Circuit's holding (and presumably the Supreme Court's decision) was based on the conclusion that *Stern,* taken together with the Supreme Court's 1989 decision in *Granfinanciera SA v. Nordberg*, compelled categorizing fraudulent transfer claims against noncreditors as outside the claims allowance process and thus beyond the constitutional limits where

bankruptcy courts can enter final judgments.[12] In *Granfinanciera*, the Supreme Court held that a noncreditor retains a Seventh Amendment right to a jury trial on a fraudulent transfer claim, reasoning that fraudulent transfer claims seeking a money judgment "are quintessentially suits at common law" when brought against a noncreditor and, therefore, outside the claims allowance process.[13] Thus, because bankruptcy courts lack the power to conduct a jury trial absent the parties' consent,[14] without such consent they cannot preside over a trial on a fraudulent transfer claim involving a noncreditor when there is a jury demand.

In light of the two holdings in *Executive Benefits* and *Granfinanciera* that (1) a bankruptcy court lacks constitutional authority to enter a final judgment in a fraudulent transfer case against a noncreditor and (2) such a claim gives rise to a constitutional right to a jury trial, at first blush it may seem that a substantial question is raised as to whether a bankruptcy court properly can exercise authority and enter a final judgment in a fraudulent transfer claim against a creditor who has filed a claim. Indeed, creditor–defendants in fraudulent transfer claims have vigorously pressed such arguments.[15] The issue is highlighted because fraudulent transfer claims involving tens of millions (or more) dollars are often brought in bankruptcy court against creditor–defendants, some of whom may have relatively small claims. Upon close examination, however, because fraudulent transfer claims are necessary to resolve as part of the claims allowance process, the bankruptcy court is well within its authority to enter a final judgment on fraudulent transfer claims against creditor–defendants and there is no constitutional right to a jury trial on such claims.

The Bankruptcy Court's Authority to Enter a Final Judgment With Respect to Fraudulent Transfer Claims Against Creditor Defendants

Once a creditor files a claim in a bankruptcy proceeding, the claim becomes part of the claims allowance process governed by, among other provisions, § 502. As to fraudulent transfer claims in particular, "the court shall disallow any claim from any entity from which property is recoverable" as a fraudulent transfer.[16] Thus, a creditor's claim cannot be resolved until after the fraudulent transfer claim is first determined.

Despite the questions initially raised by *Stern*, its holding explicitly was intended to be "narrow."[17] In *Stern,* the Court held that "Congress, in one isolated respect" ran afoul of the constitutional separation of powers principles under Article III by attempting to give bankruptcy courts "authority to enter a final judgment on a state law counterclaim that is not resolved in the process of ruling on a creditor's proof of claim."[18] In essence, the separation of powers concern at issue in *Stern* boils down to the following: "[T]he question is whether the action at issue stems from the bankruptcy itself or would necessarily be resolved in the claims allowance process."[19] The state law claims that were at issue in *Stern* did not satisfy this standard. In particular, the Supreme Court observed: "[T]here was never any reason to believe that the process of adjudicating [the] proof of claim [at issue in *Stern*] would necessarily resolve [the bankruptcy estate's] counterclaim [for tortious interference]," and the bankruptcy estate's "claim [for tortious interference] is in no way derived from or dependent upon bankruptcy law; it is a state tort action that exists without regard to any bankruptcy proceeding."[20]

The state law counterclaim was, therefore, fundamentally different from the claims at issue in the Court's earlier decisions in *Katchen v. Landy*[21] and *Langenkamp v. Culp.*[22] In those cases, the Supreme Court held that where a creditor filed a claim, no right to a jury trial attached to fraudulent transfer and preferential transfer claims filed against the creditor-defendants. As noted by *Stern,* the Supreme Court's key principle used to underpin the *Katchen* and *Langenkamp* decisions was that the bankruptcy court's exercise of power was proper over avoidance claims that would "necessarily be resolved in the claims allowance process."[23] *Langenkamp* was decided after *Granfinanciera* and, therefore, confirmed the continuing distinction post-*Granfinanciera* between claims resolved in the claims allowance process and those that are not.

The Ninth Circuit, as well, in its comprehensive treatment of the issues in *Executive Benefits*, focused extensively on the fundamental difference between (1) *Katchen* and *Langenkamp*, where no jury-trial right was held to apply to the fraudulent transfer claim at issue and (2) *Granfinanciera*, where the jury-trial right did attach, and *Stern*, where Article III was applicable. The Ninth Circuit expressly stated: "[T]he dispositive distinction between the claims in *Stern* [(and *Granfinanciera*)] and *Katchen* is that in *Katchen*, the trustee's … action 'would necessarily be resolved in the claims allowance process.'"[24]

Once a creditor files a claim in a bankruptcy proceeding, the claim becomes part of the claims allowance process governed by, among other provisions, § 502. As to fraudulent transfer claims in particular, "the court shall disallow any claim from any entity from which property is recoverable" as a fraudulent transfer.[16]

Although *Stern* does not specifically elaborate on the meaning of the phrase "necessarily be resolved in the claims allowance process," fraudulent transfer claims under § 544 and § 548 should satisfy this standard in light of the plain text of 11 U.S.C. § 502(d). As held in one bankruptcy case: "The mandatory language 'shall' [in section 502(d)] makes it necessary to resolve the issues referred to in the statute unless the party filing a proof of claim either turns over the property or pays for it."[25] In other words, issues regarding a creditor's liability for fraudulent transfers necessarily must be decided before or in connection with a bankruptcy court's ruling on whether to disallow that creditor's claim under Section 502(d). Even post-*Stern*, therefore, a bankruptcy court may fully and finally adjudicate fraudulent transfer and preference claims against a creditor who has filed a proof of claim without overstepping any constitutional separation of powers boundaries.

The Supreme Court's discussion in *Stern* of its earlier *Katchen* and *Langenkamp* decisions cements this conclusion. In *Katchen v. Landy*, the Supreme Court "permitted a bankruptcy referee acting under the Bankruptcy Acts of 1898 and 1938 (akin to a bankruptcy court today) to exercise what was known as 'summary jurisdiction'

over a voidable preference claim brought by the bankruptcy trustee against a creditor who had filed a proof of claim in the bankruptcy proceeding."[26] The creditor in *Katchen* argued that the "preferen[tial transfer at issue in that case] should be resolved through a 'plenary suit' in an Article III court," but the Supreme Court "concluded that summary adjudication in bankruptcy was appropriate, because it was not possible for the referee to rule on the creditor's proof of claim without first resolving the voidable preference issue."[27] "There was no question that the bankruptcy referee could decide whether there had been a voidable preference in determining whether and to what extent to allow the creditor's claim" under the version of Section 502(d) then in effect.[28] Thus, "[t]he plenary proceeding the creditor sought could be brought into the bankruptcy court because the same issue arose as part of the process of allowance and disallowance of claims."[29] In other words, one of the consequences of filing the proof of claim "was resolution of the preference issue as part of the process of allowing or disallowing claims, and accordingly there was no basis for the creditor to insist that the issue be resolved in an Article III court." For purposes of this analysis, "of course it makes no difference … whether the bankruptcy trustee urges only a [claim] objection or also seeks affirmative relief."[30]

Langenkamp v. Culp similarly supports the conclusion that filing a proof of claim necessarily brings resolution of fraudulent transfer and preference actions within the claims allowance process and, by extension, within the constitutionally permissible realm of bankruptcy court authority. In *Stern,* the Supreme Court quoted *Langenkamp*'s explanation "that a preferential transfer claim can be heard in bankruptcy when the allegedly favored creditor has filed a claim, because then 'the ensuing preference action by the trustee becomes integral to the restructuring of the debtor creditor relationship.'" [31] "If, in contrast, the creditor has not filed a proof of claim, the trustee's preference action does not 'become part of the claims-allowance process' subject to resolution by the bankruptcy court." In essence, *Langenkamp* confirms the proposition "that by filing a claim against a bankruptcy estate[,] the creditor triggers the process of 'allowance and disallowance of claims,' thereby subjecting himself to the bankruptcy court's equitable power."[32]

Moreover, *Langenkamp* clarified the scope of the Court's then-recent, prior *Granfinanciera SA v. Nordberg* opinion, making clear that the constitutional limits in *Granfinanciera* do not apply where a creditor has filed a proof of claim:

> "In Granfinanciera we recognized that by filing a claim against a bankruptcy estate the creditor triggers the process of allowance and disallowance of claims, thereby subjecting himself to the bankruptcy court's equitable power. If the creditor is met, in turn, with a preference action from the trustee, that action becomes part of the claims-allowance process which is triable only in equity. In other words, the creditor's claim and the ensuing preference action by the trustee become integral to the restructuring of the debtor–creditor relationship through the bankruptcy court's equity jurisdiction."[33]

When read together with *Stern*, the *Katchen* and *Langenkamp* decisions bring the "necessarily be resolved in the claims allowance process" standard in *Stern* into focus. Given the reaffirmation of these cases in *Stern* and the unambiguous text of § 502(d), it should be evident that where a creditor has filed a proof of claim, fraudulent transfer and preference claims asserted against that creditor under 11 U.S.C. §§ 544, 547, 548, and 550 "necessarily" become part of the claims allowance process within the meaning of *Stern*. As such, the "narrow" and "isolated" constitutional separation of powers concern identified in *Stern* simply does not apply to such claims.

Two circuits essentially have adopted this reading of *Stern* as it applies to fraudulent transfer claims against creditors that have filed claims. In a 2013 post-*Stern* decision, *Peterson v. Somers Dublin Ltd.,*[34] the Seventh Circuit came to the same conclusion outlined above for essentially the same reasons. The Seventh Circuit said: "The current dispute comes within a bankruptcy judge's authority, notwithstanding *Stern*, because all of the defendants submitted proof of claims as … creditors and thus subjected themselves to preference recovery and fraudulent conveyance claims by the Trustee."[35] The Seventh Circuit's conclusion was based on a citation to § 502(d) and its observations that the "Supreme Court [so] held in *Katchen* … and *Langenkamp*" and that "*Stern* stated that its outcome is consistent with those decisions."[36]

Similarly, in *Onkyo America Inc. v. Global Technovations Inc.* (*In re Global Technovations Inc.*),[37] the Sixth Circuit held: "It is crystal clear that the bankruptcy court had constitutional jurisdiction to adjudicate [a fraudulent transfer claim] because 'it was not possible … to rule on [the creditor's] proof of claim without first resolving the fraudulent-transfer issue." The Sixth Circuit noted that the debtor's defense against the proof of claim was the fraudulent transfer claim against the creditor.[38] This defense, of course, arises out of Section 502(d) and applies in all cases where the debtor pursues a fraudulent transfer claim against a creditor who filed a proof of claim.

The Sixth Circuit went on to observe that "[w]hat is not crystal clear is whether the bankruptcy court had jurisdiction under *Stern"* to make findings that may not have been necessary to determine the creditor's proof of claim.[39] The Court of Appeals then further held: "We do not believe that *Stern* requires a court to determine, in advance, which facts will ultimately prove strictly necessary to resolve a creditor's proof of claim."[40] Findings that the bankruptcy court reaches as part of its resolution of the fraudulent transfer defense are within the authority of the bankruptcy court to make. Under the solid logic of the *In re Global Technovations Inc.* decision, because it is necessary to resolve a fraudulent transfer defense to resolve a creditor's proof of claim, the bankruptcy court is within its constitutional authority, as refined by *Stern,* to enter a final judgment on the affirmative claim for relief that is part and parcel of the fraudulent transfer issues raised by the § 502(d) defense.

A Creditor Who Has Filed a Claim Should Not Be Found to Have a Right to a Jury Trial With Respect to a Debtor's Fraudulent Transfer Claim

For the same reasons outlined above, a creditor who has filed a proof of claim should not be found to have a right to a jury trial with respect to a debtor's fraudulent transfer claim. As described by the Ninth Circuit in *Executive Benefits*, "*Stern* fully equated bankruptcy litigants' Seventh Amendment right to a jury trial in federal bankruptcy proceedings with their right to proceed before an Article III judge."[41] A creditor who has filed a proof of claim subjects herself to the claims allowance process. Under *Katchen* and *Langenkamp* the claims allowance process is within the authority of the bankruptcy court to decide and does not give rise to a right to a jury trial.[42] *Stern* described in detail how its decision was consistent with the *Katch-*

en/Granfinanciera/Lagenkamp precedents.[43] In sum, there is no substantial reason to doubt that the long familiar rule that there is no right to a jury trial on a debtor's fraudulent transfer action if the creditor has filed a proof of claim still stands on solid ground.

A Bankruptcy Court's Final Judgment on a Fraudulent Transfer Claim Against a Creditor Who Has Filed a Proof of Claim Is Subject to the Standard Appellate Process

As a practical matter, one of the most significant results of having the bankruptcy court enter a final judgment is that such a final judgment is subject to the normal process for appellate review of bankruptcy court appeals from "final judgments, orders and decrees" under 28 U.S.C. § 158(a). The appeal is then governed by Federal Rules of Bankruptcy Procedure (FRBP) Rules 8001–8020. Factual findings are reviewed under the clearly erroneous standard of review set forth in FRBP Rule 8013, and "due regard shall be given to the opportunity of the bankruptcy court to judge the credibility of the witnesses." Conclusions of law are reviewed de novo. The briefing process for bankruptcy appeals generally mirrors the traditional appellate process.

In contrast, of course, when the bankruptcy court lacks authority to enter a final judgment, it may only issue proposed findings of fact and conclusions of law. These are presented to the district judge for entry of a final judgment "after considering the bankruptcy judge's proposed findings and conclusions and after reviewing de novo those matters as to which any party has timely and specifically objected" pursuant to 28 U.S.C. § 157(c)(1). The review of proposed findings of fact and conclusions of law is governed by FRBP Rule 9033. As discussed below, review of findings of fact is de novo "upon the record, or after additional evidence, of any portion" of the proposed findings as to which there is a specific objection made.[44] The briefing is limited by rule to the written objections and a response, with shorter time periods than in the usual appellate review process.

Fraudulent Transfer Claims Brought Against Parties That Are Not Creditors

Determining the Proper Forum

The Supreme Court's 2015 decision in *Wellness*, coupled with its 2014 decision in *Executive Benefits*, reaffirms the essential underpinnings of the "division of labor in the current statute" as enacted in the aftermath of *Northern Pipeline* back in 1984. Indeed, in *Wellness*, the Supreme Court expressly noted the importance of bankruptcy judges (and magistrate judges) to the work of the federal courts: "[I]t is no exaggeration to say that without the distinguished service of these judicial colleagues, the work of the federal court system would grind to a halt."[45] The Court emphasized the importance of practical attention to substance rather than form in considering the proper forum to hear claims related to bankruptcy proceedings. The Court also emphasized that the close relationship of Article III courts to bankruptcy judges diminishes concerns that leaving *Stern* claims for decision in the bankruptcy courts usurps the role of Article III courts.[46]

The Court recognized the basic value of the effort by Congress to "supplement[] the capacity of the district courts through the able assistance of bankruptcy judges. So long as those judges are subject to control by the Article III courts, their work poses no threat to the separation of powers."[47] The *Wellness* decision thus builds on the recognition in *Executive Benefits* that the process for handling noncore claims by submitting proposed findings of fact and conclusions of law "may be applied naturally to *Stern* claims."[48] With respect to fraudulent transfer claims in particular, the Court in *Executive Benefits* noted the inherent relationship between the bankruptcy case as a whole and fraudulent transfer claims, which "[a]t bottom … assert that property that should have been part of the bankruptcy estate and therefore available to creditors pursuant to Title 11 was improperly removed."[49]

The two recent decisions should go far in reassuring district courts and litigants, as well as bankruptcy courts, that, absent unusual circumstances, fraudulent transfer claims remain a prime example of the type of labor that is appropriate to rest on the shoulders of the bankruptcy courts, rather than Article III judges, in the first instance.[50] Thus, even when there is a fraudulent transfer claim against a noncreditor, the cases presumptively should be adjudicated in the bankruptcy court before being sent to the district court for entry of a final judgment.

In cases in which there is no jury demand, *Executive Benefits* teaches that "these *Stern* claims fit comfortably within the category of claims governed by section 157(c)(1) [thus permitting] the Bankruptcy Court … to follow the procedures required by that provision, i.e., submit proposed findings of fact and conclusions of law to the District Court to be reviewed de novo."[51] When such claims are filed in the bankruptcy courts, they will remain there unless there is a motion to withdraw the reference in accordance with 28 U.S.C. § 157(d). Withdrawal can be sought on mandatory or permissive grounds. It is now established that mandatory withdrawal of the reference is not required as a result of some statutory "gap," as had been argued often in the wake of *Stern*.[52]

That leaves permissive withdrawal of the reference as the option for removing fraudulent transfer claims filed in the bankruptcy court. Permissive withdrawal of the reference requires that it be for "cause shown." Although § 157(d) does not define "cause," the following factors help guide whether sufficient cause exists for permissive withdrawal of the reference: (1) the efficient use of judicial resources; (2) the delay and costs to the parties; (3) the uniformity of bankruptcy administration; (4) the prevention of forum shopping; and (5) other related factors.[53] "Permissive withdrawal is permitted only in a limited number of circumstances."[54] As such, courts "strictly construe the section 157(d) factors so that it does not provide an 'escape hatch' out of bankruptcy court."[55]

It should be the rare case in which sufficient cause will exist to remove fraudulent transfer claims from bankruptcy courts under ordinary circumstances. Many courts throughout the country have recognized that all of the factors generally will weigh in favor of keeping the case with the bankruptcy courts and thus taking advantage of the bankruptcy courts' knowledge of the underlying case, promoting uniformity with respect to multiple claims, the specialized expertise of the judges in bankruptcy law, and the judicial efficiency to be gained by keeping these cases on the bankruptcy court's docket.[56] While there was initial uncertainty in the immediate aftermath of *Stern* about the wisdom of keeping the cases in the bankruptcy forum,[57] the established recent trend is to maintain fraudulent transfer cases in the bankruptcy courts.[58]

Even in cases where a jury demand has been made and thus the case may ultimately be removed to the district court for the jury trial, permissive withdrawal of the reference generally should be delayed until discovery is complete, all dispositive motions have been ruled upon, and the case is ready for trial. As held by the Ninth Circuit in *In re Healthcentral.com*, "[a] Seventh Amendment jury trial in the

district court does not mean the bankruptcy court must instantly give up jurisdiction and that the action must be transferred to the district court."[59] To the contrary, as the chief district judge in the Eastern District of California also recently held, "[a]llowing the bankruptcy court to handle the discovery issues, settlement conferences, and motion practice is the most efficient outcome" and best ensures that the efficient division of labor between district courts and bankruptcy courts is maintained.[60] Indeed, withdrawing the reference simply because there is a jury demand creates a serious risk of inconsistent results, because many bankruptcy cases involve multiple fraudulent actions and most are likely to be filed against creditors, in which no jury-trial right attached, so most actions would likely be heard in the bankruptcy courts.

Many of the concerns with keeping fraudulent transfer cases raised in the aftermath of *Stern* arose out of the prospect that de novo review by an Article III court would require the functional equivalent of a complete "do over."[61] As discussed next, however, the nature of the de novo review of proposed findings of fact and conclusions of law in fraudulent transfer actions against noncreditors where there has been no jury demand does not create any need for a complete rehash of the underlying proceedings; instead, it is a targeted, focused, and flexible review process. Similarly, where there is a valid jury demand against a noncreditor, the review process for any case involving dispositive rulings by the bankruptcy court would be substantially the same as the review for other proposed findings of fact and conclusions of law by bankruptcy courts. With respect to any nondispositive case rulings in jury trial cases, the district court should retain great flexibility to decide which, if any, nondispositive case rulings by the bankruptcy court to review before submitting any remaining claims to a jury.

The Review of Bankruptcy Court Decisions in Fraudulent Transfer Claims Brought Against Parties That Are Not Creditors

The de novo review of proposed findings of facts and conclusions of law outlined in 28 U.S.C. § 157(c)(1) is statutorily contained to a review of "those matters to which any party has timely and specifically objected." It does not require that a district court conduct a rehearing or broadly reconsider all matters that were before the bankruptcy court from scratch. Rather, the review proceeds in accordance with FRBP Rule 9033(a) with a targeted focus on a party's "written objections [that] identify the specific grounds for such proposed findings or conclusions objected to and state the grounds for such objection." The Rule is modeled after Federal Rule of Civil Procedure (FRCP) Rule 72, which governs the review of proposed findings of fact and conclusions of law submitted to district courts by magistrate judges.[62]

In the 1980 decision of *United States v. Raddatz*, the Supreme Court considered whether the procedure in FRCP Rule 72 comported with due process.[63] The Court began by stating, "It should be clear that on these dispositive motions [the procedures] call[] for a de novo determination, not a de novo hearing." The Court noted that the statute governing proposed findings of fact and conclusions of law submitted by magistrate judges to the district court, the language of which is tracked in § 157(c)(1), "grants the district judge the broad discretion to accept, reject or modify the magistrate's proposed findings."[64] The Court recognized the value to the district courts in making use of previous proceedings and in the assembling and analysis of facts presented for review.[65] The Supreme Court held that the district judges act well within their broad discretion "to give such weight as [their] merit commends and the sound discretion of the judge warrants[.] [T]hat delegation does not violate Article III so long as the ultimate decision is made by the district court."[66]

The *Raddatz* decision established that there is no general duty on the part of district courts either to conduct new de novo hearings or to comb exhaustively through the underlying record to conduct a de novo review of the bankruptcy court's recommendations. Rather, much as is the case with traditional appellate review, the reviewing court's focus will be driven by the parties' contentions of error and the parties' use of the record to support or rebut the contentions. While the district court reviewing proposed findings of fact and conclusions of law may request "additional evidence" or "recommit the matter to the bankruptcy judge with instructions," the district judge retains great flexibility in using his or her judgment to evaluate the need for more evidence and to choose the proper course. The court of appeals will review the district judge's decisions in accepting, rejecting, or modifying the proposed findings on the merits and presume that the district court conducted an appropriate analysis of the record before ruling on the recommendations of the bankruptcy court.[67]

In his concurring opinion in *Raddatz*, Justice Harry Blackmun emphasized the benefits of the two step review of proposed findings of fact and conclusions of law to accurate decision making. As the justice astutely observed, eliminating the first level of decision making would undermine, not enhance, the procedural protections and efforts to get to the right results.[68] For decades, the process by bankruptcy courts of submitting proposed findings of fact and conclusions of law to district courts has improved the efficient use of judicial resources, relieved overburdened district courts of their work, and resulted in a system that works well. As the dust has settled after *Stern*, it should be considerably more apparent that the concern of having to conduct proceedings twice in order to conduct de novo review of proposed findings of fact and conclusions of law if *Stern* claims remained in the bankruptcy court through the initial determinations was overblown. The system established by § 157(c)(1), FRBP Rule 9033, and related rules does not result in inefficiencies, extra work, or unnecessary duplication.

In fraudulent transfers cases against a noncreditor in which there is a jury demand and the case is left in the bankruptcy court until it is ready for trial, questions may arise with respect to both rulings on case-dispositive motions (i.e., motions for summary judgment or dismissal as a matter of law) and with regard to noncase-dispositive motions ruled upon by the bankruptcy court in the course of getting the matter ready for trial. The question should be easily answered with respect to dispositive motions—those rulings should be submitted as proposed findings of fact and conclusions of law following the procedures in § 157(c)(1) and FRBP Rule 9033 in accordance with the holding in *Executive Benefits*.

The decision on how a district court should handle nondispositive rulings when the case is withdrawn as ready for trial, especially rulings on summary adjudication motions that resolve some, but not all claims, is more difficult. One option would be to proceed to a jury trial on all of the remaining claims and consider the nondispositive rulings once there is a final judgment. Indeed, in a recent district court case, the

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defendants argued that the district court had no authority to rule on partial summary judgment orders of the bankruptcy court—that such orders could only be reviewed on direct appeal to the court of appeals after a final judgment was entered.[69] The district court rejected the argument that the bankruptcy court's rulings granting summary adjudication of entire claims should be considered as final dispositions of those claims and treated as proposed findings of fact and conclusions of law.[70] Those rulings would be considered de novo before the jury trial on the remaining claims. On the other hand, the district court declined to review de novo pretrial rulings that were not dispositive of entire claims.[71]

The district court's approach is consistent with the general rule for nondispositive motions set forth in FRCP Rule 54(b). This provides that "any order or decision … that adjudicates fewer than all of the claims … may be revised at any time before entry of a [final] judgment." When the bankruptcy court has certified the case as ready for trial and the case is withdrawn to the district court, the district court will be in the best position to judge how the trial should proceed before the jury and what issues and prior rulings are significant enough to merit de novo review before the trial is conducted. The parties should be provided an opportunity to specify which, if any, pretrial rulings should be reviewed and the reasons for their position. The other party should be afforded an opportunity to oppose the request to reconsider pretrial rulings. With respect to nondispositive rulings that dispose of entire causes of action or resolve the claims as to some, but not all parties, a proper default rule may be to consider all such rulings as proposed findings of fact and conclusions of law subject to de novo review.[72] With respect to those rulings that are reviewed, the review should be conducted in accordance with FRBP 9033.

Additional Procedural Rule Changes Are Likely To Further Clarify the Landscape

The decisions in *Wellness* and *Executive Benefits* set the stage for additional clarification of both the FRBP and the rules of local courts. In particular, in 2012 the Advisory Committee on Bankruptcy Rules proposed amending FRBP Rules 7008, 7012, 7016, 9027, and 9033 to reflect changes to account for the decision in *Stern*.[73] Only one of the rule changes was adopted: Rule 7008 was amended to require that in an adversary proceeding before a bankruptcy court, the complaint, counterclaim, cross-claim, or third-party claim contain a statement as to whether the pleader consents to entry of a final judgment by the bankruptcy court regardless of whether the matter is statutorily core or noncore. (Prior to the amendment, such a statement was only required if the matter was noncore.)

The other proposed amendments would have required such a statement in an answer to a complaint or similar pleading (Rule 7012); directed the bankruptcy court to consider its authority to enter a final judgment at a Rule 7016 pretrial conference; required that the statement of consent or nonconsent in Rule 9027 (governing motions to withdraw) also be amended to apply to both statutorily core and noncore matters; and required that Rule 9033 be amended to specify that its procedures apply to review of proposed findings of fact and conclusions of law issued by the bankruptcy court in any proceeding, whether or not statutorily core or noncore. With the guidance of *Wellness* and *Executive Benefits*, these proposed changes and similar changes to clarify the consent issues and the applicability of Rule 9033 in *Stern* claims are open for reconsideration.

Similarly, the local bankruptcy rules in many districts have been revised to clarify the consent and appeal procedures regarding the handling of potential *Stern* claims. For example, in the Northern District of California a statement of consent or nonconsent is required in both affirmative and responsive pleadings (Local Rules 7008-1 and 7012-1).[74] The local rules even provide guidance with respect to appealing bankruptcy decisions and preserving a litigant's right to challenge the authority of the bankruptcy court to issue a final order.[75] The local rules specify that if the "District Court agrees that the Bankruptcy Court should have issued proposed findings and conclusions, it can treat the decision of the Bankruptcy Court as proposed conclusions subject to de novo review."[76] Such rule changes, along with the guidance of the cases post-*Stern*, will help practitioners navigate the wrinkles to the core/noncore dichotomy created by *Stern.* Moreover, practitioners should be careful to review the local bankruptcy rule and the FRBP rules before filing and responding to fraudulent transfer claims, and other potential *Stern* claims, to ensure that they are aware of the latest developments.

Conclusion

The *Stern* decision caused a lot of chaos, confusion, and procedural maneuvering by litigants. Recent developments, though, have calmed the waters. The procedures for litigating fraudulent transfer claims to final judgment both in and out of bankruptcy courts should develop further and with more predictability going forward. ⊙

Endnotes

1 564 U.S. ___, 131 S. Ct. 2594 (2011).

2 131 S. Ct. at 2629.

3 *Id*. at 2620.

4 102 S. Ct. 2858 (1982). In *Northern Pipeline*, the Court held that it was an unconstitutional violation of Article III of the U.S. Constitution to vest a bankruptcy court—as a non-Article III court—with jurisdiction to decide a state law contract claim that was not integral to "the restructuring of debtor–creditor relations, which is at the core of the federal bankruptcy power." *Id*. at 71-72 & n. 26. (Unlike Article III courts, bankruptcy courts lack life tenure, protection from removal during good behavior, and constitutional salary protection. *See* Article III, section 1, U.S. Constitution.) In response to *Northern Pipeline*, Congress enacted the Bankruptcy Amendments and Federal Judgeship Act of 1984, which granted each district court the power to refer to bankruptcy judges for the district all cases related to bankruptcy proceedings. 28 U.S.C. § 157(a). The bankruptcy courts were granted the statutory authority to hear and finally determine all "core" bankruptcy proceedings, as listed in § 157(b)(1), and more limited authority with respect to "noncore" proceedings under section 157(b)(2). As to "noncore" proceedings, absent consent, the bankruptcy court was only given authority to "submit proposed findings of fact and conclusions of law" to be reviewed by the district de novo. 28 U.S.C. § 157(c)(1).

5 Unless noted otherwise, statutory citations will be to the U.S. Bankruptcy Code, 11 U.S.C. §§ 101 *et seq.*

6 Recovering on fraudulent transfers is actually a two step process: The transfer is first

avoided under § 548 or 544 and then the property transferred, or the value of the property transferred, can be recovered under § 550.

[7] *See, e.g., In re Heller Ehrman LLP*, 464 B.R. 348, 358 (N.D. Cal. 2011); *Kelly v. J.P. Morgan Chase & Co.,* 464 B.R. 854, 858 (D. Minn. 2011).

[8] 135 S. Ct. 1932 (2015).

[9] 134 S. Ct. 2165 (2014).

[10] In particular, the term "*Stern* claims" refers to those claims that Congress designated as "core" proceedings under 28 U.S.C. § 157(b)(2), but as to which bankruptcy courts lack constitutional authority to enter a final judgment under the holding of *Stern. Executive Benefits* held that bankruptcy courts could hear such "unconstitutional core claims" and issue proposed findings of fact and conclusions of law in the same manner that statutory "noncore" proceedings are treated under 28 U.S.C. § 157(c)(1).

[11] 134 S. Ct. 2169 (quoting *In re Bellingham Ins. Agency Inc.,* 702 F.3d 553, 565 (9th Cir. 2012)). Interestingly, the Supreme Court did not actually reach the issue, but instead "assume[d] without deciding that the fraudulent claims in this case are *Stern* claims [(claims that are designated by statute as core, but that as to which the bankruptcy court cannot constitutionally enter a final judgment)]." *Id.* at 2174.

[12] *See* 702 F.3d at 561.

[13] 102 S. Ct. 2782, 2798 (1989).

[14] 28 U.S.C. § 157(e).

[15] *Official Committee of Unsecured Creditors of Appalachian Fuels LLC v. Energy Coal Res. Inc.* (*In re Appalachian Fuels*), 472 B.R. 731, 741 (E.D. Ky. 2012).

[16] 11 U.S.C. § 502(d). "Entity" includes any person. 11 U.S.C. § 101(15).

[17] 131 S. Ct. at 2619.

[18] *Id.* at 2620.

[19] *Id.* at 2618.

[20] *Id.* at 2617-18.

[21] 86 S. Ct. 467 (1966).

[22] 111 S. Ct. 330 (1990).

[23] 131 S. Ct. at 2616-17 (internal quotations and citations omitted).

[24] 702 F.3d at 564.

[25] *Doctors Hosp. of Hyde Park,* __BR__, 2013, WL 5524696, at *20-21 (emphasis added).

[26] *Stern,* 131 S. Ct. at 2616 (citing Katchen v. Landy, 86 S. Ct. 46 (1966)).

[27] *Id.* at 2616.

[28] *Id. see also Katchen,* 86 S. Ct. at 473.

[29] *Stern*, 131 S. Ct. at 2616.

[30] *Katchen,* 86 S. Ct. at 477.

[31] *Stern*, 131 S. Ct. at 2617 (quoting *Langenkamp v. Culp,* 111 S. Ct. 330 (1990).

[32] *Langenkamp,* 111 S. Ct. at 331.

[33] *Id.* at 44–45 (1990) (internal quotations and citations omitted).

[34] 729 F.3d 741, 747 (7th Cir. 2013).

[35] *Id.*

[36] *Id.* 747 (citations omitted).

[37] 694 F.3d 705, 722 (6th Cir. 2012).

[38] *Id.*

[39] *Id*.

[40] *Id.*

[41] 702 F.3d at 563.

[42] *Katchen*, 86 S.Ct at 477; *Langenkamp,* 498 U.S. at 44.

[43] *Stern*, 131 S. Ct. at 2616-18; *see also Peterson*, 729 F.3d at 747.

[44] Fed. R. Bankr. P. 9033(d)

[45] 135 S. Ct. at 1938-39.

[46] *Id.* at 1944-45.

[47] *Id.* at 1946.

[48] 134 S. Ct. at 2173.

[49] *Id.* at 2174.

[50] *See Wellness*, 135 S. Ct. at 1946.

[51] 134 S. Ct. at 2174.

[52] *See, e.g., In re Heller Ehrman LLP*, 464 B.R. 348, 358 (Bankr. N.D. Cal. 2011); *In re Blixeth*, 2011 Bankr. LEXIS 29533, 2011 WL 3274042 (Bankr. D. Mont. 2011).

[53] *See, e.g*., *In re Canter*, 299 F.3d 1150, 1154 (9th Cir. 2002) (quoting *Sec. Farms v. Int'l Bhd. of Teamsters, Chauffeurs, Warehousemen, & Helpers*, 124 F.3d 999, 1008 (9th Cir. 1997)).

[54] *E.g., In re The Mortgage Store Inc.*, 464 B.R. 421, 428 (D. Haw. 2011) (quoting *Hawaiian Airlines*, 355 B.R. at 223).

[55] *In re Don's Making Money LLP*, No. CV-07-319-PHX-MHM, 2007 WL 1302748, at *7 (D.Ariz. May 1, 2007) (internal quotations and citations omitted). The movant, moreover, bears the burden of showing that these factors constitute sufficient cause to withdraw the reference. *See, e.g., In re First Alliance Mortgage Co.*, 282 B.R. 894, 902 (Bankr. C.D. Cal. 2001).

[56] *E.g., In re Healthcentral.com*, 504 F.3d 775, 788 (9th Cir. 2007).

[57] *See, e.g., In re Bearingpoint Inc.,* 453 B.R. 486, 488 (Bankr. S.D.N.Y. 2011) (bankruptcy court declined to hear state law claims as required in confirmation plan due to concerns raised by *Stern*).

[58] *See, e.g., In re Rhodes Cos. LLC*, No. 2:12-CV-01272-MMD, 2012 WL 5456084, at *6 (Bankr. D. Nev. Nov. 7, 2012) ("Judicial economy militates in favor of allowing the bankruptcy court to proceed with pretrial matters in cases involving fraudulent conveyance claims."); *In re Heller Ehrman LLP*, 464 B.R. 348, 358 (Bankr. N.D. Cal. 2011) (denying motion to withdraw the reference and noting that "several other district courts have come to the same conclusion, focusing on the efficiency of the bankruptcy system as a whole and the specific knowledge of bankruptcy judges as to federally-created fraudulent conveyance actions").

[59] 504 F.3d at 788.

[60] *Bell v. Lehr*, 2014 WL 526406, at *2 (Bankr. E.D. Cal. Feb. 7, 2014).

[61] *See Dev. Specialists Inc. v. Akin Gmp Strauss Hauer & Feld, LLP* (*In re Coudert Brothers LLP*), 462 B.R. 457, 472 (Bankr. S.D.N.Y. 2012).

[62] Fed. R. Bankr. P. 9033, Notes of Advisory Committee on Rules—1987.

[63] 447 U.S. 667, 669 (1980).

[64] *Id*. at 680-81.

[65] *Id.* at 683.

[66] *Id.*

[67] *See Home Federal Savings & Loan Ass'n v. Dillon Construction Company Inc.* (*In re Dillon Construction Co. Inc.*), 922 F.2d 495, 497 (8th Cir. 1982); *Vekamaf Holland BV v. Pipe Benders Inc.,* 671 F.2d 1185, 1886 (9th Cir. 1982).

[68] 447 U.S. at 438-39 (Blackmun, J., concurring).

[69] *Schoenmann v. Torchia* (*In re Synergy Acceptance Corp.*), 2015 WL 3958155 *3 & n.6 (Bankr. N.D. Cal. June 29, 2015).

[70] *Id*. at *4.

[71] *Id.*

[72] *See, e.g., id.; In re Rady*, 138 B.R. 608, 610 (Bankr. D. Nev. 1992).

[73] 2012 Report to the Standing Committee, Advisory Committee on Bankruptcy Rules.

[74] www.canb.uscourts.gov/procedures/local-rules.

[75] N.D. Cal. Bankr. Local Rule 8001-2.