Supreme Court Upholds Limited Bankruptcy Court Jurisdiction Over Defendants in Fraudulent Transfer Actions; Leaves an Open Door to Constitutional Challenges When Parties Face a Trial in Bankruptcy Court

On June 9, 2014, the Supreme Court issued a decision in *Executive Benefits Insurance Agency v. Arkison*, a case that tested the extent of the jurisdiction of bankruptcy court judges to decide fraudulent transfer and certain other claims against non-debtors. Ropes & Gray LLP represented the petitioner in obtaining certiorari and in the Supreme Court proceedings.

Executive Benefits resolved a question left open by the Supreme Court's 2011 *Stern v. Marshall* decision, which held that Congress violated Article III of the Constitution when it assigned bankruptcy judges, who are not Presidentially appointed and lack life tenure, authority to enter final judgment in certain "core claims" against non-debtors. In *Executive Benefits*, the Court held that when bankruptcy courts address fraudulent transfer or other "*Stern*-governed core claims" for which they cannot enter final judgment under *Stern v. Marshall*, the bankruptcy court may instead treat the claims as statutory "non-core" claims and hear pretrial motions and issue proposed findings of fact and conclusions of law. The *Executive Benefits* opinion instructs district courts to review these proposed findings and conclusions in *Stern*-governed claims "*de novo*" before entering final judgment. Significantly, the Court's emphasis on the district court's *de novo* review raises questions about how district courts should proceed when they address bankruptcy court orders, or aspects of those orders, that would typically be reviewed more deferentially on appeal.

The Supreme Court sidestepped constitutional questions presented in the *Executive Benefits* case about whether and when bankruptcy judges may enter final judgment based on consent of the parties, where jurisdiction would otherwise be lacking under Article III in light of *Stern*. Instead, the Court held that the appellant's constitutional Article III rights were satisfied when a district court entered judgment upholding a bankruptcy court's legal conclusions following *de novo* review. In basing its ruling on the *district court*'s constitutional authority to enter final judgment, the Supreme Court expressly reserved for another day questions concerning whether and what manner of party consent might confer constitutional authority for bankruptcy courts to enter enforceable final judgments.

Going forward, the *Executive Benefits* decision will allow bankruptcy courts to continue the practice of hearing summary judgment or other dispositive pre-trial motions on *Stern*-governed claims and proposing conclusions of law for district court consideration.

At the same time, the opinion applies only to judgments reviewed by the district court *de novo*. This appears to open the door to constitutional challenges where a bankruptcy court conducts a trial. The *Executive Benefits* decision thus gives parties sued for commercial contract or fraudulent transfer claims by bankruptcy estates in bankruptcy court—a common occurrence—additional ability to demand withdrawal of trials on those claims to district court.

The Supreme Court's express reservation of the constitutional question may mean that the issue will come before the Court again soon, perhaps in a case in which the factual findings of a bankruptcy judge, or of a magistrate judge, were given deference under a "clearly erroneous" standard of review.

To find out how the Supreme Court decision in *Executive Benefits* affects your interest, please contact your usual Ropes & Gray attorney or one of the Ropes & Gray attorneys listed below.

Douglas Hallward-Driemeier
D. Ross Martin
Mark I. Bane