

# A Road Map for Bankruptcy Litigation

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By Scott A. Wolfson

## Introduction

A litigator's fundamental skill set is portable from state and federal district courts to the bankruptcy court. However, successfully litigating bankruptcy-related matters also requires knowledge of the jurisdictional and procedural nuances unique to bankruptcy litigation. The consequences of being unfamiliar with concepts like "bankruptcy counting" can be severe—from inadvertent waiver of jury trial rights to missing a response deadline. The goal of this article is to provide practitioners with an overview of important bankruptcy litigation statutes and rules and to highlight potential pitfalls.

## Bankruptcy Court Jurisdiction

The jurisdictional scheme governing bankruptcy courts is complicated by the fact that bankruptcy judges are not Article III judges, but Article I judges. As a result of the U.S. Supreme Court's decision in *Northern Pipeline Constr Co v Marathon Pipe Line Co*,<sup>1</sup> which struck down a broad grant of jurisdiction to the bankruptcy courts, bankruptcy courts are courts of limited jurisdiction that derive their jurisdiction from the district courts.<sup>2</sup>

District courts are granted "original and exclusive jurisdiction of all cases under title 11" by 28 USC § 1334(a).<sup>3</sup> A "case" under title 11 means a bankruptcy action commenced with the filing of a bankruptcy petition.<sup>4</sup> Additionally, district courts are vested with "original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11" by 28 USC § 1334(b).<sup>5</sup>

Whether a bankruptcy court can enter final orders with respect to a particular proceeding depends upon the jurisdictional category into which the proceeding falls and whether the proceeding is "core" under 28 USC § 157.<sup>6</sup>

### *Arising in or Under Title 11 - "Core" Proceedings*

Proceedings that arise in a case under title 11 are those that, by their very nature, could arise only in a bankruptcy case.<sup>7</sup> For example, an action to appoint a trustee under section

1104 to investigate the financial condition of a debtor could only arise in a bankruptcy case.

The phrase "arising under title 11" describes those proceedings that involve a cause of action created or determined by a statutory provision of title 11.<sup>8</sup> A common example of a cause of action created by title 11 would be an action under section 547 to avoid a preferential transfer.

Bankruptcy judges may hear and determine all cases under title 11 and all "core proceedings" arising under title 11 or arising in a case under title 11.<sup>9</sup> Courts in the Sixth Circuit appear to consider all proceedings that arise under or arise in a case under title 11 to be core proceedings.<sup>10</sup>

### *Related to a Case Under Title 11 - "Non-Core" Proceedings*

The standard for determining whether a case is related to a bankruptcy case is very liberal. A case is generally held to be related to a case under title 11 if its outcome could "conceivably" have any effect on the debtor's estate.<sup>11</sup> A proceeding does not even have to be against the debtor or the debtor's property to satisfy the requirements of related to jurisdiction.<sup>12</sup>

The related to category encompasses all matters which may be placed in the arising under or arising in categories. "Therefore, for purposes of determining section 1334(b) jurisdiction, it is necessary only to determine whether a matter is at least 'related to' the bankruptcy."<sup>13</sup>

Related to actions are non-core proceedings. The bankruptcy judge's findings of fact and conclusions of law in a "related to" action are subject to objection by the parties under Federal Rule of Bankruptcy Procedure (Bankruptcy Rules) 9033(b) and *de novo* review by the district court judge, unless the parties have consented to the entry of final orders or judgment by the bankruptcy judge.<sup>14</sup>

## The Bankruptcy Court's Abstention from Hearing State Law Causes of Action

Bankruptcy courts must abstain from hearing certain cases.<sup>15</sup> Mandatory abstention under section 1334(c)(2) applies if the following six

requirements are satisfied: (1) a motion to abstain is timely filed; (2) the proceeding is “based upon a State law claim or State law cause of action;” (3) the claim or cause of action is related to a bankruptcy case but did not arise in or under the bankruptcy case; (4) the only basis for original jurisdiction in federal court is the bankruptcy filing; (5) the state law claim or cause of action is the subject of “an action [that] is commenced...in a State forum of appropriate jurisdiction;” and (6) the state court action “can be timely adjudicated.”<sup>16</sup> Where a bankruptcy court determines that it must abstain from a case, the proceeding is remanded to the state court where it was initially pending.

Even where a bankruptcy court has jurisdiction over a case because it arises in or under title 11 or is related to a case under title 11, the bankruptcy court may abstain from hearing the case under 28 USC § 1334(c)(1) “in the interest of comity with State courts or respect for State law....” This is known as “permissive abstention.” Bankruptcy courts have listed over a dozen non-exclusive factors as relevant to determining whether abstaining from hearing a state law cause of action is appropriate.<sup>17</sup>

### “Removal” – Transferring a State Court Case to Bankruptcy Court

Section 1452 of title 28 permits a party to remove a claim or cause of action to the bankruptcy court where the bankruptcy court has jurisdiction under 28 USC § 1334.<sup>18</sup> The liberal bankruptcy jurisdiction rules under 28 USC § 1334(b)—that a bankruptcy court has jurisdiction over a claim “arising in or related to cases under title 11”—means that removal should be permitted where the case could conceivably have any effect on the debtor’s estate.<sup>19</sup> There is no requirement in section 1452 that the debtor be a party to the case being removed.

Removal is accomplished by filing a “notice of removal” “with the clerk for the district and division within which is located the state or federal court where the civil action is pending.”<sup>20</sup> For example, removing a case filed in the Kent County, Michigan Circuit Court that is related to a pending bankruptcy in Detroit’s Eastern District of Michigan would require filing a notice of removal and a motion to transfer venue to the bankruptcy court in Detroit with the bankruptcy court for the Western District of Michigan in Grand Rapids, as well as a copy of the notice of re-

moval with the clerk of the Kent County Circuit Court.<sup>21</sup> Bankruptcy Rule 9027 outlines the requisite contents of a notice of removal and the procedure and time for filing the notice.

### Adversary Proceedings

Adversary proceedings are lawsuits within the bankruptcy case commenced by filing a complaint.<sup>22</sup> Part VII (Rules 7001-7087) of the Bankruptcy Rules contains most of the rules governing adversary proceedings.<sup>23</sup> Bankruptcy Rules 7001 through 7087 generally incorporate the Federal Rules of Civil Procedure. For example, Bankruptcy Rule 7003 simply states, “Rule 3 F.R.Civ.P. applies in adversary proceedings.” However, some of the Bankruptcy Rules differ from the Federal Rules of Civil Procedure, with the modifications ranging from slight to dramatic. Bankruptcy Rule 7001 lists proceedings that are adversary proceedings. Those proceedings are:

- to recover money or property, with several exceptions;
- to determine the validity, priority, or extent of a lien or other interest in property;
- to obtain approval for the sale of both the interest of the estate and of a co-owner in property;
- to object to or revoke a discharge;
- to revoke an order of confirmation of a chapter 11, 12, or 13 plan;
- to determine the dischargeability of a debt;
- to obtain an injunction or other equitable relief;
- to subordinate any allowed claim or interest;
- to obtain a declaratory judgment relating to any of the foregoing; and
- to determine a claim or cause of action removed under 28 USC § 1452.

Additionally, an objection to a claim that includes a demand for relief of the kind specified in Bankruptcy Rule 7001 is an adversary proceeding.<sup>24</sup>

A common mistake non-bankruptcy practitioners make is seeking relief of the type specified in Bankruptcy Rule 7001 by motion rather than by filing a complaint. Because adversary proceedings must be commenced by filing a complaint, they get case numbers separate from the underlying bankruptcy case and are docketed separately. The cap-

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**“Corporate Ownership Statement”****Requirement in Adversary Proceedings**

Bankruptcy Rule 7007.1 requires that any corporation that is a party to an adversary proceeding must file “a statement that identifies any corporation...that directly or indirectly owns 10% or more of any class of the corporation’s equity interests....”<sup>35</sup> This statement must be filed by a party with its first filing and must be updated to reflect any subsequent change in circumstances.<sup>36</sup> The purpose of this filing is to assist bankruptcy judges in making informed disqualification decisions.<sup>37</sup>

**Pleading**

Bankruptcy Rule 7008 incorporates Rule 8 of the Federal Rules of Civil Procedure, but includes a requirement that the claim “shall contain a statement that the proceeding is core or non-core and, if non-core, that the pleader does or does not consent to entry of final orders or judgment by the bankruptcy judge.”<sup>38</sup>

**Answer**

Bankruptcy Rule 7012 incorporates some, but not all of Rule 12 of the Federal Rules of Civil Procedure, and provides that a defendant must serve an answer within 30 days after the *issuance* of the summons.<sup>39</sup>

**Counting Days in Bankruptcy**

Litigating in bankruptcy court may require re-learning how to count “days.” Many a seasoned federal court litigator, familiar with the nuances of computing time under Rule 6 of the Federal Rules of Civil Procedure, has been late with a filing as a result of Bankruptcy Rule 9006. That rule, unlike its Rule 6 counterpart, provides that intermediate Saturdays, Sundays, and legal holidays are excluded in the computation of a time-period when the period is *less than 8 days*.<sup>40</sup> Rule 6 of the Federal Rules of Civil Procedure contains identical language to Bankruptcy Rule 9006, but provides an 11-day cutoff for the special counting.<sup>41</sup> State court litigators are often unaware that every day may not count as a day in calculating a response period.

Another wrinkle in the time calculation, also contained in Bankruptcy Rule 9006, applies most commonly where service is by mail. In certain circumstances, service by mail (including electronic mail) results in an additional three days being added to a time to respond.<sup>42</sup>

The Committee on Rules of Practice and Procedure of the Judicial Conference of the United States has created a Time-Computation Subcommittee to examine the time-computation provisions found in the federal appellate, bankruptcy, civil, and criminal rules “with a view to simplifying those provisions and eliminating inconsistencies among them.”<sup>43</sup> “The project was launched in response to frequent complaints by practitioners about the time, energy and nervous anxiety expended in calculating time periods and to comments by judges about the anomalous results of the current computation system.”<sup>44</sup> As of the writing of this article, the Time-Computation Subcommittee was seeking comments on proposed amendments to time-computation rules. For now, a “day” is not necessarily a “day.”

**Jury Trial Rights and Waiver**

The right to a trial by jury under the Seventh Amendment fully applies to bankruptcy proceedings that are legal, as opposed to equitable in nature, regardless of whether the proceeding is core or non-core.<sup>45</sup> Bankruptcy Rule 9015 incorporates a number of Federal Rules of Civil Procedure pertaining to jury trials, including Rule 38, and provides that the parties may consent to have the bankruptcy judge conduct the jury trial.<sup>46</sup> Local rules of bankruptcy procedure often provide detailed procedures and time lines for demanding that an Article III district court judge conduct the jury trial rather than the Article I bankruptcy judge.<sup>47</sup>

The largest trap for the unwary is that the right of a bankruptcy litigant to a jury trial is *waived* if the party has filed a proof of claim in the bankruptcy court. The reasoning behind the rule is that the filing of a claim initiates the process of allowing and disallowing claims, such that the filer is deemed to have submitted to the equitable powers of the bankruptcy court.<sup>48</sup>

**Conclusion**

Procedural hazards abound in bankruptcy litigation. Successfully litigating bankruptcy matters requires a keen awareness of bankruptcy-specific statutes, rules of procedure, and, oftentimes, case-specific orders.

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## NOTES

1. 458 US 50 (1982).
2. See *In re Granger Garage, Inc.*, 921 F2d 74, 77 (6th Cir 1990) (“The bankruptcy court is a court of limited jurisdiction.”). Bankruptcy judges for each circuit are appointed by the United States court of appeals for that circuit. 28 USC § 152. “[Bankruptcy courts] do not operate under an exclusive grant of jurisdiction as in § 1471(c) but rather derive their jurisdiction from the district courts . . . .” *White Motor Corp v Citibank NA*, 704 F2d 254, 263 (6th Cir 1983).
3. Emphasis added.
4. The Sixth Circuit Court of Appeals defined a “title 11 case” in *Stewart v Henry (In re Stewart)*, 62 Fed Appx 610, 613 (6th Cir 2003) as “containing a claim made under an actual provision of title 11. \* \* \* In other words, the claim itself must invoke a provision of title 11. \* \* \* [A]n action commenced in a federal district court or bankruptcy court with the filing of a petition pursuant to 11 U.S.C. §§ 301, 302 or 303.” (internal citation and quotation omitted.)
5. Emphasis added.
6. Section 157(b)(2) of title 28 contains a non-exclusive list of core proceedings.
7. *Mich Empl Sec Comm’n v Wolverine Radio Co (In re Wolverine Radio Co)*, 930 F2d 1132, 1144 (6th Cir 1991).
8. *Id.*
9. 28 USC § 157(b)(1).
10. See *Eglinton v Loyer (In re GAD, Inc)*, 340 F3d 331, 336 (6th Cir 2003) (a “core proceeding” is one that “invokes a substantive right created by federal bankruptcy law or one which could not exist outside of the bankruptcy.”); *Lowenbraun v Canary (In re Lowenbraun)*, 453 F3d 314 (6th Cir 2006).
11. *Lindsey v O’Brien (In re Dow Corning Corp)*, 86 F3d 482, 489-90 (6th Cir 1996).
12. *Id.* (holding that claims asserted against a non-debtor defendant that had the potential to result in the debtor’s liability for indemnification were sufficiently related to the bankruptcy to warrant jurisdiction in federal court).
13. *8300 Newburgh Rd Partnership v Time Constr (In re Time Constr)*, 43 F3d 1041, 1044 (6th Cir 1995), quoting *Mich Empl Sec Comm’n v Wolverine Radio Co*, 930 F2d at 1141 (emphasis added).
14. See 28 USC § 157(c) and Bankruptcy Rules 7008 and 9033(d).
15. Section 1334(c)(2) of 28 USC provides:  
Upon timely motion of a party in a proceeding based upon a State law claim or State law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a State forum of appropriate jurisdiction.
16. *In re K-Mart Corp*, 307 BR 586, 591 (Bankr ED Mich 2004).
17. (1) the effect or lack of effect on the efficient administration of the estate if a court abstains;  
(2) the extent to which state law issues predominate over bankruptcy issues;  
(3) the difficulty or unsettled nature of the applicable state law;  
(4) the presence of a related proceeding commenced in state court or other non-bankruptcy court;  
(5) the jurisdictional basis, if any, other than 28 U.S.C. § 1334;
- (6) the degree of relatedness or remoteness of the proceeding to the main bankruptcy case;
- (7) the substance rather than form of an asserted “core” proceeding;
- (8) the feasibility of severing state law claims from core bankruptcy matters to allow judgments to be entered in state court with enforcement left to the bankruptcy court;
- (9) the burden [on the bankruptcy court’s] docket;
- (10) the likelihood that the commencement of the proceeding in bankruptcy court involves forum shopping by one of the parties;
- (11) the existence of a right to jury trial;
- (12) the presence in the proceeding of non-debtor parties; and
- (13) any unusual or other significant factors.  
See *K-Mart*, 307 BR at 596-97 (citations omitted).
18. Section 1452(a) provides:  
A party may remove any claim or cause of action in a civil action other than a proceeding before the United States Tax Court or a civil action by a governmental unit to enforce such governmental unit’s police or regulatory power, to the district court for the district where such civil action is pending, if such district court has jurisdiction of such claim or cause of action under section 1334 of this title.  
Although 28 USC § 1452 expressly addresses the district court, a district court may refer all cases and proceedings that fall within 28 USC § 1334 to the bankruptcy court. 28 USC § 157(a). Although this power is discretionary, “courts ‘routinely refer’ most bankruptcy cases to the bankruptcy court.” *In re Resorts Int’l, Inc*, 372 F3d 154, 162 (3d Cir 2004).
19. See *Lindsey v O’Brien (In re Dow Corning Corp)*, 86 F3d at 489-90.
20. Bankruptcy Rule 9027(a)(1).
21. Bankruptcy Rule 9027(c).
22. Bankruptcy Rule 7003.
23. Bankruptcy Rule 7001 states that “[a]n adversary proceeding is governed by the rules of this Part VII.”
24. Bankruptcy Rule 3007.
25. Notes of Advisory Committee on Rule 9014 (1983) (emphasis added).
26. 11 USC § 101 et seq.
27. For example, see Local Rule 9014-1 of the Bankruptcy Court for the Eastern District of Michigan.
28. See Bankruptcy Rule 4001(a)(1).
29. Bankruptcy Rule 9014(c) incorporates Bankruptcy Rules 7028-7037.
30. Bankruptcy Rule 9014(d).
31. See, e.g., Delphi’s Claim Objection Procedures Order, United States Bankruptcy Court for the Southern District of New York, Case No. 05-44481 (Docket No. 6089).
32. See Bankruptcy Rule 9017.
33. For example, service on an insured depository institution must be by certified mail. Bankruptcy Rule 7004(b) and (h). In addition, personal service of a subpoena is required by Bankruptcy Rule 9016, which provides that Federal Rule of Civil Procedure 45 applies in cases under the Bankruptcy Code.
34. Bankruptcy Rule 9014(b) makes Bankruptcy Rule 7004 applicable to contested matters.
35. Bankruptcy Rule 7007.1(a).
36. Bankruptcy Rule 7007.1(b).
37. See Bankruptcy Rule 7007.1 Advisory Committee Note – 2003 Amendment.
38. Bankruptcy Rule 7008(a).

39. Bankruptcy Rule 7012(a). Bankruptcy Rule 7004(e) requires that the complaint be served within ten days of its issuance.

40. Bankruptcy Rule 9006(a) states: "When the period of time prescribed or allowed is less than 8 days, intermediate Saturdays, Sundays, and legal holidays shall be excluded in the computation."

41. Fed R Civ P 6.

42. "When there is a right or requirement to act or undertake some proceedings within a prescribed period after service and that service is by mail or under Rule 5(b)(2)(C) or (D) F. R. Civ. P., three days are added after the prescribed period would otherwise expire under Rule 9006(a)." Bankruptcy Rule 9006(f).

43. June 29, 2007 Memorandum from the Time-Computation Subcommittee to Judge David F. Levi and the Standing Committee on Rules of Practice and Procedure, p 1.

44. *Id.* (footnote omitted).

45. See *Granfinanciera, SA v Nordberg*, 492 US 33, 41-42 and 60-91 (1989).

46. Bankruptcy Rule 9015 provides:

(a) Applicability of Certain Federal Rules of Civil Procedure. Rules 38, 39, and 47-51 F.R.Civ.P., and Rule 81(c) F.R.Civ.P. insofar as it applies to jury trials, apply in cases and proceedings, except that a demand made pursuant to Rule 38(b) F.R.Civ.P. shall be filed in accordance with Rule 5005.

(b) Consent to Have Trial Conducted by Bankruptcy Judge. If the right to a jury trial applies, a timely demand has been filed pursuant to Rule 38(b) F.R.Civ. P., and the bankruptcy judge has been specially designated to conduct the jury trial, the parties may consent to have a jury trial conducted by a bankruptcy judge under 28 U.S.C. § 157(e) by jointly or separately filing a statement of consent within any applicable time limits specified by local rule.

47. See, e.g., Local Rule 9015-1 of the Eastern District of Michigan:

A party who demands a jury trial shall be deemed to have consented to the bankruptcy judge conducting the jury trial unless, concurrently with the filing of the jury demand, the demanding party files a motion to withdraw the reference. The other party or parties shall have 10 days after the service of a jury demand to file a motion to withdraw the reference; otherwise the non-demanding party shall be deemed to have consented to a jury trial conducted by the bankruptcy judge.

48. See *Granfinanciera, SA v Nordberg*, 492 US at 51-57.



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