No. 13-935

IN THE

Supreme Court of the United States

WELLNESS INTERNATIONAL NETWORK, LIMITED, *et al.*,

Petitioners,

v.

RICHARD SHARIF,

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SEVENTH CIRCUIT

BRIEF OF CERTAIN *TOUSA* DEFENDANTS AS *AMICI CURIAE* IN SUPPORT OF RESPONDENT

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QUESTIONS PRESENTED

This Court held in *Stern v. Marshall*, 131 S. Ct. 2594 (2011), that non-Article III bankruptcy courts cannot finally adjudicate certain claims despite their designation as "core" under 28 U.S.C. § 157. The petition for writ of certiorari in this case presents the question whether litigants nevertheless may consent to the exercise of such authority by bankruptcy courts and, if so, whether such consent may be implied by their conduct. *Amici* will address the following two questions:

1. Whether "implied consent" to the exercise of authority barred by *Stern* is sufficient in light of Federal Rule of Bankruptcy Procedure 7012(b)'s requirement that in non-core proceedings bankruptcy courts can enter final orders and judgments only with the express consent of the parties; and

2. Whether "implied consent" to the exercise of authority barred by *Stern* can be derived solely from the fact that the litigants did not expressly challenge the bankruptcy court's authority before *Stern* was decided.

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STATEMENT OF INTEREST OF THE *AMICI CURIAE*

The *amici curiae* are members of a group of defendants referred to as the "Transeastern Lenders" in a case currently pending before the United States District Court for the Southern District of Florida, *3V Capital Master Fund Ltd. v. Official Committee of Unsecured Creditors of TOUSA, Inc. (In re TOUSA, Inc.)*, Case No. 10-62035-CIV-Moore (the "TOUSA Litigation").[1] The TOUSA Litigation began in July 2008 when the Official Committee of Unsecured Creditors (the "Committee") of TOUSA, Inc. ("TOUSA"),[2] a Florida homebuilder that filed for bankruptcy protection in January 2008, filed an adversary proceeding against the Transeastern Lenders and two other groups of defendants on behalf of certain TOUSA subsidiaries. The Committee alleged, *inter alia*, that certain transfers made by the TOUSA subsidiaries were fraudulent transfers under 11 U.S.C. §§ 544, 548, and Florida and New York law. (*See* Case No. 08-01435-JKO, ECF No. 243.) The bankruptcy court issued a purported

1. All parties have been timely notified of the undersigned's intent to file this brief; both petitioners and respondent have consented to the filing of this brief. Respondent has filed with the Court a letter consenting to the filing of *amicus curiae* briefs in support of either or neither party. A copy of petitioners' consent is filed herewith. No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amici curiae* or their counsel made a monetary contribution to its preparation or submission. The *amici curiae* are identified in the attached appendix.

2. The Committee is the predecessor of the current appellee the Liquidation Trustee.

final judgment in favor of the Committee against the Transeastern Lenders (and other defendants), but the district court, reviewing legal determinations *de novo* and findings of fact under a clear error standard, "quashed" the judgment and found the Transeastern Lenders not liable. *See generally In re TOUSA, Inc.*, 422 B.R. 783 (Bankr. S.D. Fla. 2009); *In re TOUSA, Inc.*, 444 B.R. 613 (S.D. Fla. 2011). The Committee appealed the district court's decision to the Eleventh Circuit.

This Court decided *Stern* six days after the Transeastern Lenders submitted their opposition brief before the Eleventh Circuit. Although the Transeastern Lenders filed a letter pursuant to Federal Rule of Appellate Procedure 28(j) advising the court of *Stern* prior to scheduling of oral argument, the Eleventh Circuit reviewed the bankruptcy court's judgment using a deferential standard as though it were a final judgment. The Eleventh Circuit made no mention of *Stern* in its decision. The Eleventh Circuit affirmed the bankruptcy court judgment as to liability and remanded the case to the district court to review the bankruptcy court's remedial scheme. *See In re TOUSA, Inc.*, 680 F.3d 1298, 1316 (11th Cir. 2012). The Eleventh Circuit stated that it was reviewing the bankruptcy court's judgment "independently of the district court," reviewing the bankruptcy court's factual findings for clear error and its equitable determinations for abuse of discretion. *Id.* at 1310 ("The factual findings of the bankruptcy court are not clearly erroneous unless . . . we are left with the definite and firm conviction that a mistake has been made. Neither the district court nor this Court is authorized to make independent factual findings; that is the function of the bankruptcy court.") (internal citations and quotation

marks omitted). The Transeastern Lenders subsequently filed a petition for rehearing, again raising the issue of *Stern*'s applicability to the TOUSA Litigation. The Eleventh Circuit denied the petition without comment.

This Court's decisions in *Stern* and *Executive Benefits Insurance Agency v. Arkison*, 134 S. Ct. 2165 (2014) ("*Executive Benefits*"), clearly affect a bankruptcy court's ability to finally adjudicate fraudulent transfer claims against defendants like the Transeastern Lenders—defendants that (except for one former Transeastern Lender that since settled its liability) did not file proofs of claim against the bankruptcy estates. Such defendants have a right to Article III adjudication of the claims asserted against them. The bankruptcy court may enter proposed findings of fact and conclusions of law to be reviewed by the district court *de novo*, but the bankruptcy court does not have authority to enter a final judgment on those claims. Accordingly, under the standard recently articulated by this Court, the district court decision reviewing the bankruptcy court's order should have been the final judgment in the TOUSA Litigation,[3] and the Eleventh Circuit should have reviewed that decision with deference. It should not have reviewed the bankruptcy court order "independently" of the district court judgment.

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3. By finding that the bankruptcy court's factual findings were clearly erroneous, the district court necessarily would have reached the same conclusion if it had exercised its own independent judgment as to the factual record, as *Executive Benefits* requires. Stated differently, the district court's findings and judgment of no liability for the Transeastern Lenders would have necessarily been the same if the district court had reviewed the bankruptcy court judgment *de novo* rather than deferentially.

The Transeastern Lenders agree with respondent that litigants cannot consent to the adjudication of a private right by a non-Article III court (*see* Resp. Br. at 39-49),[4] but submit this brief to address two discrete issues: (1) whether, assuming *arguendo* that a party can consent to adjudication of a private right by an Article III court, such consent must be express; and (2) whether, assuming this Court finds that consent could be either express or implied, such consent can be implied from the mere fact that a litigant did not argue, prior to this Court's decision in *Stern*, that the bankruptcy court's exercise of final adjudicative authority expressly provided for in the Bankruptcy Code was unconstitutional.

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4. *See also Commodity Futures Trading Comm'n v. Schor*, 478 U.S. 833, 850-51 (1986) (stating that "Article III, § 1 safeguards the role of the Judicial Branch" and prevents "the encroachment or aggrandizement of one branch at the expense of the other" and "[t]o the extent that this structural principle is implicated in a given case, the parties cannot by consent cure the constitutional difficulty for the same reason that the parties by consent cannot confer on federal courts subject-matter jurisdiction beyond the limitations imposed by Article III"); *Waldman v. Stone*, 698 F.3d 910, 918 (6th Cir. 2012) ("Waldman's objection [that the bankruptcy court lacked constitutional authority to enter judgment] thus implicates not only his personal rights, but also the structural principle advanced by Article III. And that principle is not Waldman's to waive."), *cert. denied*, 133 S. Ct. 1604 (2013); *BP RE, L.P. v. RML Waxahachie Dodge, L.L.C. (In re BP RE, L.P.)*, 735 F.3d 279, 286 (7th Cir. 2013) (adopting "the compelling and thorough reasoning of *Waldman*, which held that parties cannot consent to such circumvention of Article III that impinges on the structural interests of the Judicial Branch."), *reh'g en banc denied*, 744 F.3d 1371 (7th Cir. 2014).

INTRODUCTION AND SUMMARY OF THE ARGUMENT

The Seventh Circuit held below that, under this Court's decision in *Stern*, bankruptcy courts do not have the authority to enter final judgments on alter-ego claims. *Wellness Int'l Network, Ltd. v. Sharif*, 727 F.3d 751, 775-76 (7th Cir. 2013) ("*Wellness*"), Pet'r's. App. 51a. The court further held that "a constitutional objection based on *Stern* is not waivable because it implicates separation-of-powers principles." *Id.* at 755, Pet'r's. App. 3a. If this Court were to reverse the Seventh Circuit's holding that a constitutional objection based on *Stern* is not waivable, the Court nevertheless should hold that only express consent, rather than implied consent, is sufficient to confer jurisdiction on a bankruptcy court to enter final judgment on a *Stern* claim.

The *Executive Benefits* Court held that a *Stern* claim should be treated as non-core under 28 U.S.C. § 157(c). 134 S. Ct. at 2173. In non-core proceedings, under Federal Rule of Bankruptcy Procedure 7012(b), express consent of the parties is required to confer jurisdiction on the bankruptcy court to enter a final judgment. The Advisory Committee notes to Federal Rules of Bankruptcy Procedure 7012(b) and 7008 reiterate that consent must be express. The Ninth Circuit erred in holding to the contrary in *Executive Benefits*. Relying on this Court's decision in *Roell v. Withrow*, 538 U.S. 580 (2003), the Ninth Circuit held that Rules 7008 and 7012 do not preclude a finding of implied consent. *See Exec. Benefits Ins. Agency v. Arkison (In re Bellingham Ins. Agency)*, 702 F.3d 553, 568-69 (9th Cir. 2012) ("*Bellingham*"). But *Roell* is inapplicable. In *Roell*, this Court held that with regard

to 28 U.S.C. § 636(c)(1), which provides that a magistrate judge may enter a final order where designated to do so by the district court "upon the consent of the parties," a court may "accept implied consent where . . . the litigant or counsel was made aware of the need for consent and the right to refuse it, and still voluntarily appeared to try the case before the Magistrate Judge." *Roell*, 538 U.S. at 590. The Ninth Circuit was mistaken in extending the reasoning of *Roell* to *Bellingham* for three reasons. First, *Roell* held that as a matter of *statutory* construction implied consent may satisfy § 636(c)(1). Second, *Roell* did not address or interpret the Bankruptcy Code or Federal Rules of Bankruptcy Procedure. Third, the *Roell* Court warned that consent should only be implied in limited, exceptional circumstances such as those in the case.

The United States, as *amicus curiae* supporting petitioners, has suggested that respondent knowingly waived his constitutional right by asking the bankruptcy court—prior to the decision in *Stern*—to rule on the alter-ego claim. The United States argued that such action, although not express, constituted knowing waiver because "the principal building blocks of *Stern*'s reasoning were contained in the Court's 1989 decision in *Granfinanciera*, which is why the parties in *Stern* had been litigating about the question for more than a decade." (Br. of United States as *Amicus Curiae* in Supp. of Pet'r at 30-31, *Wellness Int'l Network, Ltd. v. Sharif*, 134 S. Ct. 2901 (2014) (No. 13-935) ("United States Br.").) Even if this Court were to conclude that consent can be implied, the Court should hold that Sharif's failure to raise a *Stern* objection before *Stern* was decided did not constitute consent. Under this Court's precedents, and as a matter of common sense and fairness, the failure to assert a right before the law recognizes such right cannot be considered a knowing

and intelligent waiver of that right. Before *Stern*, Sharif was litigating in the face of a statute that unambiguously stated that the bankruptcy court had authority to enter a final judgment. He had no reasonable basis on which to object. Sharif did not knowingly consent to the bankruptcy court's exercise of unlawful authority by failing to raise an argument that contradicted existing statutory law prior to this Court's decision in *Stern*. The failure to assert a presently-nonexistent right cannot be a knowing waiver of that right.

ARGUMENT

I. A Litigant's Consent To A Bankruptcy Court Entering Final Judgment On A Private Right Claim Must Be Express

If this Court were to reverse the Seventh Circuit and hold that a party can consent to a bankruptcy court entering final judgment on a private right claim, which it should not do, it should make clear that such consent must be express and cannot be implied.

A. A Bankruptcy Court Cannot Enter A Final Judgment In A Non-Core Proceeding Without Express Consent Of The Parties

In *Executive Benefits*, this Court held that 28 U.S.C. § 157 "permits *Stern* claims to proceed as non-core within the meaning of § 157(c)." 134 S. Ct. at 2173. The Bankruptcy Code provides that, for non-core proceedings, "the consent of all the parties to the proceeding" is required before the district court can refer a non-core proceeding to the bankruptcy court to enter a final judgment. 28 U.S.C. § 157(c)(2). The Federal Rules of Bankruptcy Procedure

clarify that the consent must be express: "in non-core proceedings final orders and judgments shall not be entered on the bankruptcy judge's order except with the *express consent* of the parties." Fed. R. Bankr. P. 7012(b) (emphasis added). The 1987 Advisory Committee notes to Rule 7012(b) reiterate the point: "[a] final order or judgment may not be entered in a non-core proceeding heard by a bankruptcy judge unless all parties *expressly consent*." Fed. R. Bankr. P. 7012 (1987 adv. comm. note) (citing 28 U.S.C. § 157(c)) (emphasis added). Furthermore, Federal Rule of Bankruptcy Procedure 7008 requires that "[i]n an adversary proceeding before a bankruptcy judge [complaints or the like] 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 judgments by the bankruptcy judge" and the 1987 Advisory Committee notes to the rule again reiterate the need for express consent: "[f]ailure to include the statement of consent does not constitute consent. *Only express consent* in the pleadings or otherwise is effective to authorize entry of a final order or judgment by the bankruptcy judge in a non-core proceeding." Fed. R. Bankr. P. 7008 (1987 adv. comm. note) (emphasis added).

The bankruptcy rules are not mere suggestions—they are imperatives. *See Kontrick v. Ryan*, 540 U.S. 443 (2004) (Federal Rules of Bankruptcy Procedure are mandatory); *see also Bank of N.S. v. United States*, 487 U.S. 250, 255 (1988) ("[I]n every pertinent respect, . . . [a Federal Rule of Criminal Procedure is] as binding as any statute duly enacted by Congress, and federal courts have no more discretion to disregard the Rule's mandate than they do to disregard constitutional or statutory provisions."). Accordingly, only express consent by all litigants can allow a bankruptcy court to enter a final judgment in a non-

core proceeding involving *Stern* claims. *See Weisfelner v. Blavatnik (In re Lyondell Chem. Co.)*, 467 B.R. 712, 722 (S.D.N.Y. 2012) (stating that in light of Federal Rule of Bankruptcy Procedure 7012(b) "mere implied consent appears to be insufficient"); *Messer v. Bentley Manhattan Inc., LLC (In re Madison Bentley Assocs.)*, 474 B.R. 430, 436 (S.D.N.Y. 2012) (same); *Penson Fin. Servs. v. O'Connell (In re Arbco Capital Mgmt., LLP)*, 479 B.R. 254, 266-67 (S.D.N.Y. 2012) ("The Bankruptcy Code, as amended in 1987, however, requires 'express consent of the parties' for a bankruptcy judge to enter final orders and judgment in non-core matters. . . . Furthermore, 'present law seems to mandate that parties must expressly consent to the entry of a final order by the bankruptcy court in the determination of non-core matters.'") (citations and internal punctuation omitted); *Pryor v. Tromba*, No. 13-CV-676, 2014 U.S. Dist. LEXIS 47969, at *21 (E.D.N.Y. Apr. 7, 2014) ("The Bankruptcy Code, however, requires 'express consent of the parties' for a bankruptcy judge to enter final orders and judgments in non-core matters.").

B. The Ninth Circuit's Holding That Implied Consent Is Sufficient Ignores The Plain Language Of The Federal Rules Of Bankruptcy Procedure

The Ninth Circuit's decision in *Bellingham* is the only circuit court decision to hold that implied consent is sufficient despite Federal Rules of Bankruptcy Procedure 7008 and 7012's requirement of express consent.[5] 702 F.3d at 568-69. The Ninth Circuit relied on this Court's

5. This Court did not reach the issue of consent in *Executive Benefits* and thus had no reason to address this argument. 134 S. Ct. at 2170 n.4.

decision in *Roell* and reasoned that *Roell* precluded an objection on the basis of the bankruptcy rules. *Id.* The Ninth Circuit erred.

In *Roell*, this Court held that implied consent may satisfy 28 U.S.C. § 636(c)(1), which governs the jurisdiction of magistrate judges and speaks only of the "consent of the parties, without qualification as to form." 538 U.S. at 586-87 (internal quotation marks omitted).[6] In holding that *Roell* precluded any objection based on the bankruptcy rules, the Ninth Circuit compared § 636(c) with § 157(c) and noted that neither provision specified that consent had to be express. *Bellingham*, 702 F.3d at 569. But the Ninth Circuit was mistaken in extending the reasoning of *Roell* to *Bellingham*. First, *Roell* merely held that—as a matter of *statutory* construction—implied consent may satisfy 28 U.S.C. § 636(c)(1). *Roell*, 538 U.S. at 586-87 ("the only question" is whether implied consent "can count as conferring 'civil jurisdiction' under § 636(c)(1), or whether adherence to the letter of § 636(c)(2) is an absolute demand"); *see id* at 587 n.5.[7] The *Roell* Court had no occasion to address whether implied consent would satisfy Article III concerns.

Second, *Roell* did not address or interpret the Bankruptcy Code or Federal Rules of Bankruptcy Procedure, which make clear that express consent

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6. Notably, four justices dissented and rejected the majority's conclusion that implied consent sufficed. *See id.* at 592 (Thomas, J., dissenting, joined by Stevens, Scalia, and Kennedy, JJ.).

7. Section 636(c) also states that its provisions are "[n]otwithstanding any provision of law to the contrary. 28 U.S.C. § 636(c). There is no equivalent language in § 157.

is required. Instead, *Roell* addressed the Federal Magistrates Act, specifically, 28 U.S.C. § 636(c)(1). The *Roell* Court reached the conclusion that implied consent could satisfy § 636(c)(1) only after determining that implied consent was consistent with "the text and structure of [§ 636] as a whole." *Id.* at 587. Although § 636 and § 157 are similar in many respects, § 636 provides numerous protections to ensure that consent is given knowingly and voluntarily. Not only does § 636(c) require litigant consent, it also provides that a litigant's decision to consent (or not to consent) is reported only to the clerk and while the statute permits judges to remind litigants of the referral option, it requires them also to "advise the parties that they are free to withhold consent without adverse substantive consequences." 28 U.S.C. § 636(c)(2). Accordingly, the *Roell* Court observed that a litigant's personal "Article III right is substantially honored" by those safeguards. *Roell*, 538 U.S. at 590. The Bankruptcy Code contains none of these safeguards included in the Federal Magistrate Act or any other similar measures to ensure that waiver is voluntary.

Finally, this Court cautioned in *Roell* that consent should be implied only in limited, exceptional circumstances. *Id.* at 591 n.7 ("implied consent will be the exception, not the rule, since . . . district courts remain bound by the procedural requirements of § 636(c)(2) and Federal Rule of Civil Procedure 73(b)"). In *Roell*, the party raising the constitutional objection (Withrow) had expressly consented and then waited until after he lost at trial to argue that the magistrate judge lacked authority to enter a final judgment because the *prevailing party* had not expressly consented to adjudication by the magistrate. *Id.* at 582-84. The Court had no opportunity to address a

situation in which the *complaining party* did not consent to adjudication by a non-Article III court. In addition, the two parties who originally did not expressly consent (Roell and Garibay), "'clearly implied their consent' by their decision to appear before the Magistrate Judge, without expressing any reservation, after being notified of their right to refuse and after being told that she intended to exercise case-dispositive authority" and then later indicated their express consent by filing a formal letter of consent with the district court after the case was remanded from the court of appeals to the district court. *Id.* at 583-84, 586; *see also id.* at 584 n.1 ("On at least three different occasions, counsel for Roell and Garibay was present and stood silent when the Magistrate Judge stated that they had consented to her authority."). What the Court referred to as "implied consent" from Roell and Garibay was implied from circumstances far different from those at issue in *Wellness* or the TOUSA Litigation where the parties were not even aware they had a right to a final adjudication before an Article III court.

As a result, the *Roell* Court was particularly concerned about a litigant sandbagging and belatedly raising an argument concerning a magistrate's authority as a tactical maneuver. *See id.* at 589-90. This Court limited its holding in *Roell* by noting that:

> the better rule is to accept implied consent where, as here, the litigant or counsel was made aware of the need for consent and the right to refuse it and still voluntarily appeared before the Magistrate Judge. Inferring consent *in these circumstances* thus checks the risk of gamesmanship by depriving parties of the

> luxury of waiting for the outcome before denying the magistrate judge's authority.

Id. at 590 (emphasis added).

Because the Federal Rules of Bankruptcy Procedure require express consent, this Court should reject the suggestion that a litigant can impliedly consent to a bankruptcy court entering final judgment on a private right claim.

II. A Party Cannot Knowingly Waive A Right That Does Not Exist By Not Asserting It

If the Court nonetheless were to conclude that a party can impliedly consent to the bankruptcy court entering final judgment on a private right claim, the Court should require that such waiver be knowing and unequivocal. Importantly, the Court should make clear that the fact that a party did not raise a *Stern* objection before *Stern* was decided does not provide the requisite knowing consent.

A. Waivers Of Constitutional Rights Should Not Lightly Be Inferred

As a general matter, "courts closely scrutinize waivers of constitutional rights, and 'indulge every reasonable presumption against a waiver.'" *Sambo's Rests., Inc. v. City of Ann Arbor*, 663 F.2d 686, 690 (6th Cir. 1981) (citing *Aetna Ins. Co. v. Kennedy*, 301 U.S. 389 (1937)). Courts have long held that "an effective waiver must . . . be one of a 'known right or privilege.'" *Curtis Publ'g Co. v. Butts*, 388 U.S. 130, 143 (1967) (citing *Johnson v. Zerbst*, 304 U.S. 458, 464 (1938)); *see, e.g., Roell*, 538 U.S. at 590 (where consent was an explicit feature of the Federal

Magistrates Act, the Court repeatedly emphasized that litigants must voluntarily consent to proceed before a magistrate with awareness of the "need to consent and the right to refuse it"); *Brady v. United States*, 397 U.S. 742, 748 (1970) ("Waivers of constitutional rights not only must be voluntary but must be knowing, intelligent acts done with sufficient awareness of the relevant circumstances and likely consequences.").

B. Litigants In Pending Cases Can Raise Arguments That Arise Upon Changes In The Law

Courts have also held that where there is an intervening change in the law, an exception to normal waiver rules "exists to protect those who, despite due diligence, fail to prophesy a reversal of established adverse precedent." *GenCorp, Inc. v. Olin Corp.*, 477 F.3d 368, 374 (6th Cir. 2007). As this Court held in *Curtis Publishing*, a party does not waive a "known right" simply by failing to assert the right before it was recognized in a subsequent decision. 388 U.S. at 143-45; *see also Hormel v. Helvering*, 312 U.S. 552, 558-59 (1941) (exception to waiver exists in "those [cases] in which there have been judicial interpretations of existing law after decision below and pending appeal—interpretations which if applied might have materially altered the result"). Federal circuits have repeatedly reiterated this point: "Where the Supreme Court decides a relevant case while litigation is pending . . . omission of an argument based on the Supreme Court's reasoning does not amount to a waiver." *Indiana Bell Tel. Co. v. McCarty*, 362 F.3d 378, 390 (7th Cir. 2004).[8]

8. *See also Ray v. UNUM Life Ins. Co. of Am.*, 314 F.3d 482, 487 (10th Cir. 2002) ("[A]n intervening change in the law

"[T]he doctrine of waiver demands conscientiousness, not clairvoyance, from parties," and thus a party should be allowed to assert a new objection on appeal when there is a "changed legal landscape." *Hawknet,* 590 F.3d at 92-93.

These well-known principles reflect a fundamental principle of fairness—a litigant "can hardly be faulted for failing to raise an argument before there was legitimate legal support for such an argument." *Planned Parenthood Cincinnati Region v. Taft*, 444 F.3d 502, 516 (6th Cir. 2006). In addition, there is a practical reason

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permits appellate review of an issue not raised below."); *Forshey v. Principi*, 284 F.3d 1335, 1356 (Fed. Cir. 2002) ("[D]ecision of an issue not decided or raised below is permitted when there is a change in the jurisprudence of the reviewing court or the Supreme Court after consideration of the case by the lower court."); *Big Horn Cnty. Elec. Coop., Inc. v. Adams*, 219 F.3d 944, 953 (9th Cir. 2000) (rejecting waiver theory and applying principles from intervening decision where plaintiff altered its stance once decision was issued, noting "an exception to the waiver rule exists for intervening changes in the law"); *DSC Commc'ns Corp. v. Next Level Commc'ns*, 107 F.3d 322, 326 n.2 (5th Cir. 1997) (applying principles from case decided after oral argument, stating "[w]e are unwilling to ignore this important clarification of the law, and perpetuate incorrect law, merely because [the case] was decided after briefing and oral argument in this case"); *Gucci Am. v. Bank of China*, 768 F.3d 122, 135 (2d Cir. 2014) ("While arguments not made in the District Court are generally waived, 'a party cannot be deemed to have waived objections or defenses which were not known to be available at the time they could first have been made'") (quoting *Hawknet, Ltd. v. Overseas Shipping Agencies*, 590 F.3d 87, 92 (2d Cir. 2009)) (internal citation omitted); *Schaff v. R.W. Claxton, Inc.*, 144 F.2d 532, 533 (D.C. Cir. 1944) (finding that the "appellant did not have a fair chance to raise and press at the trial" an argument based on a decision in another case issued after the trial).

for having such an exception to the normal waiver rules. Without such an exception, "[p]arties would be forced to . . . litter their pleadings with every argument which might conceivably be adopted during the pendency of a proceeding." *Id.* Waiver rules certainly were not intended to have such consequences.

C. *Stern v. Marshall* Was An Intervening Change In The Law

Congress granted to the bankruptcy courts under 28 U.S.C. § 157(b)(1) the authority to "hear and determine . . . all core proceedings" and "enter appropriate orders and judgments." 28 U.S.C. § 157(b)(1). Section 157(b)(2) provides a non-exclusive list of "core" proceedings that includes "counterclaims by the estate against persons filing claims against the estate," at issue in *Stern*. 28 U.S.C. § 157(b)(2). The Seventh Circuit in *Wellness* proceeded as if the alter-ego claim at issue was a core claim that the bankruptcy court had statutory authority to enter final judgment on because the parties did not argue otherwise. *See Wellness*, 727 F.3d at 762, Pet'r's. App. 20a-21a.h. *Stern* effected a change in the existing positive law by declaring that—despite the plain language of § 157(b)—bankruptcy courts lack constitutional authority to enter final judgments on state law counterclaims that would not be resolved in the process of ruling on a creditor's proof of claim. *Stern*, 131 S. Ct. at 2620.

Despite relying on past precedent—primarily *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 458 U.S. 50 (1982), and *Granfinanciera, S.A. v. Nordberg*, 492 U.S. 33 (1989)—"*Stern* goes further than both those cases." *Dev. Specialists, Inc. v. Akin Gump Strauss Hauer & Feld LLP*, 462 B.R. 457, 468 (S.D.N.Y.

2011). *Northern Pipeline* held that the assignment of state-law contract claims to bankruptcy courts under the Bankruptcy Act of 1978 violated Article III of the Constitution. 458 U.S. at 87. A majority of this Court agreed that the state-law contract claims at issue did not involve "public rights" that could be delegated to bankruptcy courts for resolution, but a majority of the Court was unable to agree on the confines of the public rights exception. *Id.* at 69-72.

Seven years later in *Granfinanciera*, this Court held that a non-creditor defending against a fraudulent transfer claim brought by a bankruptcy estate was entitled to a jury trial under the Seventh Amendment. 492 U.S. at 58-59, 64. This Court held that "[a]lthough the issue admits of some debate, a bankruptcy trustee's right to recover a fraudulent conveyance under 11 U.S.C. § 548(a)(2) seems to us more accurately characterized as a private rather than a public right," because such claims are "quintessentially suits at common law that more nearly resemble state-law contract claims brought by a bankrupt corporation to augment the bankruptcy estate than they do creditors' hierarchically ordered claims to a pro rata share of the bankruptcy res." *Id.* at 55-56. Significantly, *Granfinanciera* did not hold that any portion of § 157 was unconstitutional or that bankruptcy courts could not finally adjudicate fraudulent transfer claims. In fact, this Court stated explicitly that it was not "express[ing] any view as to whether the Seventh Amendment or Article III allows jury trials in such actions to be held before non-Article III bankruptcy judges."[9] *Id.* at 64.

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9. The overwhelming majority of courts, including numerous circuit courts, assumed the constitutionality of Section 157(b)(2) long after *Granfinanciera*. *See, e.g.*, *Turner v. Davis, Gillenwater*

In *Stern*, a majority of the Court found that the state-law counterclaim at issue was indistinguishable from the fraudulent conveyance claim in *Granfinanciera*: "Vicki's counterclaim—like the fraudulent conveyance claim at issue in *Granfinanciera*—does not fall within any of the varied formulations of the public rights exception in this Court's cases." *Stern*, 131 S. Ct. at 2614. Accordingly, the Court held that § 157(b)(2)(C), by authorizing bankruptcy courts to enter final judgments on such state law counterclaims, violated Article III of the Constitution. *Id.* at 2608, 2616, 2620. "*Stern* represent[ed] the first time a solid majority of the Supreme Court ha[d] applied the categorical, historical approach to limit the final adjudicative authority of the Bankruptcy Court following the 1984 Act." *Dev. Specialists*, 462 B.R. at 468.

The *Stern* Court explicitly acknowledged that its decision was a departure from certain assumptions in prior decisions: "In past cases, we have suggested that a proceeding's 'core' status alone authorizes a bankruptcy

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& Lynch (In re Inv. Bankers), 4 F.3d 1556, 1561 (10th Cir. 1993) (concluding that "the bankruptcy court's determination of the trustee's preference and fraudulent conveyance claims did not violate Article III" and that "[o]ther courts have similarly concluded that the bankruptcy courts have authority to preside over preferential and fraudulent transfer proceedings") (citations omitted); *Sigma Micro Corp. v. Healthcentral.com (In re Healthcentral.com)*, 504 F.3d 775, 787 (9th Cir. 2007) ("canvass[ing] the numerous courts outside this circuit who have already addressed the issue" and holding bankruptcy court had authority to enter summary judgment order because "[u]niversally these courts have all reached the same holding, that is, a Seventh Amendment jury trial right does not mean the bankruptcy court must instantly give up jurisdiction and that the case must be transferred to the district court").

judge, as a statutory matter, to enter final judgment in the proceeding." 131 S. Ct. at 2604 (citing *Granfinanciera*, 492 U.S. at 50). Lower courts generally adopted the same assumption. *See, e.g., In re Arbco Capital Mgmt.*, 479 B.R. at 260 ("[P]rior to *Stern*, it was widely understood that, pursuant to the 1984 Act, the Bankruptcy Court had the authority to finally resolve core matters . . . ."); *Dev. Specialists*, 462 B.R. at 466 ("Before *Stern*, courts . . . were accustomed to resolving whether the Bankruptcy Court could finally adjudicate a given claim by asking whether or not it could be considered 'core' under 28 U.S.C. § 157."). This Court's decision in *Stern* upended the widespread belief that bankruptcy courts had the authority to issue final judgments on core claims pursuant to § 157(b)(1) and (2).

D. Litigants In Pending Cases Should Be Allowed To Argue That Bankruptcy Courts Lacked Authority To Enter A Final Judgment Based On *Stern*

Before this Court's decision in *Stern*, defendants could not have known that they had a right to contest the authority of the bankruptcy court to enter final judgments on certain claims because it was *Stern* itself that provided defendants "with a legal basis to contest the Bankruptcy Court's adjudicative power that they did not have before." *Dev. Specialists*, 462 B.R. at 472 (noting that a "waiver of important rights should only be found where it is fully knowing").[10] As discussed above,

10. *See In re Madison Bentley*, 474 B.R. at 440 (holding that defendants' conduct did "not warrant the waiver of important rights given the emergence of important new precedent" where

principles of waiver, fairness and common sense dictate that a party in a pending case who, before *Stern*, did not object to the authority of the bankruptcy court to enter a final judgment on a "core" claim—which 28 U.S.C. § 157 clearly provides—should be allowed to contest the bankruptcy court's authority following *Stern* provided it is done within a reasonable time period and without prejudicial delay.

According to the United States as *amicus curiae*, Sharif should have predicted this Court's decision in *Stern* based on *Granfinanciera* and contested the bankruptcy court's constitutional authority. (*See* United States Br. at 30-31.) But, *Granfinanciera* did not put litigants on notice that aspects of § 157(b) were unconstitutional. *See supra* at 17; *see also Teleservices Grp.*, 456 B.R. at 339 n.66 (rejecting argument that defendant should have been aware of the constitutional deficiencies of § 157 based on *Granfinanciera* and *Northern Pipeline*). Courts in the Seventh Circuit, like most courts, assumed the

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defendants filed a motion to withdraw the reference eight months after *Stern*); *Wolf v. Nayna Networks, Inc. (In re Prof'l Satellite & Commc'n, LLC)*, No. 12cv70 L(MDD), 2012 WL 6012829, at *2 (S.D. Cal. Dec. 3, 2012) (finding motion to withdraw reference timely "[g]iven the timing of the *Stern* decision"); *Retired Partners of Coudert Bros. Trust v. Baker McKenzie LLP (In re Coudert Bros. LLP)*, No. 11-2785(CM), 2011 WL 5593147, at *12 (S.D.N.Y. Sept. 23, 2011) ("[U]ntil *Stern* strongly embraced the approach of the *Marathon* plurality, it is doubtful that the [defendant] knew or could have known that it had a right to Article III adjudication that it was waiving."); *Meoli v. Huntington Nat'l Bank (In re Teleservices Grp., Inc.)*, 456 B.R. 318, 339 (Bankr. W.D. Mich. 2011) (stating that, prior to the issuance of *Stern*, defendant did not make a knowing waiver of its right to have an Article III judge enter a final judgment on fraudulent transfer claims).

constitutionality of § 157(b)(2) long after *Granfinanciera*. *See Paloian v. Carl Edward Avallon Trust (In re Pro-Pak Serv.),* No. 02 C 5528, 2002 U.S. Dist. LEXIS 24926, at *5-7 (N.D. Ill. Dec. 30, 2002) (noting *Granfinanciera* and rejecting motion to withdraw reference for preference and fraudulent conveyance claims because they were defined as core by § 157(b)(2)); *Plan Adm'r v. Lone Star RV Sales, Inc. (In re Conseco Fin. Corp.)*, 324 B.R. 50, 55-56 (N.D. Ill. 2005) (rejecting defendant's motion to withdraw the reference based on defendant's intention to seek a jury trial and noting that the bankruptcy court may resolve dispositive motions which would eliminate the need for a jury trial in the district court). The United States does not point to a single case decided before *Stern* from the Seventh Circuit or any other jurisdiction holding that bankruptcy courts lacked the constitutional authority to finally adjudicate core matters.

Although this Court in *Stern* referenced *Granfinanciera* and other prior decisions, reliance on precedent—an inherent feature of judicial decision-making—hardly means the outcome was so predictable that it should have been anticipated by any prudent litigant. This Court rejected such an approach to waiver in *Curtis Publishing.* The Court there reviewed whether the defendant had waived certain constitutional defenses to libel claims based on the decision in *New York Times Co. v. Sullivan*, 376 U.S. 254 (1964), which was issued soon after the jury returned a verdict against the defendant in *Curtis Publishing. See* 388 U.S. at 138-39. The appellate court held that the defendant waived any right to challenge the verdict based on *Sullivan* because "the general state of the law at the time of [the] trial was such that [appellant] should . . . have seen 'the handwriting on the wall.'" *Id.*

at 143 (citing 351 F.2d 702, 734 (5th Cir. 1965)). This Court disagreed, stating that although *Sullivan* "did draw upon earlier precedents," there was also strong precedent indicating that libel actions were not subject to constitutional challenge.[11] *Id.* at 143-44. The Court held that it was the "eventual resolution of [*Sullivan*], rather than its facts and the arguments presented by counsel, which brought out the constitutional question," and thus the Court, "would not hold [the defendant] waived 'a known right' before it was aware of the [*Sullivan*] decision." *Id.* at 145.

Consistent with this Court's holding in *Curtis Publishing*, litigants should be allowed to assert a *Stern* objection to the bankruptcy court's exercise of authority to finally adjudicate a particular claim, even if they did not assert that objection before *Stern* was decided. Courts should look at a litigant's conduct after *Stern* was decided. *See Dev. Specialists*, 462 B.R. at 469 (stating that the timeliness of a motion to withdraw the reference "should be evaluated by looking to how promptly the [defendants] moved for withdrawal following *Stern*"). If the litigant asserted an objection based on *Stern* within a reasonable time and before availing itself of the bankruptcy court's jurisdiction then the objection should be heard. In contrast, if the litigant waits, participates

11. The Court stated further that "[g]iven the state of the law prior to our decision in [*Sullivan*], we do not think it unreasonable for a lawyer trying a case of this kind . . . to have looked solely to the defenses provided by state libel law." 388 U.S. at 144. Moreover, the Court rejected the notion that its grant of certiorari in *Sullivan* should have signaled a different conclusion, or that defendants' counsel, who were involved in *Sullivan*, should have been alerted to the constitutional issues. *Id.*

in the bankruptcy court proceedings and then belatedly raises the *Stern* objection to gain a tactical advantage, only then could the *Stern* objection be deemed waived. *See Bank of Neb. v. Rose (In re Rose)*, 483 B.R. 540, 545 (B.A.P. 8th Cir. 2012) (debtor consented to bankruptcy court's final judgment on state law counterclaims where debtor failed to object at trial or in the post-trial brief filed nearly one year after *Stern* was issued and objected only after receiving an adverse judgment).[12] Where a litigant asserts its newly articulated rights within a reasonable period of time, there is no concern about sandbagging and no waiver of a known right should be found.[13]

Under Seventh Circuit precedent controlling at the time, Sharif did not have a valid constitutional objection to the bankruptcy court's adjudication of the claims against

12. *See also Gibson v. Tucker (In re G&S Livestock Co.)*, 478 B.R. 906, 917-18 (S.D. Ind. 2012) (defendants consented to bankruptcy court adjudication of fraudulent transfer claims where they stipulated to the court's authority under § 157 in their post-trial brief filed four months after *Stern* was issued and objected to the court's authority only after receiving an adverse judgment); *Dev. Specialists*, 462 B.R. at 472 (distinguishing litigants that move to withdraw the reference after an adverse ruling from defendants who moved to withdraw shortly after the *Stern* decision was issued, making "sandbagging" concerns "considerably less acute").

13. *Stern* discusses "sandbagging" in response to the statutory argument that the bankruptcy court lacked jurisdiction to enter final judgment on a defamation claim against the bankruptcy estate under § 157(b)(5), which provides for trial of certain claims in the district court. 131 S. Ct. at 2607-08. The *Stern* Court's comments about sandbagging did not relate to the argument that the bankruptcy court lacked constitutional authority to enter final judgment on the bankruptcy estate's counterclaim. *Id.*

him. *Stern* gave Sharif the objection and Sharif thereafter asserted it. Sharif did not waive the objection by failing to assert it when it did not yet exist.

CONCLUSION

For the foregoing reasons, the judgment of the United States Court of Appeals for the Seventh Circuit should be affirmed.

Respectfully submitted,

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APPENDIX

Appendix

APPENDIX — LIST OF *AMICI CURIAE*

The *amici curiae* consist of the following entities:

- Atascosa Investments, LLC;
- Aurum CLO 2002-1 Ltd.;
- Bank of America, N.A.;
- Burnet Partners, LLC;
- Deutsche Bank Trust Company Americas;
- Flagship CLO III;
- Flagship CLO IV;
- Flagship CLO V;
- Gleneagles CLO Ltd.;
- Goldman Sachs Credit Partners, L.P.;
- Grand Central Asset Trust, HLD Series;
- Grand Central Asset Trust, SOH Series;
- Hartford Mutual Funds, Inc., on behalf of The Hartford Floating Rate Fund by Hartford Investment Management Company, their Sub-Advisor;

- Highland CDO Opportunity Fund, Ltd.;
- Highland Credit Opportunities CDO Ltd.;
- Highland Floating Rate Advantage Fund;
- Highland Floating Rate LLC;
- Highland Legacy Limited;
- Highland Loan Funding VII, LLC;
- Highland Offshore Partners, L.P.;
- Jasper CLO, Ltd.;
- LL Blue Marlin Funding LLC;
- Liberty CLO, Ltd.;
- Merrill Lynch Credit Products LLC;
- Ocean Bank;
- Rockwall CDO, Ltd.;
- Silver Oak Capital LLC;
- Stedman CBNA Loan Funding LLC;
- The Foothills Group, Inc.;

Appendix

- Van Kampen Dynamic Credit Opportunities Fund;
- Van Kampen Senior Income Trust;
- Van Kampen Senior Loan Fund; and
- Wells Fargo Bank, N.A.