UNITED STATES HOUSE OF REPRESENTATIVES

HOUSE JUDICIARY COMMITTEE
SUBCOMMITTEE ON COURTS, COMMERCIAL
AND ADMINSTRATIVE LAW

HEARING ON CHAPTER 11 BANKRUPTCY VENUE REFORM ACT OF 2011 H.R. 2533

SEPTEMBER 8, 2011

TESTIMONY OF THE HON. FRANK J. BAILEY
CHIEF JUDGE
UNITED STATES BANKRUPTCY COURT
DISTRICT OF MASSACHUSETTS

Mr. Chairman and Members of the Subcommittee on Courts, Commercial and Administrative Law:

My name is Frank J. Bailey, I am the Chief Bankruptcy Judge for the United States Bankruptcy Court for the District of Massachusetts. Thank you for the opportunity to discuss with you the Chapter 11 Bankruptcy Venue Reform Act of 2011, H.R. 2533.

I am one of the five bankruptcy judges in the District of Massachusetts and I primarily handle cases in Boston. In addition to Boston, we have courts in Worcester and Springfield, Massachusetts. I have been on the bench for a little under three years. Before that I was a partner in a Boston law firm for many years where I practiced both litigation and bankruptcy. I graduated from the Georgetown University School of Foreign Service here in Washington in 1977 and from the Suffolk University Law School in 1980. I then served as law clerk to the Honorable Herbert P. Wilkins, Associate Justice of the Supreme Judicial Court of Massachusetts. Following that I joined the law firm of Sullivan & Worcester LLP where I worked primarily in the bankruptcy department. Later I joined Sherin and Lodgen LLP where I chaired the Litigation Department and was a member of the Management Committee for many years.

I was appointed to the bench by the First Circuit Court of Appeals in late 2008 after nomination by the 1st Circuit Merit Selection Panel and became the chief judge in late 2010. I co-chair the Local Rules Committee and am active in lecturing for continuing legal education programs and at bar and academic functions, as do all of my Massachusetts colleagues. I also teach Creditors Rights and Bankruptcy Law at New England Law Boston, a Boston area law school. I am active in the National Conference of Bankruptcy Judges and serve on the Endowment Committee. I am also a member of the Board of Directors of the Immigrant Learning Center in Malden, Massachusetts, which provides free English language classes to new Americans.

I am testifying today on my own behalf, and my views do not reflect the views of the Judicial Conference of the United States, the National Conference of Bankruptcy Judges, or any committee on which I serve. Also, I am attending at my own expense today, without reimbursement from the judiciary or any of the organizations in which I am active. That is because I believe strongly in this bill and wish to indicate my support for it.

SUMMARY OF TESTIMONY

When Congress enacted the current bankruptcy venue statute, 28 U.S.C. sect. 1408, the intent was to offer large public companies broad latitude in deciding where to file a reorganization case. Logically and sensibly, the choices included the location of the corporate headquarters and the place where most of the corporate assets are located. This was also consistent with the history of bankruptcy venue for large public company cases. Congress expanded the choices to include the place of incorporation and the place that a corporate affiliate, no matter how small or recently formed, had previously filed. This was applicable even if the corporation transacted little or no business in those places. Congress no doubt was comfortable with offering such broad venue choices because the statute gives courts the power, on request, to overrule the venue choice of the filer if it is inconvenient or unfair to other parties. 28 U.S.C. sect. 1412.

It has simply not worked out the way Congress intended. This broad grant of venue choices has had an unexpected impact on the distribution of large bankruptcy cases. While the convenience of counsel and others close to the center of the process has proven a key to case placement, the rights

of small creditors, vendors, employees and pensioners has been allowed to suffer.

Through creative lawyering, or perhaps what could be described less generously as “clever” lawyering, cases are now often filed in certain select "magnet" courts in districts far from where the corporation actually operated its business. And efforts to ask that a court overrule the filer's choice have proven to be much too expensive for all but the most well-heeled creditors. And even when such a bid to change venue has been tried, the strong legal presumption that the debtor chose the appropriate place has proven to be a very difficult legal hurdle to overcome.

It has evolved that the driving force in venue decisions in bankruptcy filings has become what is best for the lawyers and other turnaround and workout professionals that advise corporate management. And in a world of prepackaged plans, lock up agreements and claims trading, often all of the largest financial stakeholders have agreed to a particular venue choice long before filing. This means the banks, bondholders, and hedge funds can, together with the debtor, select a venue that is convenient for them, and the employees, local governments, landlords and smaller vendors will be stuck with that choice.

The proposed amendments will go far toward fixing this unfairness.

CASE STUDIES: POLAROID CORPORATION and EVERGREEN SOLAR, INC.

In the structure of American business people engage in enterprises through the legal fiction of corporations. Corporations are merely combinations of people that have as their goal the organization, development and operation of that enterprise for a profit. As such, corporations become citizens of the community in which they operate. Like symphonies, museums, colleges and universities and professional sports teams, business corporations are woven into the fabric of the community. Perhaps more than the afore-mentioned cultural institutions, the businesses at which people work and into which they invest their futures often become iconic representatives of the communities themselves. Coca Cola in Atlanta, Gillette in Boston, FedEx in Memphis, the Tampa Bay Bucs in Tampa/St. Pete and Microsoft in Seattle: communities such as these are impressed with the corporate seal of the companies that are founded and nourished through the ingenuity and sweat of local citizens that work for them, as well as those that provide goods and services to them.

I would like to focus on two companies that were very much part of the soul of the Boston-area communities in which they were founded and grown.

Polaroid Corporation. Polaroid is a famous company. It was founded in 1937 by Edwin Land after his breakthrough scientific research of polarization techniques. This of course led to the development of polarized lenses and eventually to the instant film developing techniques for which the company became famous. Polaroid was, since its inception, headquartered in Cambridge, Massachusetts. It had management, research and development, and manufacturing capabilities around the globe, but it always maintained a large commitment to Massachusetts – including a large Massachusetts-based work force. In fact, Polaroid employed thousands of people in the District of Massachusetts and kept many other thousands of people working to provide it goods and services. Then, after a long period of decline mostly caused by a failure to appreciate newly emerging digital photography, Polaroid filed a Chapter 11 bankruptcy proceeding on October 11, 2001. But that bankruptcy case was filed in the District of Delaware, not in the District of Massachusetts or in any other district where Polaroid had significant investment or assets. Thus, any

interested party had to either travel to Wilmington, Delaware or hire a lawyer to appear in the Delaware court in order to make known its views as the Chapter 11 case of Polaroid progressed through the courts.

Evergreen Solar, Inc. Let me now focus on a much more recent example. The Commonwealth of Massachusetts has worked hard to identify the segments of the global economy in which it could most successfully compete. Leveraging the presence of its world class colleges and universities and the human capital that inevitably is attracted to such institutions, the state government identified, among others, businesses in the alternative energy arena as a focus. One of those businesses is Evergreen Solar, Inc. Please refer to **Exhibit 1**. Evergreen, which was incorporated in Delaware, develops materials for the production of solar power. As a targeted company in a targeted industry, the state offered Evergreen $58 million in incentives to locate a plant in Massachusetts. This was the largest corporate incentive offering in state history. In addition, Massachusetts provided a $500 tax rebate to in-state customers of Evergreen.

But the story does not end well for Massachusetts. On August 15, 2011 Evergreen filed a Chapter 11 petition in the District of Delaware, citing

an inability to compete with similar companies, mostly in China. At or just before its filing, Evergreen maintained its corporate headquarters in Marlborough, Massachusetts (30 miles West of Boston) and employed well over a thousand workers in the state.

The reason I focus on these two companies is to highlight that companies that are closely identified with the citizens and government of Massachusetts have chosen to file for bankruptcy relief far from the District of Massachusetts. These companies filed far from the employees that hoped for a successful outcome in the bankruptcy case and to save their jobs and perhaps their pensions. These companies filed far from where most vendors of goods and services to those companies had come to expect that they would deal with the companies. These companies filed far from where the local governments – state and municipal – had provided support and, in the case of Evergreen, very large incentives.

These are merely two examples of Massachusetts companies that have elected to file in locations outside the District of Massachusetts in recent years. Since 2000, at least thirty large and mid-cap companies that are rooted in Massachusetts have filed in districts outside of the District of Massachusetts. Please refer to **Exhibit 2**. Some notable examples include

Carematrix, General Cinemas, KB Toys, Polaroid, Filene's Basement II, Barzel Industries, Bradlees Department Stores, and Genuity, Inc. According to data compiled by the staff to the Committee, eight of these companies alone had nearly 30,000 employees and assets worth more than $9.6 billion.

WHY DOES IT MATTER THAT CASES FILE LOCALLY?

Each of the companies identified in the preceding section surely could have filed in the District of Massachusetts. They would have had proper venue under the existing statute, 11 U.S.C. sect. 1408. All of those companies had their corporate headquarters in Massachusetts at the time of filing. Most all of them had their principal assets in the state at the time of filing. But many of them were incorporated in, or had an affiliate in, another jurisdiction at the time they filed, thus their management and bankruptcy professionals had a choice. For a host of reasons that I will leave to the academic community, which has studied the issue closely for many years, those that select the place of filing, as well as those that counsel them, have chosen to file public company cases in jurisdictions other than the District of Massachusetts.

Let me be clear, the judges that have handled those cases are outstanding judges. They are experienced and dedicated to meeting the goals of the Bankruptcy Code in an open, fair and expeditious manner, and they have achieved those goals time and again. But, as I will discuss next, I believe the stakeholders in these cases would have achieved the same results in the District of Massachusetts. The difference is that if the cases had been filed in Massachusetts, the stakeholders, large and small, would have had an opportunity to participate in the proceeding. At a minimum, stakeholders would have received notices that told them that they *could* participate in the proceeding at a courthouse near where they live and work before a judge that lives in the same community as they do. This is to say there would have been the perception that their opportunity was real and accessible. And perception is often paramount.

The concept of "venue" informs courts regarding the placement of legal proceedings. Inherent in the judicial notion of venue is the concept that cases should be filed and determined in the place that is most convenient to the stakeholders, i.e., those that have an interest in that case. In most legal cases this means the convenience of two parties, a plaintiff and a defendant. In complex cases, venue considerations may

require the convenience of several parties. In those cases, the venue rules ensure that the case is brought in a place that takes into account the convenience of, and fairness to, the defendants that had no chance to select the forum. Significantly, in bankruptcy, because the entity that files forces all creditors, wherever they are located in the United States, to come to the forum the filer has chosen, the court may need to consider the convenience of hundreds or thousands of creditors. Venue focuses on the convenience of the parties because life-changing decisions occur in judicial proceedings, and those most affected by those decisions must have the right and capability, if they choose, to participate in those proceedings.

The bankruptcy venue rule as currently written, section 1408, turns these venue principles on their head. It focuses on the convenience of the debtor who alone chooses where to file its case, rather than on the convenience of the creditors who are forced to deal with the debtor at its chosen place of filing. In non-bankruptcy cases the law has developed that considerable deference is accorded to the plaintiff's choice of venue. Following the lead of such decisions, judges afford this same deference to the venue choice of bankruptcy debtors. See, e.g., In re: Enron Corp., 274 B.R. 327, 342 (S.D.N.Y. Bankr. 2002) ("[A] debtor's choice of forum is

entitled to great weight if venue is proper.") But that deference is wholly misplaced in bankruptcy because it is the debtor that drags the creditors to its chosen forum, not the other way around.

The ability of smaller stakeholders to attend proceedings, or at least to feel they could if they so desired, is central to their belief that they are being dealt with fairly. In consumer cases, I always allow pro se creditors to have their say in court. I always attempt to explain to them what is happening and why. In business cases I have the same policy, and often those with smaller claims and employees will ask their regular, trusted counsel to attend hearings to make known the views of their clients. Frequently, Bankruptcy Judges have to deliver rulings that are seen as bad news to these stakeholders. Jobs are lost and benefit promises, including those of pensions and healthcare, are broken. It is my experience that those who suffer these losses, while disappointed or worse, can accept it so long as they can see that the court made the decision after hearing all sides and that the decision was fair and compelled by existing law. Even if they decide not to attend the hearings, stakeholders know where the decisions are being made and by whom. If the case is filed in my session, they know

that all they need to do is to take an “Orange Line” train to State Street in Boston to get to the courthouse.

In short, although the Bankruptcy Code offers as one of its core values an “opportunity to be heard”, there is no true “opportunity “ if the case is pending in a courthouse that is hundreds or thousands of miles away.

THE QUALITY AND SOPHISTICATION OF THE MASSACHUSETTS BENCH

It has been suggested that the judges in the so-called “magnet” courts have developed a high level of expertise in dealing with large, public company Chapter 11 cases. Indeed, there is no doubt that much innovation in the processing and determination of large Chapter 11 cases has developed in those courts through the efforts of talented and dedicated judges. That is not to say, however, that the judges on the District of Massachusetts Bankruptcy bench are not also talented and dedicated. And, most importantly, the Massachusetts bench is typical of the bankruptcy bench nationwide.

The judges in Massachusetts have a combined sixty years of experience on the bench. Please refer to **Exhibit 3**. They include leaders in national bankruptcy organizations, such as the American Bankruptcy

Institute, the National Conference of Bankruptcy Judges, the American Law Institute and others. Indeed, the in-coming president of the National Conference of Bankruptcy Judges is a Massachusetts bankruptcy judge who sits in Boston. In recent years that most prominent leadership position has been occupied by judges from Nevada, Texas, Ohio and Oregon.

The Massachusetts bankruptcy judges have contributed to the development of bankruptcy law by writing hundreds of scholarly opinions as both bankruptcy court trial judges and as Bankruptcy Appellate Panel judges. They also have demonstrated a high level of scholarship and have produced some of the leading legal resources in bankruptcy practice and on the law of secured transactions. They teach at local law schools and are invited to lecture at programs both nationally and internationally. Before joining the bench, the Massachusetts judges were specialists in bankruptcy law, were leaders in their law firms both large and small, and in local bar associations. The judges also exhibited a high degree of business experience and acumen. Indeed, I served as a director of several public companies. To suggest that these judges could not provide the proper expertise to manage large Chapter 11 cases is, frankly, absurd.

The United States Bankruptcy Court for the District of Massachusetts has developed the tools needed to ensure the timely, efficient and effective disposition of large Chapter 11 cases. For many years, the court has had Local Rules of Bankruptcy Procedure to address the joint administration of related corporations. MLBR 1015-1. The Court adopted Case Management Procedures that offer the use of such procedures as omnibus hearing dates, notices of agenda, the payment of interim fees and expenses, and other matters typical in large Chapter 11 cases. MLBR 9009-2. Indeed, the Court has developed and adopted sample case management procedures. MLBR App. 6. In short, the Court has anticipated meeting the needs of large and complex cases.

Those that oppose the amendments to the venue statute have also stated that the "magnet" courts can ensure expedited determination of large Chapter 11 cases because they have the sophistication and experience to do so. The United States Courts collect data concerning the time from case opening to case closing of all Chapter 11 filings. The average time nationwide for opening and closing such cases is 13.9 months for the period from July 1, 2010 to June 30, 2011. In the District of Massachusetts the time from opening to closing Chapter 11 cases was 14

months during the same period. Although many cases involving large local companies are not filed in the District of Massachusetts, as is demonstrated above, Massachusetts is fifteenth in the United States for the number of Chapter 11 filings, so there is a sizeable population of Chapter 11 cases to study in the District of Massachusetts. These cases run the gamut from individual Chapter 11 cases to small operating companies and larger, mid-cap companies. Thus, the Massachusetts judges, with the support of an experienced Court Clerk and Clerk's Office staff, is able to process Chapter 11 cases at least at the national average for such cases. Finally, it emphasized that the size (in assets, claims or liabilities) of a Chapter 11 case does not necessarily reflect the complexity of the issues and challenges that the cases present. Thus, the data concerning the speed with which cases are resolved is, I believe, applicable to cases large and small.

Finally on this point, allow me to draw the Subcommittee's attention to a case to which I was assigned in the past year. On December 9, 2010, a publicly traded company called Molecular Insight Pharmaceuticals, Inc. filed a Chapter 11 petition in the District of Massachusetts. Please refer to **Exhibit 4**. Molecular was a Cambridge, Massachusetts based company that was developing a series of drugs for the treatment of cancer. The debtor

stated that it required expedited determination of its case because it had limited cash reserves and would need to shut down if it could not get through the Chapter 11 process in a few months. After presenting a series of "first day" motions that were decided almost immediately, the debtor began the process of negotiating a consensual plan with its principal lender. In the early phases of the case I was asked to decide a series of contested matters that helped the debtor achieve an agreement for emergence from bankruptcy. These steps were achieved through coordinated planning between the Clerk's Office and the interested parties to ensure timely adjudication of all necessary issues. In the end, the debtor achieved a confirmed Chapter 11 plan on May 5, 2011, less than six months after the case was filed. The point is that this local company that is developing important cancer fighting drugs achieved a timely and satisfactory result in its Chapter 11 case after filing in the District of Massachusetts.

THE PROPOSED AMENDMENTS SHOULD BE ADOPTED

Those who oppose the amendments to the current bankruptcy venue rule have argued that there is no need for the amendments because of section 1412, which provides for the transfer of venue when to do so would accommodate the convenience of the parties and the interests of justice

and fairness. But section 1412 is often ineffective. First and foremost, it is very expensive to litigate a motion for a change of venue. Only the most well-heeled parties in interest are able to support such a motion, and they are the least likely to seek a change in venue. It is the small vendor, the former employee, or the pensioner that may desire a change in venue, but they cannot afford the litigation for the same reasons they cannot afford to participate in the proceeding at a remote "magnet" district. Second, as noted above, because there is a strong presumption in favor of the forum chosen by the debtor it is very difficult to carry the burden of persuading the Court to change venue. Finally, many parties that may wish to seek a change in venue will be reluctant to do so because the same court that decides that motion will handle the case in the likely event that the motion is denied.

The current venue statute is an historical anomaly. The large cases of an earlier time were principally railroad reorganization cases. Those cases were governed by a railroad receivership provision in the original 1898 Bankruptcy Act and railroads were limited to filing in the state of the railroad's principal place of business or principal assets. Skeel, 1 Del. L. Rev. 1, 8-9 (1998). Later, when the Act was rewritten in 1934, Chapter X, which

governed bankruptcy cases for publicly held companies, also limited filings to the place where the public company had its principal place of business or assets. Thus, the current proposed amendments merely return the venue requirements for public companies to those that had been established for many years.

Those in opposition to the amendments seem to think that Congress intended to create, through the current venue statute, certain national bankruptcy courts for the disposition of large public company cases. There is nothing in the language of the statute or, to my knowledge, the legislative history, to support such a reading. Indeed, Congress knows how to confer national jurisdiction on a court when it feels that consistency and uniformity are a sufficient basis to do so. That is the reason for a national court for patent appeals. Certainly it cannot be argued seriously that Congress intended by the current venue statute to create such a court for large Chapter 11 bankruptcy cases. To the contrary, there is much to be said for the development of innovative case management techniques and legal interpretations from bankruptcy judges around the nation, a goal that will be served by the proposed amendments.

CONCLUSION

At the very heart of the concept of venue is the idea that those affected by a court proceeding should have access to the proceeding. Whether access means an actual ability to attend the hearings, the ability of the local press to follow the proceedings first hand and then to pass on developments to the local population, or the perception that the events in the case are occurring in the court with the most ties to all constituencies, the important goal of judicial transparency is served by the proposed amendments.

Thank you very much for the opportunity to provide to the Subcommittee my views on this important legislation.