ABLJ Symposium: Equitable Powers of the Bankruptcy Court 40 Years After the Enactment of the Bankruptcy Code

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Table of Contents

The Equitable Powers of the Bankruptcy Court .............. 1
Coordes Abstract ..............................................16
Dick Abstract ....................................................17
Markell Abstract ............................................... 18
Westbrook Abstract ..........................................19
Courting Equity in Bankruptcy .................................20
THE EQUITABLE POWERS OF THE BANKRUPTCY COURT

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“But Your Honor, this is a bankruptcy court—a court of equity—surely, you can grant the requested relief under your equitable powers.”

Words to this effect are often spoken in bankruptcy courts across the country. They are grounded in traditional notions of equitable relief and the historical characterization of bankruptcy courts as “courts of equity.” But do they still ring true today? This question arises because of what some commentators suggest is a continuing contraction of the bankruptcy courts’ equitable powers.¹ These commentators point to recent U.S. Supreme Court decisions, such as Law v. Siegel, 571 U.S. 415 (2014), to support their thesis. In Siegel, the Supreme Court explained, in the context of discussing a bankruptcy court’s authority to impose sanctions under section 105 or its inherent powers, that “whatever … sanctions a bankruptcy court may impose on a dishonest debtor, it may not contravene express provisions of the Bankruptcy Code ….” Id. at 427–28.

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¹ See, e.g., Adam James Wiensch, The Supreme Court, Textualism, and the Treatment of Pre-Bankruptcy Code Law, 79 GEO. L.J. 131, 1860–61 (1991) (“The equitable powers of the bankruptcy courts were codified in section 105 of the Bankruptcy Code. The [Supreme] Court has taken a very narrow view of these powers. In addition to adopting a textualist approach to interpret the Bankruptcy Code, the Court has expressly limited the equitable powers of the bankruptcy courts on several occasions.”) (citations omitted). See also Lawrence Ponoroff, Whither Recharacterization, 68 RUTGERS U.L. REV. 1217, 1222 (2016) (“[T]he bankruptcy courts’ general equitable authority under § 105(a) has taken something of a drubbing in recent years.”); Daniel J. Sheffner, Situating Reimposition of the Automatic Stay Within the Federal Common Law of Bankruptcy, 47 U. TOL. L. REV. 447, 449 (2016) (“Unfortunately, § 105’s history, salient scholarly commentary, and the Supreme Court’s recent decision in Law v. Siegel indicate that it is improper to base reimposition [of the stay] on § 105”); Melanie L. Cyganowski & Lloyd M. Green, The Demise of Equitable Disallowance of Claims, 24 J. BANKR. L. & PRAC. 6, art. 1 (Dec. 2015) (“By reason of the Supreme Court’s 2014 decision in Law v. Siegel, in which the Court limited the scope of the bankruptcy court’s equitable powers and the reach of section 105(a), the future of equitable disallowance is in doubt.”).
The appropriate scope of the bankruptcy courts’ equitable powers is not a new question. Rather, it dates back to the inception of the Union\(^2\) and how the U.S. Constitution allocates jurisdiction to federal courts\(^3\) and power to Congress “[t]o establish … uniform Laws on the subject of Bankruptcies throughout the United States ….” U.S. Const. art. I, § 8, cl. 4. It generally flows from the powers vested in the English Court of Chancery, the notion that the law does not always provide an adequate or sufficiently determinant remedy, and the policies underlying federal bankruptcy law.\(^4\) Nonetheless, the precise parameters of the bankruptcy courts’ equitable powers have evolved over time.

The scope of the bankruptcy courts’ equitable powers also is not a settled question. Commentators have long debated the existence and extent of the bankruptcy courts’ equitable powers.\(^5\) They also debate what it means for a court to do “equity” and how those notions relate to a court’s inherent and statutory powers. Some even suggest that a bankruptcy court is not a court of equity at all.\(^6\)

\(^2\) See infra notes 14–18 and accompanying text.
\(^3\) See, e.g., U.S. Const. art. III, § 1 (“The judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish.”); U.S. Const. art. I, § 8, cl. 9 (“The Congress shall have Power . . . To constitute Tribunals inferior to the supreme Court . . .”).
\(^4\) See infra notes 23–27 and accompanying text.
\(^5\) See, e.g., Lynne F. Riley & Maria C. Furlong, The Supreme Court Restores Discretion and Enhances Jurisdiction of the Bankruptcy Courts, 2008 NORTON ANN. SURV. BANKR. L. 4 (2008) (“[A] growing body of academia that examines the historical underpinnings of the bankruptcy court as a basis for disputing the court’s status as a court of equity. Proponents of this theory profess strict limitations on the bankruptcy court’s discretion to utilize equitable and inherent powers whenever the Bankruptcy Code is silent, vague, or contradictory.”); Matthew T. Gunlock, An Appeal to Equity: Why Bankruptcy Courts Should Resort to Equitable Powers for Latitude in Their Interpretation of “Interests” Under Section 363(f) of the Bankruptcy Code, 47 WM. & MARY L. REV. 347, 365–66 (2005) (“Widespread criticism, however, does not render the language of § 105(a) meaningless. Rather, the language’s inclusion within the Bankruptcy Code should serve as a reminder that, ultimately, bankruptcy courts are equitable in nature and that all of the Code’s provisions are subject to a balancing of the equities in any case.”); Daniel B. Bogart, Resisting the Expansion of Bankruptcy Court Power Under Section 105 of the Bankruptcy Code: The All Writs Act and an Admonition from Chief Justice Marshall, 35 ARIZ. ST. L.J. 793, 794 (2003) (“In this article, the author joins a small but growing chorus of scholarly voices criticizing the over-ambitious use of section 105.”); Marcia S. Krieger, “The Bankruptcy Court Is A Court of Equity”: What Does That Mean?, 50 S.C. L. REV. 275, 275–76 (1999) (noting that “scholars regularly debate the scope of the bankruptcy court’s equitable powers and jurisdiction”).
This preface does not attempt to answer these ever prevalent and important questions. Rather, it provides a brief overview of the origins and evolution of the bankruptcy courts’ equitable powers. This overview likewise does not explore all potential nuances, critiques, or alternative perspectives, as that task falls to the exceptionally talented academics participating in the Symposium. Instead, this preface merely strives to set the table for the Symposium and a more forward-looking conversation.

The academic papers that follow (and that are described at the end of this preface) critically analyze the bankruptcy courts’ equitable powers, namely what they are and what, perhaps, they should be. Regardless of existing critiques and questions concerning “bankruptcy courts as courts of equity,” courts and parties frequently invoke, and rely upon, the bankruptcy courts’ equitable powers. The appropriate scope of the bankruptcy courts’ equitable powers thus remains an important issue that affects not only how bankruptcy judges perform their jobs on a daily basis, but also how debtors’ and creditors’ rights are resolved in bankruptcy cases.

I. The Origins of Courts of Equity

An appropriate starting point for evaluating the equitable powers of the bankruptcy courts is the English Court of Chancery. The development of the English Court of Chancery was in many

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7 Equity, as a concept relating to the administration of laws, can be traced to, among others, Greek and Roman philosophers, the Pandects, and Roman law. 1 JOSEPH STORY, COMMENTARIES ON EQUITY JURISPRUDENCE §§1–4, at 1–5 (Boston, Charles C. Little & James Brown 14th ed. 1918) (explaining the development of the English Court of Chancery). The concept of equity or what it means for a court to do equity also is subject to various meanings. For example, Justice Story noted that “[i]n the most general sense we are accustomed to call that Equity which in human transactions is founded in natural justice, in honesty and right, and which properly arises ex aequo et bono.” Id. at §1, at 1. Dean Pound observed, A stage of liberalization, which may be called the stage of equity or natural law, succeeds the strict law. This stage is represented in Roman law by the periods of the *ius gentium* and *ius naturale*, in English law by the rise of the Court of Chancery and development of equity, in the law of Continental Europe by the period of the law-of-nature school, that is, the seventeenth and eighteenth centuries. The watchword of the stage of strict law was certainty. The watchword of this stage is morality or some phrase of ethical import, such as good conscience, *aequum et bonum*, or natural law. The former insists on uniformity, the latter on morality; the former on form, the latter on justice in the ethical sense; the former on remedies, the latter on duties, the former on rule, the latter on reason. The capital ideas of the stage of equity or natural law are the
ways a response to the perceived rigidness of the common law, which arguably was too inflexible to accommodate the particular facts and circumstances of any given case.\textsuperscript{8} Parties who were unhappy with an application of the common law in England would request relief from the King based on the equities of the matter.\textsuperscript{9} As this practice became more commonplace, the role of the King’s chanceries expanded, and eventually England established a formal Court of Chancery.\textsuperscript{10}

Chancellors in the English system initially wielded wide discretion, basically providing a remedy whenever a Chancellor personally found an injustice. They addressed a variety of matters, from trusts and uses and agency law to fraud and other claims, defenses, and remedies not available under the common law.\textsuperscript{11} Over time, the English Court of Chancery evolved, and certain parameters emerged. For example, its jurisdiction was limited to those instances in which no adequate remedy existed under the common law; Chancellors increasingly published their decisions to establish precedent; and Chancery practice generally became more standardized.\textsuperscript{12} Even with these refinements, however, not everyone supported the Court of Chancery,\textsuperscript{13} skeptical of the broad discretion and jurisdiction purportedly vested in Chancellors.

\begin{footnotesize}
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\item See Oleck, supra note 8, at 35; Gordon supra note 8, 185–87.
\item See Oleck, supra note 8, at 35–36, 38; Morley, supra note 9, at 228. See also \textit{Story}, supra note 7, §§38–57, at 42–61.
\item See Oleck, supra note 8, at 39–40; Morley, supra note 9, at 229.
\item Morley, supra note 9, at 229; Gordon, supra note 8, at 190.
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Such was the state of affairs at the time of the adoption of the Articles of Confederation and the early formation of the judicial branch in the United States. The colonies were divided in their approaches to courts of equity and equitable powers more generally.\textsuperscript{14} The Articles of Confederation did not mention “equity,” and it was only added to the U.S. Constitution late in the drafting process.\textsuperscript{15} That revision resulted in the final language of Section 2 of Article III of the Constitution, which provides, “The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States, and Treaties made, or which shall be made, under their Authority....” U.S. Const. art. III, § 2. “The \textit{Federalist Papers} defended Article III’s jurisdictional grant over cases in equity by explaining that federal courts need the power to fairly adjudicate cases otherwise within their jurisdiction that involve ‘ingredients of fraud, accident, trust, or hardship.’” Michael T. Morley, \textit{The Federal Equity Power}, 59 B.C. L. Rev. 217, 231 (2018) (emphasis in original).

The scope of federal courts’ equity jurisdiction, though grounded in the Constitution, was initially unsettled given the interplay of federal and state law, particularly in diversity cases. The Supreme Court consistently described the equitable powers of the federal courts as akin to those vested in the English Court of Chancery and upheld a wide array of lower court decisions based in equity.\textsuperscript{16} That approach did not change entirely, but it was refined in the context of federal diversity

\textsuperscript{14} See Oleck, \textit{supra} note 8, at 40–41; Morley, \textit{supra} note 9, at 230; Gordon, \textit{supra} note 8, at 185–87, 198–98; Donald J. Wolfe, Jr. \& Michael A. Pittenger, \textit{Corporate and Commercial Practice in the Delaware Court of Chancery} § 1-02, at 1-3 (2018) (“Delaware’s creation of a separate court of equity in 1792 ran decidedly against the trend of the late eighteenth century, a time when most other American jurisdictions either were moving away from separate courts of law and equity or, as was the case in Delaware prior to 1792, had never established a separate equity court in the first instance.”). For a general discussion of courts of equity in the United States in the early 1900s, see Henry H. Ingersoll, \textit{Confusion of Law and Equity}, 21 Yale L.J. 58 (1911).

\textsuperscript{15} Morley, \textit{supra} note 9, at 231; Gordon, \textit{supra} note 8, at 198–98.

\textsuperscript{16} See, e.g., \textit{Sheffield Furnace Co. v. Witherow}, 149 U.S. 574, 578, 579 (1893) (holding that a federal court could entertain a bill in equity to enforce a mechanic’s lien, even though a state statute “provide[d] for an action at law” to enforce mechanic’s liens, because “foreclosure of a mechanic’s lien is essentially an equitable proceeding” and that states, “by prescribing an action at law to enforce even statutory rights, cannot oust [] Federal court[s], sitting in equity, of its jurisdiction to enforce such rights, provided they are of an equitable nature”). \textit{See also Hipp for Use of Cuesta
cases following the Supreme Court’s decision in *Erie R. Co. v. Tompkins*.\(^{17}\) 304 U.S. 64 (1938) (disapproving of its prior decision in *Swift v. Tyson* and holding that federal courts sitting in diversity must apply applicable substantive, state law).\(^{18}\) The decision did not, however, otherwise limit the general equitable powers of the federal courts.

II. The Origins of Bankruptcy Courts as Courts of Equity

The genesis of bankruptcy courts’ equitable powers is arguably more nuanced than that of Article III courts. The structure of bankruptcy courts as Article I courts that operate as a unit of Article III district courts creates a hybrid platform from which to analyze bankruptcy courts’ equitable powers.\(^{19}\) Some commentators argue that the structure of the bankruptcy court limits its equitable powers, though that same structure may support both the general equitable powers vested in federal courts and those granted by the Bankruptcy Code.

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\(^{17}\) See, e.g., *Guar. Tr. Co. of N.Y. v. York*, 326 U.S. 99, 112 (1945) (“Dicta may be cited characterizing equity as an independent body of law. To the extent that we have indicated, it is. But insofar as these general observations go beyond that, they merely reflect notions that have been replaced by a sharper analysis of what federal courts do when they enforce rights that have no federal origin.”).

\(^{18}\) See, e.g., *Shady Grove Orthopedic Assocs., P.A. v. Allstate Ins. Co.*, 559 U.S. 393, 406 (2010) (“Erie involved the constitutional power of federal courts to supplant state law with judge-made rules. In that context, it made no difference whether the rule was technically one of substance or procedure; the touchstone was whether it ’significantly affect[s] the result of a litigation.”) (quoting *Guaranty Trust Co.*, 326 U.S. at 109).

\(^{19}\) 28 U.S.C. § 151 (2019) (“In each judicial district, the bankruptcy judges in regular active service shall constitute a unit of the district court to be known as the bankruptcy court for that district. Each bankruptcy judge, as a judicial officer of the district court, may exercise the authority conferred under this chapter with respect to any action, suit, or proceeding and may preside alone and hold a regular or special session of the court, except as otherwise provided by law or by rule or order of the district court.”).
Any analysis of a bankruptcy court’s equitable powers should consider the policies and language of Articles I and III of the Constitution, the concept of equity in federal courts, and the Bankruptcy Code. Moreover, Congress did not craft the Bankruptcy Code on a clean slate, but against the backdrop of the Bankruptcy Act of 1898 and the exercise of equitable power in insolvency cases prior to that time.

Before considering the language of the Bankruptcy Code, it is helpful to reflect on the traditional jurisdiction of courts of equity. As noted, courts of equity generally focus on situations in which the remedy at law is inadequate or indeterminate. As Justice Story concisely explained, “[p]erhaps the most general if not the most precise description of a Court of Equity, in the English and American sense, is that it has jurisdiction in cases of rights, recognized and protected by the

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20 Congress is empowered to create uniform bankruptcy laws, and it has reserved certain equitable powers to the bankruptcy courts in that legislation. U.S. Const. art. I, § 8, cl. 9; 11 U.S.C. § 105. See also 2 COLLIER ON BANKRUPTCY ¶ 105.02 (16th ed. 2019) (discussing the bankruptcy court’s inherent and statutory powers under section 105 and providing examples of how courts exercise such powers).

21 The Supreme Court noted this general concept in the context of civil contempt and section 105, explaining: Our conclusion rests on a longstanding interpretive principle: When a statutory term is “obviously transplanted from another legal source,” it “brings the old soil with it.” Taggart v. Lorenzen, 139 S. Ct. 1795, 2019 WL 2331303, at *4 (2019).

22 See, e.g., Gordon, supra note 8, at 185–87 (“Chancery recognized forms of equitable property (trusts, mortgages, and priorities of estates and interests), enforced torts by injunction, enforced contracts by specific performance and injunction, afforded relief against the rigidity of the common law (fraud, undue influence, accident, and mistake), and provided procedural convenience (account, interrogatories, and discovery).”); Kristin A. Collins, “A Considerable Surgical Operation”: Article III, Equity, and Judge-Made Law in the Federal Courts, 60 DUKE L.J. 249, 266 (2010) (“Both historically and today, the term “equity” refers to a set of rights, remedies, and procedures available ostensibly to ameliorate defects of the common law (such as in the cases of fraud, mistake, and forgery) and to enforce equitable instruments that require the ongoing supervision of a court (such as trusts and guardianships.”); Thomas O. Main, Traditional Equity and Contemporary Procedure, 78 WASH. L. REV. 429, 442 (2003); Chateau Apartments Co. v. City of Wilmington, 391 A.2d 205, 207 (Del. 1978) (“In order for the Court of Chancery to assume jurisdiction over a proceeding, of course, there must be an absence of an adequate remedy at law.10 Del.C. s 342.”).
municipal jurisprudence, where a plain, adequate, and complete remedy cannot be had in the Courts of Common Law.”

Courts in the United States historically have viewed situations in which a debtor’s assets are insufficient to satisfy her obligations to creditors as instances in which equity may assist. If a debtor cannot pay an obligation and an award of damages would prove futile, equitable principles may fill the void. Indeed, the premise of enjoining creditors’ actions to promote a fair and equitable distribution of the debtor’s assets is aligned with remedies commonly granted by courts of equity. Congress was aware of the various uses of equity in the context of resolving debtor-creditor relationships when it enacted early bankruptcy legislation, including the Bankruptcy Act of 1898.

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23 STORY, supra note 7, §33, at 29.
24 Ralph A. Newman, The Effect of Insolvency on Equitable Relief, 13 ST. JOHN’S L. REV. 44, 44–45 (1938). See also Matter of Terry Ltd. P’ship, 169 B.R. 182, 185 (Bankr. N.D. Ind.), aff’d sub nom. Invex Holdings, N.V. v. Equitable Life Ins., 179 B.R. 111 (N.D. Ind. 1993), aff’d sub nom. Matter of Terry Ltd. P’ship, 27 F.3d 241 (7th Cir. 1994); In re Landau Boat Co., 8 B.R. 436, 437–439 (Bankr. W.D. Mo. 1981). In a related context, the English Court of Chancery routinely exercised jurisdiction over actions of account, which could include incidental matters such as “the administration of personal assets; consequently of debts, legacies, the distribution of the residue, and the conduct of executors and administrators.” 2 JOSEPH STORY, COMMENTARIES ON EQUITY JURISPRUDENCE §593, at 10 (Boston, Charles C. Little & James Brown 14th ed. 1918) (explaining the development of the English Court of Chancery). See also In re Judiciary Tower Assocs., 170 B.R. 8, 9–10 (Bankr. D.D.C. 1994) (“In Cook, a joint bankruptcy commission was taken against two partners, and the partners’ assets were assigned for the benefit of their joint creditors. Thereafter, the partners’ individual creditors took out a separate commission on the partner’s individual assets. The English court required an action at equity to account for the assets as between the assignee for the benefit of the joint creditors and the assignees for the benefit of the individual creditors.”).
25 The English Court of Chancery used injunctive relief in various scenarios. See, e.g., Oleck, supra note 8, at 38 (describing English Court of Chancery granting “injunctive restraint for nuisances”); Hagner v. Heyberger, 1844 WL 4922, at *1 (Pa. 1844) (“The English chancery can by injunction restrain the commission of acts contrary to equity.”). See also STORY, supra note 24, §§1181–1191, at 549–558. Likewise, U.S. district courts overseeing equity receiverships relied on their equitable powers to prevent dissipation of the debtor’s assets prior to a resolution of the receivership. See Harry W. Kroeger, The Jurisdiction of Courts of Equity to Administer Insolvents’ Estates, Considered in Relation to Historical Antecedents, 9 ST. LOUIS L. REV. 179 (1924). The district courts continue to invoke similar powers in the context of federal receiverships, which are largely based on equitable principles. See, e.g., S.E.C. v. Credit Bancorp, Ltd., 290 F.3d 80, 90 (2d Cir. 2002) (“We agree with the District Court that receiverships are ‘insolvency proceedings,’ and that the law of federal equity receiverships applies.”); S.E.C. v. Elliott, 953 F.2d 1560, 1566 (11th Cir. 1992) (“The district court has broad powers and wide discretion to determine relief in an equity receivership” … “This discretion derives from the inherent powers of an equity court to fashion relief.”) (citations omitted).
26 The relation to existing concepts of equity is evident even in the language of the statute itself. For example, “Section 77(a) of the Bankruptcy Act, 11 U.S.C. s 205(a), provides that the reorganization court shall ‘have exclusive jurisdiction of the debtor and its property wherever located, and shall have and may exercise in addition to the powers conferred by this section all the powers, not inconsistent with this section, which a Federal court would have had if it
Under the Bankruptcy Act of 1898, Congress recognized the role of equity in bankruptcy cases. Specifically, section 2(a)(15) of the Act permitted courts to:

Make such orders, issue such process, and enter such judgments, in addition to these specifically provided for, as may be necessary for the enforcement of the provisions of this Act: Provided, however, That an injunction to restrain a court may be issued by the judge only.

11 U.S.C. § 11(a)(15) (1938). Although limited in scope, section 2(a)(15) drew upon traditional notions of equity. As explained by the Supreme Court:

By section 2 of the Bankruptcy Act (U.S.C. title 11, s 11, 11 USCA s 11), courts of bankruptcy are invested 'with such jurisdiction at law and in equity as will enable them to exercise original jurisdiction in bankruptcy proceedings.' They are essentially courts of equity, and their proceedings inherently proceedings in equity, the words ‘at law’ probably having been inserted only with regard to clause (4) of section 2, 11 USCA s 11(4), which confers authority to arraign, try, and punish bankrupts and others for violations of the act. Local Loan Co. v. Hunt, 292 U.S. 234, 240, 54 S.Ct. 695, 78 L.Ed. 1230, 93 A.L.R. 195. Their adjudications and orders constitute in all essential particulars decrees in equity. Id., page 241 of 292 U.S., 54 S.Ct. 695. The power to issue an injunction when necessary to prevent the defeat or impairment of its jurisdiction is, therefore, inherent in a court of bankruptcy, as it is in a duly established court of equity.


The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.

11 U.S.C. § 105. As discussed below, courts continue to recognize the broad grant of equitable powers to the bankruptcy courts under the Bankruptcy Code, but often urge caution in the exercise of those powers. \(^{31}\)

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\(^{30}\) See, e.g., In re Padilla, 389 B.R. 409, 431 (Bankr. E.D. Pa. 2008) (“Section 2a(15) is quite similar to and is considered § 105(a)’s direct antecedent.”); In re James, 20 B.R. 145, 149 (Bankr. E.D. Mich. 1982) (“The legislative history to this Code provision states that s 105 is derived from s 2(a)(15) of the Act.”); In re Mason, 18 B.R. 817, 823 (Bankr. W.D. Tenn. 1982) (“11 U.S.C. Section 105(a) is based on, and does not substantially differ from Section 2(a)(15) of the former Bankruptcy Act, 11 U.S.C. Section 11(a)(15).”).

\(^{31}\) James, 20 B.R. at 150 (“Section 105 of the Bankruptcy Code, 11 U.S.C. s 105, retained this broad grant of equitable powers, but at the same time caution is urged. “The basic intention of the section is to enable the bankruptcy court to do whatever is necessary to aid its jurisdiction, i.e., anything arising in or relating to a bankruptcy case.” 2 Collier on Bankruptcy at 105-4 (15th ed. 2003).”)


III. Courts’ Use and Interpretation of Section 105(a) of the Bankruptcy Code

Courts and parties in bankruptcy cases consistently refer to bankruptcy courts as courts of equity.\textsuperscript{32} Perhaps just as frequently, courts acknowledge limitations on the bankruptcy courts’ equitable powers. Those powers are qualified and may not necessarily encompass all authority vested in traditional courts of equity. Indeed, courts tend to confine the bankruptcy courts’ equitable powers to those “necessary or appropriate” to implement the policies and provisions of the Bankruptcy Code.

The Supreme Court concisely articulated this proposition in \textit{Norwest Bank Worthington v. Ahlers}, explaining that “whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code.”\textsuperscript{33} 485 U.S. 197, 206 (1988). Although the principle is simply stated, courts tend to struggle with its implementation. See, e.g., \textit{In re Aquatic Dev. Grp., Inc.}, 352 F.3d 671, 673, 680–81 (2d Cir. 2003) (vacating a \textit{nunc pro tunc} order that retroactively closed a bankruptcy estate and noting that “the general grant of equitable power contained in section 105(a) cannot trump specific provisions of the Bankruptcy Code, but must instead be exercised within the parameters of the Code itself”); \textit{In re Combustion Eng’g. Inc.},

\textsuperscript{32} See, e.g., \textit{Young v. United States}, 535 U.S. 43, 50 (2002) (“That is doubly true when it is enacting limitations periods to be applied by bankruptcy courts, which are courts of equity and “appl[y] the principles and rules of equity jurisprudence.” Pepper v. Litton, 308 U.S. 295, 304, 60 S.Ct. 238, 84 L.Ed. 281 (1939). \textit{See also United States v. Energy Resources Co.}, 495 U.S. 545, 549, 110 S.Ct. 2139, 109 L.Ed.2d 580 (1990); \textit{Katchen v. Landy}, 382 U.S. 323, 326–27 (1966) (“The bankruptcy courts are expressly invested by statute with original jurisdiction to conduct proceedings under the Bankruptcy Act. These courts are essentially courts of equity, ..., and they characteristically proceed in summary fashion to deal with the assets of the bankrupt they are administering.”) (citations omitted); \textit{Young v. Higbee Co.}, 324 U.S. 204, 214 (1945) (“Courts of bankruptcy are courts of equity and exercise all equitable powers unless prohibited by the Bankruptcy Act.”) (citations omitted).

\textsuperscript{33} This general proposition also was articulated by the Supreme Court in one of its last cases decided under the Bankruptcy Act. \textit{See Butner v. United States}, 440 U.S. 48, 55–56 (1979) (“The equity powers of the bankruptcy court play an important part in the administration of bankrupt estates in countless situations in which the judge is required to deal with particular, individualized problems. But undefined considerations of equity provide no basis for adoption of a uniform federal rule affording mortgagees an automatic interest in the rents as soon as the mortgagor is declared bankrupt.”).
391 F.3d 190, 236 (3d Cir. 2004), as amended (Feb. 23, 2005) (vacating and remanding a decision of the bankruptcy court that expanded the scope of a channeling injunction and stating that “the Bankruptcy Court relied upon § 105(a) to achieve a result inconsistent with § 524(g)(4)(A)”; In re Saxman, 325 F.3d 1168, 1170, 1174 (9th Cir. 2003) (holding that “bankruptcy courts may partially discharge student debt pursuant to their equitable authority under 11 U.S.C. § 105(a)” as “§ 523(a)(8) is silent with respect to whether the bankruptcy court may partially discharge the loan”).

In 2014, the Supreme Court further addressed the equitable powers of bankruptcy courts when faced with a specific statutory provision. In Law v. Siegel, the Court made clear that, although bankruptcy courts possess statutory and inherent powers, they “may not contravene specific statutory provisions” in exercising them. 571 U.S. 415, 420–21. It held that the bankruptcy court could not surcharge a debtor’s statutorily exempt property on equitable grounds, though it recognized that the bankruptcy court could impose sanctions against the debtor under Federal Rule of Bankruptcy Procedure 9011(c)(2). 34 The Court concluded that the Bankruptcy Code does not confer on bankruptcy courts “a general, equitable power … to deny exemptions based on a debtor’s bad-faith conduct.”

Subsequent case law has confirmed Siegel’s edict, while observing that such a ruling does not strip bankruptcy courts of their powers under section 105(a) of the Bankruptcy Code. See, e.g., In re Arthur B. Adler & Assocs., Ltd., 588 B.R. 864, 874 (Bankr. N.D. Ill. 2018) (“[T]he Supreme Court in Siegel explicitly stated that a bankruptcy court may not exercise its inherent powers in

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34 Siegel, 571 U.S. at 427. The Supreme Court further observed that bankruptcy courts “may also possess further sanctioning authority under either § 105(a) or its inherent powers.” Id. See also 2 Collier on Bankruptcy ¶ 105.01 (16th ed. 2019) (discussing Siegal opinion).
35 Siegel, 571 U.S. at 425.
contravention of the statutory provisions of the Bankruptcy Code. … In that case, the Supreme Court determined that a bankruptcy court allowing the surcharge of a debtor’s exemption had exceeded its statutory and inherent authority. … However, that decision did not strip bankruptcy courts of their authority pursuant to 11 U.S.C. § 105(a). Rather, it merely requires a bankruptcy court to be mindful of the remedies it crafts to avoid contravening the Bankruptcy Code.”) (citations omitted); In re Brown, 851 F.3d 619, 625 (6th Cir.), cert. denied sub nom. Brown v. Ellmann, 138 S. Ct. 328, 199 L. Ed. 2d 212 (2017) (emphasis in the original) (“Law [v. Siegel] does not strip bankruptcy courts of their ability to interpret the Bankruptcy Code; it merely reinforces the common-sense notion that bankruptcy courts may not use their discretionary powers to reach results that are inconsistent with the clear meaning of the Bankruptcy Code.”).

The language of the Bankruptcy Code and Supreme Court precedent unquestionably continue the tradition of bankruptcy courts as courts of equity. That general proposition does not, however, end the inquiry. Questions remain concerning the appropriate scope of the bankruptcy courts’ equitable powers. Some commentators continue to debate whether the bankruptcy courts should even have equitable powers, while others suggest that changes are needed to vest the bankruptcy courts with more flexibility in the exercise of such powers. The papers that follow thoughtfully explore many of these issues.

IV. Potential Future Issues and Developments

The American Bankruptcy Law Journal Symposium brings together four distinguished academics to consider the issue of the equitable powers of the bankruptcy courts forty years after the enactment of the Bankruptcy Code. Professors Coordes, Dick, Markell, and Westbrook each analyze a different, yet complementary, aspect of the bankruptcy courts’ equitable powers. Their
research and perspectives make meaningful contributions to the literature and help move the conversation forward.

For example, Professor Coordes approaches the issue through the lens of statutory interpretation. She argues that “bankruptcy judges should have particular equity powers because exercising these powers is part and parcel of the function of any entity tasked with statutory interpretation.” To support her thesis, Professor Coordes examines “other entities that regularly engage in statutory interpretation, including Article I courts such as the Tax Court ….”

Professor Dick offers data from a qualitative survey of bankruptcy judges concerning “their beliefs regarding, and approaches to, the equitable and other discretionary powers of the bankruptcy court.” She uses the survey to try to gain a better understanding of “how bankruptcy judges perceive bankruptcy courts’ equitable powers, and whether and to what extent they view them as separate and distinct from courts’ broader discretion and decision-making authority.” Her survey results should inform the conversation with a more in-depth understanding of issues facing bankruptcy judges in the exercise of their equitable powers.

Professor Markell addresses this issue from a structural perspective, considering “what it means to call a body or panel a ‘court,’ and what is added (or changed) by adding the modifier ‘of equity.’” His paper explores the concept of a statutory court and whether it has powers beyond those specifically granted in that court’s authorizing text. He concludes that, as a court, a bankruptcy court has the inherent powers of any court, subject of course to limits the Bankruptcy

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36 Laura N. Coordes, *Code-Based Courts and Equity Powers*, abstract (attached to this preface).
37 *Id.*
39 *Id.*
40 Bruce A. Markell, *Courting Equity in Bankruptcy*, abstract (attached to this preface). A draft of Professor Markell’s Symposium paper follows the four abstracts for the four papers in the symposium.
Code and the Constitution impose. With respect to equity, Professor Markell expands his examination to identify and justify actions and practices taken by bankruptcy courts in the name of equity, from allowing and disallowing claims based on equitable principles to improvising practices and remedies consistent with the Bankruptcy Code, but not precisely specified therein. He concludes, however, that his investigations “lead to a different take on the powers of a bankruptcy court to address situations in which there are no clear answers, but also reaffirms the primacy of the text of the legislation creating the courts when practical solutions are prohibited by the Code’s text.”

Professor Westbrook assesses the particular need for the bankruptcy courts’ equitable powers in the context of chapter 11 cases. He explains that “[a]dapting Chapter 11 to our rapidly changing social and financial world requires addition of statutory authority for bankruptcy judges to exercise discretion (or ‘equity’) in favor of those Congressional goals proclaimed but not yet codified.” He considers current trends in statutory interpretation and how a “plain meaning” approach might constrain the necessary evolution of the Bankruptcy Code. Consequently, he suggests a “need to codify discretion to consider and balance specified public interests.”

Each of these academic papers offers a thoughtful analysis of an issue that impacts bankruptcy courts, debtors, and creditors on an almost daily basis. Bankruptcy courts must continue to assess the use of their equitable powers on a case-by-case basis in accordance with the Bankruptcy Code and existing case law. As commentators, legislators, and courts consider the appropriate scope of bankruptcy courts’ equitable powers, these papers add new and important perspectives to that conversation.

41 Id.
42 Jay L. Westbrook, abstract (attached to this preface).
43 Id.
Outside of bankruptcy, courts and administrative agencies use equitable principles to fashion relief in accordance with the dictates of circumstances and policy. Although this ability to “do equity” is sometimes expressly delegated to these bodies, there are plenty of circumstances where the “delegation” of equity powers is implicit and indirect.

Within the bankruptcy context, there is ongoing disagreement over the extent, scope, and even existence of a bankruptcy court’s equity powers. Some scholars have argued that equity powers have no basis in the Bankruptcy Code and that therefore, a court’s ability to exercise equitable powers should be significantly cabined, if not eliminated entirely. Yet, others have argued that equitable powers should be embraced and even expanded in the bankruptcy context.

Justifications for robust equitable powers often take one of two forms: first, the Bankruptcy Code, as a statute, necessarily cannot comprehensively address every conceivable situation that arises in bankruptcy court; and second, there is no administrative agency (or equivalent) in bankruptcy designed to address situations the statutory framework does not contemplate.

This Article seeks to reframe the debate about the bankruptcy court’s equity powers as part of a larger question about the role of courts in interpreting and applying statutes. The Article will posit that bankruptcy judges should have certain equity powers, in part because exercising these powers is part and parcel of the function of any entity tasked with interpreting statutes. To support this argument, the Article will examine other entities that engage in statutory interpretation, including other Article I courts such as the Tax Court, and administrative agencies, to see when and how these entities apply equitable powers, as well as the authority they are given to exercise those powers. The Article will then consider why bankruptcy courts in particular have faced increasing scrutiny of their use of equitable powers.

Of course, no court can have unfettered discretion to simply “do equity,” and this Article will highlight some limits on the bankruptcy courts’ equitable powers. Nevertheless, as scholars and policymakers consider whether and how to update the Bankruptcy Code on the heels of its 40th anniversary, the Article will argue that we must be cognizant of ways to meld form with function and clarify that bankruptcy courts have the ability to exercise equitable powers when doing so is necessary and appropriate to their role as interpreters of the Bankruptcy Code.
Equitable Powers and Judicial Discretion: A Survey of U.S. Bankruptcy Judges

By

Diane Lourdes Dick

ABSTRACT

U.S. bankruptcy courts have been traditionally described as having “broad” and “inherent” equitable powers, with section 105(a) of the Bankruptcy Code typically cited as the current codification of such powers. Over the years, bankruptcy courts have fashioned a variety of equitable remedies in full or partial reliance on section 105(a), with some of these remedies becoming entrenched in modern bankruptcy law and practice. And, although recent judicial decisions appear to limit bankruptcy courts’ equitable powers by narrowly construing section 105(a), bankruptcy judges continue to exercise considerable equitable discretion. This is because, although courts are expected to apply the Code rather than vague principles of equity, the Code itself calls upon judges to exercise substantial discretion, with some provisions directing the court to specifically consider principles of equity. Moreover, the very nature of a bankruptcy case—with multiple parties and other stakeholders competing over scarce and dwindling resources—naturally invites courts to scrutinize claims and actions with fairness and equity in mind. All of this means that it is not always clear where the so-called inherent equitable powers end and the court’s broader judicial discretion begins.

In an effort to help clarify some of the confusion, this Article reports the results of a survey of sitting U.S. bankruptcy judges concerning their beliefs regarding, and approaches to, the equitable and other discretionary powers of the bankruptcy court. A primary goal of the survey is to understand how bankruptcy judges perceive bankruptcy courts’ equitable powers, and whether and to what extent they view them as separate and distinct from courts’ broader discretion and decision-making authority. Survey questions are designed to help understand, among other things, what judges perceive to be the sources of bankruptcy courts’ equitable powers, how they interpret and apply section 105(a), what they believe it means for a court to act in the name of equity, whether they would like more guidance from Congress or the Supreme Court regarding the scope of the court’s equitable powers, their approaches to exercising judicial discretion, and whether they have perceived a change in the level of judicial discretion that bankruptcy judges possess.

In addition to presenting and analyzing the results of the survey, the Article also highlights significant trends and important questions that emerge from survey responses. The Article concludes with a lively discussion that uses the empirical data presented in this Article to help inform the broader conceptual debates concerning the nature and extent of the bankruptcy courts’ equitable and discretionary powers.
Courting Equity in Bankruptcy
By Bruce A. Markell

Abstract

Bankruptcy courts are often referred to as courts of equity. In this paper, I want to examine this reference in detail. Specifically, I want to examine what it means to call a body or panel a “court,” and what is added (or changed) by adding the modifier “of equity.”

My investigations reveal that bestowing a body or panel with the moniker “court” assumes or requires a sophisticated apparatus and infrastructure related to binding decisionmaking. Not only do courts decide cases – that is, they decide contested allegations and apply or interpret legal rules to the allegations as decided – but they also do so in a manner which gives their decisions both legitimacy and enforceability. In United States bankruptcy, much of this work is done by borrowing concepts and structures from existing court systems. But basic competencies, such as who can appear before the bankruptcy court, how and when those may individuals appear, and how to manage and control the manner of discourse with those individuals, remains compressed in the concept of a “court” and the inherent powers possessed by any “court.”

Specifying that a court should also be a court “of equity” imbues, I maintain, a court with various powers. It first allows the court to apply the doctrines and practices developed by courts of equity in nonbankruptcy contexts, especially in the context of resolving claims against the estate. It also permits courts to create remedies and rights as directed by Congress, as with the doctrine of equitable subordination. Finally, it allows courts to make exceptions to general rules when such exceptions do not change results mandated or implied by a governing statute such as the Bankruptcy Code. One simple application of this is the traditional power of equity courts to correct their own mistakes. A more complicated application lies in the practices and customs which have evolved regarding approval and payment of attorneys.

These investigations lead to a different take on the powers of a bankruptcy court to address situations in which there are no clear answers, but also reaffirms the primacy of the text of the legislation creating the courts when practical solutions are prohibited by the Code’s text.

These investigations lead to a new take on the powers of a bankruptcy court to address situations in which there are no clear answers, but also reaffirms the primacy of the text of the legislation creating the courts when practical solutions are prohibited by the Code’s text.
Adapting Chapter 11 to our rapidly changing social and financial world requires addition of statutory authority for bankruptcy judges to exercise discretion (or “equity”) in favor of those Congressional goals proclaimed but not yet codified. The essential evolution of the Bankruptcy Code is in tension with the rise of the “plain meaning” device for statutory interpretation, which is often used to ignore any goal that is not expressly stated in the text of the statute. Yet both traditional and emerging Congressional goals may not yield specific provisions because they require balancing public interests that conflict inter se, as well as sometimes conflicting with legitimate and important private interests. Thus the need to codify discretion to consider and balance specified public interests.

The necessary authority should cover traditional goals, such as due consideration of the rights of employees and public investors. Other public interests that may require codification include court discretion in determining the relationship between arbitration and bankruptcy and in protecting tort victims, consumers, and other underrepresented stakeholders. Specific authorization of these goals will avoid grant of a too-broad discretion that might damage commercial expectations while nevertheless empowering experienced commercial judges to include these important goals in their interpretation and application of Chapter 11.
INTRODUCTION

Are bankruptcy courts properly called courts of equity? Various justices of the Supreme Court seem to assume so, but other judges and academics have asked this question in many different ways, with many different answers. The point of this article is to question whether the question is well formed. That is, can it be answered without first knowing or agreeing on what a “court” is or what “equity” means? I think not. This article thus attempts to explore these protean concepts to achieve a better understanding of what is asked by the opening question.


2 I do not write on a blank slate. Some of the key articles in this discourse are Randolph J. Haines, The Conservative Assault on Federal Equity, 88 Am. Bankr. L.J. 451 (2014); Alan M. Ahart, A Stern Reminder that the Bankruptcy Court is Not a Court of Equity, 86 Am. Bankr. L.J 191 (2012); Michael D. Sousa, Equitable Powers of a Bankruptcy Court: Federal All Writs Act and § 105 of the Code, Am. Bankr. Inst. J. at 28 (July/August 2006); Adam Levitin, Toward A Federal Common Law of Bankruptcy: Judicial Lawmaking in a Statutory Regime, 80 Am. Bankr. L.J. 1 (2006); Alan M. Ahart, The Limited Scope of Implied Powers of a Bankruptcy Judge: A Statutory Court of Bankruptcy, Not a Court of Equity, 79 Am. Bankr. L.J. 1 (2005); Steve H. Nickles & David G. Epstein, Another Way of Thinking About Section 105(a) and Other Sources of Supplemental Law Under the Bankruptcy Code, 3 Chap. L. Rev. 7 (2000); Marcia S. Kriegler, “The Bankruptcy Court is a Court Of Equity”: What Does That Mean?, 50 S.C. L. Rev. 275 (1999). All but two of these articles were written by judges, or former judges.
Start first with bankruptcy. Congress vested bankruptcy jurisdiction in Article III district courts. As “inferior courts” established by acts of Congress, district courts have the “judicial power” as provided for in the Constitution. This “power” includes equity powers. It thus follows that, unless Congress removes or limits that power when conferring jurisdiction over statutory bankruptcy cases, district courts are courts of equity when it comes to the Code. But that is trivial. District courts are courts of equity with respect to any federal statute that they are called upon to apply.

I will have more to say on what it means to be a court of equity with respect to a statutory area later, but for now, the focus is on whether the congressional permission for Article III courts to delegate bankruptcy matters to non-Article III bankruptcy judges alters this analysis. Put another way, a key question for me is whether it is permissible to delegate authority to designate bankruptcy judges as units of the district court to administer bankruptcy cases, and with that delegation transfer to the bankruptcy judges equitable powers and discretion necessary or appropriate to administer the statute at issue? Or is the fact that a collection of bankruptcy judges as a legitimate court automatically imbues them with certain equitable powers and discretion, bounded by statute and by approved methods of statutory interpretation?

COURTS

To call a body a “court” is to infuse that body with a collection of powers that cohere with the usage of “court” in legal parlance. Among these powers are the power to compel testimony and to render enforceable decrees. Adding “of equity” to “court” is generally is taken to imbue a court with different and somewhat more expansive powers than a “court of law” or a “statutory court.” I explore this distinction below.

For purposes of this article, I assume that the term “court of equity” has two discrete components: one describes a “court,” and the second is that the “court,” so described, exercises powers of “equity.” I explore these concepts separately.

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4 “The judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish.” U.S. Const., Art. III, § 1.
5 “The judicial Power shall extend to all Cases, in Law and Equity, arising under this Constitution, the Laws of the United States . . . .” U.S. Const., Art. III, § 2.
6 Title 11, United States Code. In this article, I use “Code” to refer to the Bankruptcy Code as found in title 11.
7 I don’t mean to address the thorny issues of what types of cases require determination by a court with the judicial power. Put another way, this focus of this article in not upon the limits Stern v. Marshall, 564 U.S. 462 (2011) places on bankruptcy judges. Rather, I am interested in whether Congress has permissibly created bankruptcy courts, as we know them, in such a way that they are “courts” capable of receiving a grant of equitable powers from Article III courts.
8 In this sense, I am using a bankruptcy “court” as a collective noun to describe a collection of bankruptcy judges, just as a murder of crows describes a collection of crows.
9 As noted by Professor James Pfander, the constitution speaks generally of “courts” and sparingly of “tribunals.” To address many of the problems noted in this article, Professor Pfander would distinguish between Article III courts and Article I tribunals. Professor Pfander argues that adopting such a distinction would
Statutory Powers of Courts
Courts have assumed that the bankruptcy power did not exist at common law, and that bankruptcy remedies were creatures of statute.\(^{10}\) Partial recognition of this status lies in the Constitution’s allocation of the bankruptcy power to the legislature,\(^{11}\) and the power over common law and equity matters to the courts.\(^{12}\) The current system creates statutory bankruptcy rights, and then vests the power to administer such rights in the existing Article III court system.\(^{13}\) This vesting comes with an option: the courts can delegate all bankruptcy duties to a separate system of bankruptcy judges.\(^{14}\) Examining this system can assist in determining whether bankruptcy judges exercise powers of a court of equity.

District Courts and Bankruptcy
Congress created an entire title of the United States Code to deal with bankruptcy. That title, title 11, is mostly freestanding and agnostic as to who or what administers it. It is silent on what body should administer the law. That directive comes from title 28, the title on the judiciary. In that title, Congress gave original and exclusive jurisdiction over bankruptcy cases to “the district courts.”\(^{15}\) The same section grants original but not exclusive jurisdiction over civil proceedings arising in, arising under, or related to cases under title 11 to “the district courts” as well.\(^{16}\) A “district court” is comprised of all of the district court judges appointed to a particular district.\(^{17}\) A “district judge” is someone appointed by the president and confirmed by the Senate for a particular judicial district,\(^{18}\) and who serves for life or during good behavior, whichever

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suggest[\() that Congress enjoys a degree of flexibility in creating Article I tribunals. On such a reading, the Inferior Tribunals Clause may empower Congress to create inferior “tribunals” with judges who lack Article III protections. While these tribunals must remain inferior to the Supreme Court and the judicial department, Article I does not require that they employ life-tenured judges and Article III does not formally invest these tribunals with the judicial power of the United States.


\(^{10}\) E.g., *In re Elmira Steel Co.*, 109 F. 456, 476 (N.D.N.Y. 1901) (“The provisions of the bankrupt act, which are in derogation of the common law, under which, by proceedings in invitum, parties are against their consent deprived of rights, must in their interest be construed strictly, and, as so construed, closely followed.”); *Stuart v. Hines*, 33 Iowa 60, 70 (1871) (“The act being summary in its nature, and in derogation of the common law, must receive a strict construction, and cannot be enlarged so as to include cases not provided for.”).

\(^{11}\) U.S. Const., Art I, § 8, cl. 4.

\(^{12}\) U.S. Const., Art. III.

\(^{13}\) Congress could (and at least once, in 1800, did) create a bankruptcy system that is primarily administrative, with enforcement of completed administrative decisions left to the courts.


\(^{15}\) 28 U.S.C. § 1334(a).

\(^{16}\) 28 U.S.C. § 1334(b).

\(^{17}\) 28 U.S.C. § 132(b): “Each district court shall consist of the district judge or judges for the district in regular active service.”

\(^{18}\) 28 U.S.C. § 133.
A “district judge,” as a congressionally established “inferior court” of the United States, is invested with the “judicial Power” of the United States. There is no doubt that district courts are “courts.” That means, for my purposes, that they have whatever jurisdiction Congress delegates to them (in the case of bankruptcy, whatever jurisdiction flows from section 1334), plus whatever jurisdiction is inherent in their status as a “court.” Accordingly, Congress created a bankruptcy statute using its powers under the Constitution’s bankruptcy clause, and then vested jurisdiction over that statute in the district courts, courts which have the full “judicial Power [over] all Cases, in Law and Equity.” District courts are possessed of the “judicial Power,” which gives them full equity powers with respect to matters, including bankruptcy, which come before them.

**District Courts and Referral of Delegated Jurisdiction**

Accordingly, Congress created a bankruptcy statute using its powers under the Constitution’s bankruptcy clause, and then vested jurisdiction over that statute in the district courts, courts which have the full “judicial Power [over] all Cases, in Law and Equity.” District courts are possessed of the “judicial Power,” which gives them full equity powers with respect to matters, including bankruptcy, which come before them.

The same analysis does not apply to bankruptcy judges. The source of jurisdiction for bankruptcy judges is section 157(a) of title 28. It permits, but does not require, district courts to refer “to the bankruptcy judges for the district” — not the bankruptcy court for the district — all bankruptcy cases and “any or all proceedings arising under title 11 or arising in or related to a case under title 11.” According to the statute, the judges receiving this referral “shall constitute a unit of the district court to be known as the bankruptcy court for that district.” The

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20 “The judicial power of the United States, shall be vested in one Supreme Court, and in such inferior courts as the Congress may from time to time ordain and establish.” U.S. Const., Art. III, § 1. See also 28 U.S.C. § 132(c): “the judicial power of a district court with respect to any action, suit or proceeding may be exercised by a single judge, who may preside alone and hold a regular or special session of court at the same time other sessions are held by other judges.”

21 The operative term in the statute is a “bankruptcy judge.” Section 151 of title 28 states that “In each judicial district, the bankruptcy judges in regular active service shall constitute a unit of the district court to be known as the bankruptcy court for that district.” 28 U.S.C. § 151. This statute uses “bankruptcy court” as a collective noun for the collection of all bankruptcy judges in a district; that is, the presumption is that a bankruptcy court describes a collection of judges (with the exception being one judge districts such as Montana, Alaska, or Hawaii) who have their official station in a particular judicial district. As a result, a pedant would say that the statement “I appeared before the bankruptcy court today” to be a grammatical error unless all bankruptcy judges in that district were somehow sitting en bane, or unless that bankruptcy judge had the power to commit and bind all bankruptcy judges in that district.


bankruptcy court thus receives, through the order of referral, all powers to decide bankruptcy
cases and proceedings, in accordance with the statute and with local district court rules.
Unless the equitable power is reserved in the referral, or withheld or withdrawn by the
Constitution, a statute or court rule, the bankruptcy court thus presumptively receives all
equitable powers over cases and proceedings referred as had the district court that referred them.
As stated in section 152(b), “[b]ankruptcy judges shall serve as judicial officers of the United
States district court established under Article III of the Constitution.”
The text of section 157(a) leaves little doubt that Congress permitted the district courts to
delegate their entire bankruptcy jurisdiction to bankruptcy judges. There is, however, much
doubt about how much of that delegation is permissible under the Constitution. Bankruptcy
judges are not appointed under Article III, and thus do not have the full “judicial Power” granted
district court judges under section 2 of Article III of the Constitution. Cases from Northern
Pipeline24 to Stern25 to Wellness International26 have struggled with exactly what types of cases
require decision by a judge holding the “judicial Power,” and what cases can be referred, and
decided, by judges who do not wield the “judicial Power.”
That debate has consumed much paper and ink (and electrons). I do not wish to wade into that
debate here. No one doubts that Congress could not create a court, give it jurisdiction over
traditional equitable cases, and then fail to give the judges of that court all of the protections of
Article III.27 Accordingly, Congress created a bankruptcy statute using its powers under the
Constitution’s bankruptcy clause, and then vested jurisdiction over that statute in the district
courts, courts which have the full “judicial Power [over] all Cases, in Law and Equity.” District
courts are courts with equitable powers with initial bankruptcy jurisdiction. These courts may,
but are not compelled, to refer this power to the bankruptcy judges in their districts.

Bankruptcy Courts as "Courts"
Under the delegation permitted by section 157(a), bankruptcy judges can, according to title 28,
make final decisions on matters of statutory bankruptcy law (at least to the extent that the
 provision does not usurp or overlap a cognate common law doctrine).28 That is the essence of
section 157(b)’s grant of the power to bankruptcy judges to “hear and determine all cases under
title 11 and all core proceedings arising under title 11, or arising in a case under title 11.”29 This
power is supplemented by section 151(a):

27 Although I argue that this is what Congress likely has done in 11 U.S.C. § 502(b)(1). See TAN
xxx infra.
29 28 U.S.C. § 157(b)(emphasis supplied). Matters arise under title 11 if a proceeding seeks relief
available only under a substantive Code provision (e.g., a preference action under § 547). Bethlahmy, IRA
v. Kuhlman (In re ACI-HDT Supply Co.), 205 B.R. 231 (B.A.P. 9th Cir. 1997); Ehrlich v. Am. Express
Matters arise in a case if the proceeding involves the administration and structuring of the estate
(e.g., attorney fee application; order confirming plan; borrowing order) that would have no existence but
for the bankruptcy case. See In re Wood, 825 F.2d 90, 97 (5th Cir. 1987); Dall v. Bank One, Chicago (In re
Each bankruptcy judge, as a judicial officer of the district court, may exercise the authority conferred under this chapter with respect to any action, suit, or proceeding and may preside alone and hold a regular or special session of the court, except as otherwise provided by law or by rule or order of the district court.30

So bankruptcy judges can make binding rulings on core matters31 such as motions related to the automatic stay or as to the scope of the discharge, matters alien to the common law but commonplace under the Code. These binding rules are subject to appeal, not de novo review, and thus factual findings, for example, are subject to clearly erroneous standard of review.32 The powers granted to bankruptcy judges do not stop there. Congress realized that bankruptcy judges would have to, in the exercise of their duties, decide matters that were not statutory — the amount owed to a creditor, or the existence of a perfected lien. Bankruptcy judges were given the power to “hear,” but not determine, these matters, under the so-called “related” matter jurisdiction.33 The statutory norm is that these matters are to be the subject of a bankruptcy judge’s report and recommendation to the district court, which the district court would review de novo, even to the extent the report examined and resolved factual matters in reaching its recommendation.34 After Wellness International, however, many (if not most) of these related matters are heard and determined by consent of the parties, so that appeal would be the proper method of review.35

As a result, bankruptcy judges can finally determine some matters, even without the advance consent of the parties bound. Add to that the power to compel testimony,36 and thus a collection of bankruptcy judges in a district has sufficient attributes of a “court.”

“Inherent” Powers of Courts

Not everything a bankruptcy judge does is specified by statute. From ordinary aspects such as hours of operation, to everyday matters such as specifying who can appear, to the extraordinary power of contempt, many aspects of what bankruptcy judges do is not specified by statute. For courts other than bankruptcy court, the powers not specifically granted are often collectively referred to as “inherent” powers. Do bankruptcy judges have those powers?

31 Congress specified core matters in 28 U.S.C. § 157(b)(2)(A)-(P). The Supreme Court has already determined that this list is over broad to the extent that a compulsory counterclaim to an action brought by the estate is a claim that can be decided only by a court possessing the judicial power of the United States. Stern v. Marshall, 564 U.S. 462 (2011).
32 Under Bankruptcy Rule 7052, as supplemented by Bankruptcy Rule 9014(c), all factual findings in adversary proceedings and contested matters are subject to Fed. R. Civ. P. 52. That rules states that: “Findings of fact, whether based on oral or other evidence, must not be set aside unless clearly erroneous, and the reviewing court must give due regard to the trial court’s opportunity to judge the witnesses’ credibility.” Fed. R. Civ. P. 52(a)(6).
35 This outcome is anticipated by the statute. It provides that “the district court, with the consent of all the parties to the proceeding, may refer a proceeding related to a case under title 11 to a bankruptcy judge to hear and determine . . . .” 28 U.S.C. § 157(c)(2)
Inherent Powers of District Courts
The Supreme Court addressed federal courts’ “inherent power” to manage their dockets and enforce their orders in Chambers v. NASCO, Inc.37 There, Chambers was the sole shareholder of a company involved in nasty contract litigation with NASCO. During the litigation, Chambers misbehaved in numerous ways. He tried to deprive the court of jurisdiction by selling the property subject to the contract to a third party, defied a preliminary injunction directing him to allow NASCO to inspect corporate records, and, with the help of his attorney, filed meritless motions and pleadings along with other delaying tactics.38 After losing an appeal in the initial litigation, Chambers found himself before the district court on remand having to answer for his misdeeds. Although the district court refused to impose sanctions under 28 U.S.C. § 1927 or Federal Rule of Civil Procedure 11, it did impose sanctions under its inherent power for Chambers’ bad faith conduct.39 And the damages were were significant. The district court awarded NASCO all of its attorneys’ fees and costs, totaling close to $1 million.

The Supreme Court affirmed. In doing so, the Court relied on tradition and necessity to find some power for the court to perform its duties. The Court stated, “[i]t has long been understood that ‘[c]ertain implied powers must necessarily result to our Courts of justice from the nature of their institution, ‘powers’ which cannot be dispensed with in a Court, because they are necessary to the exercise of all others.’”40 According to the Court, “[t]hese powers are ‘governed not by rule or statute but by the control necessarily vested in courts to manage their own affairs so as to achieve the orderly and expeditious disposition of cases.’”41 What are these powers? Historically, they have included the power to regulate appearances before the court (including the power to deny, permanently or temporarily, the privilege of attorneys to appear before a court)42 and the power of contempt.43

39 Chambers v. NASCO, 501 U.S. 32, 41-42 (1991). Rule 11 could not be used, since Chambers had not signed any documents. Section 1927 only applies to attorneys, and so it was also unavailable.
42 The power is one which ought to be exercised with great caution, but which is, we think, incidental to all Courts, and is necessary for the preservation of decorum, and for the respectability of the profession.
44 The power to punish for contempts is inherent in all courts; its existence is essential to the preservation of order in judicial proceedings, and to the enforcement of the judgments, orders, and writs of the courts, and consequently to the due administration of justice. The moment the courts of the United States were called into existence and invested with jurisdiction over any subject, they became possessed of this power.
45 Ex parte Robinson, 86 U.S. 505, 510 (1873) (Field, J.). In United States v. Hudson and Goodwin, 11 U.S. (7 Cranch) 32, 34 (1812), the Court held that inherent powers, under the name of contempt, did not extend to crimes not specified by statute or recognized at common law, but nonetheless said that:
Inherent Powers of Bankruptcy Judges

Do bankruptcy judges enjoy similar inherent powers? Since Chambers, the Supreme Court has toyed with the issue. In Marrama v. Citizens Bank of Massachusetts, the Court was faced with a chapter 7 debtor’s arguably bad faith attempt to convert his case to one under chapter 7, a conversion that would have reclaimed control of his assets and arguably protected him from claims of repetitious fraudulent transfers. The chapter 7 debtor argued that the Code gave him the absolute right to convert. After all, section 706(a) states that “The [chapter 7] debtor may convert a case under this chapter to a case under chapter 11, 12, or 13 of this title at any time . . . .” a right congressional history characterized as “absolute.”

The Marrama majority relied primarily on the “abuse of process” language contained in section 105. As stated by the Court:

the broad authority granted to bankruptcy judges to take any action that is necessary or appropriate “to prevent an abuse of process” described in § 105(a) of the Code, is surely adequate to authorize an immediate denial of a motion to convert filed under § 706 in lieu of a conversion order that merely postpones the allowance of equivalent relief and may provide a debtor with an opportunity to take action prejudicial to creditors.

But the Court hinted at an alternate holding based upon inherent authority. The argument was sparse but complete:

Indeed, . . . even if § 105(a) had not been enacted, the inherent power of every federal court to sanction “abusive litigation practices,” . . . . might well provide an adequate justification for a prompt, rather than a delayed, ruling on an unmeritorious attempt to qualify as a debtor under Chapter 13.

But the brevity of the observation, combined with its less-than-unequivocal “might well provide” qualification left the issue unsettled.

The Court’s reticence to declare inherent powers in bankruptcy judges surfaced again in Law v. Siegel, a case in which a fraudulent debtor tried to hornswoggle the court into believing in phantom mortgages to save his house. After much wasteful litigation, Law’s frustrated trustee sought to surcharge Law’s homestead to pay for his excessive and unjustified attempts to

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Certain implied powers must necessarily result to our Courts of justice from the nature of their institution. . . . To fine for contempt—imprison for contumacy—inform the observance of order, &c. are powers which cannot be dispensed with in a Court, because they are necessary to the exercise of all others: and so far our Courts no doubt possess powers not immediately derived from statute . . . .

perpetuate his fraud. The lower courts agreed, but the Court took the case, ruling for Law primarily on the basis that nothing in the Code permitted a trustee to surcharge a state-law provided homestead.

In its analysis, the Court flirted with declaring bankruptcy judges had inherent powers. It twice referred to inherent powers of bankruptcy courts, but each time conditioned the bankruptcy court’s possession of inherent powers with “may” — language indicating that the issue has not yet been decided.\textsuperscript{50}

Despite the Court’s dithering, many lower courts have found that bankruptcy courts have inherent powers similar to those held by district courts.\textsuperscript{51} But some have not. In particular, some article III courts have questioned as to whether Congress’ designation of the bankruptcy judges in a district as a “court” is accurate. \textit{In re Hipp} is the most famous. There, the court stated it was unsure even that today’s bankruptcy courts are “courts” in a generic sense not defined strictly by Article III. . . . In short, today’s bankruptcy courts are arguably at least as much like magistrates or even administrative agencies as they are like other non-Article III courts.\textsuperscript{52}

The Seventh Circuit Court of Appeals echoed this sentiment after \textit{Stern}. In \textit{Ortiz v. Aurora Health Care, Inc. (In re Ortiz)},\textsuperscript{53} Aurora, a medical health care provider, had filed over 3,200 proofs of claim against Wisconsin-based debtors. Each of these proofs of claim allegedly violated the medical privacy rights of the debtors under Wisconsin law. The bankruptcy judge found clear violations, and entered summary judgment against Aurora. A direct appeal to the Seventh Circuit was taken.

The Seventh Circuit dismissed for lack of jurisdiction. Key to its dismissal was that the case involved application of Wisconsin law, something that the Seventh Circuit believed \textit{Stern} required the “judicial Power” to decide. Since bankruptcy judges do not possess the “judicial Power,” the bankruptcy judge’s decision regarding Wisconsin law unconnected to bankruptcy was not supported by the Constitution, and was no more an order that could be appealed from than some jottings on a paper bag.

When the alternate argument was made that the bankruptcy court had the inherent power to regulate its claims docket by sanctioning someone who filed proofs of claim that violated state law, the Seventh Circuit was unimpressed.

\textbf{Aurora argues that the debtors’ claims are different than Vickie’s counterclaim [in \textit{Stern}] because the debtors’ claims go to the heart of the

\textsuperscript{50} Cf. \textit{Law v. Siegel}, 571 U.S. 415, 421 (2014) (stating that bankruptcy court “may also possess ‘inherent power . . . to sanction “abusive litigation practices.’”’ (emphasis supplied)), and \textit{id.} at 427 (“The court \textit{may} also possess further sanctioning authority under either § 105(a) or its inherent powers.”) (emphasis supplied).

\textsuperscript{51} See, e.g., Gowdy v. Mitchell (\textit{In re Ocean Warrior, Inc.}), 835 F.3d 1310, 1316–17 (11th Cir. 2016) (“Civil contempt power is inherent in bankruptcy courts since all courts have authority to enforce compliance with their lawful orders.”); Mapother & Mapother, P.S.C. v. Cooper (\textit{In re Downs}), 103 F.3d 472, 477 (6th Cir. 1996) (“Bankruptcy courts, like Article III courts, enjoy inherent power to sanction parties for improper conduct.”).


\textsuperscript{53} 665 F.3d 906 (7th Cir. 2011).
bankruptcy judge’s management of its Chapter 13 cases. Every court, it maintains, has authority to resolve disputes claiming that the way one party acted in the course of the court’s proceedings violated another party’s rights. Yet Aurora assumes that bankruptcy judges are akin to Article III judges by citing cases involving not legislative courts but Article III courts.54

Although the Seventh Circuit did not state so explicitly, its last sentence certainly leaves the impression that inherent powers of regular courts should not be assumed to inhere in “legislative” courts such as those comprised of bankruptcy judges. More recently, the Ninth Circuit Court of Appeals faced the issue of whether a bankruptcy appellate panel was a “court established by Act of Congress.”55 In In re Ozenne, a majority held it was not (and thus found it had no powers under the All Writs act to deal with a mandamus issue). The opinion was later neutered by an en banc opinion finding jurisdiction did not exist even if the bankruptcy appellate panel was a court, and thus the court evaded the issue.56 The initial opinion, however, was not “depublished,” leaving its logic for another day. These cases may well be outliers. As stated in Collier on Bankruptcy: “The majority of cases conclude that all courts, whether created pursuant to Article I or Article III of the Constitution, have inherent civil contempt power to enforce compliance with their lawful judicial orders, and no specific statute is required to invest a court with civil contempt power.”57 But, as shown by Hipp, Ortiz and Ozenne, doubt remains.

Section 105 and Contempt

Of course in bankruptcy, there is also section 105. Subsection (a) of that statute states that:

The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title. No provision of this title providing for the raising of an issue by a party in interest shall be construed to preclude the court from, sua sponte, taking any action or making any determination necessary or appropriate to enforce or implement court orders or rules, or to prevent an abuse of process.58

Section 105’s text would seem to grant to bankruptcy courts the powers generally bundled up and referred to as the inherent powers, including the contempt power.59 Indeed, many courts

54 Ortiz v. Aurora Health Care, Inc. (In re Ortiz), 665 F.3d 906, 913 (7th Cir. 2011).
55 In re Ozenne, 818 F.3d 514 (9th Cir.), reh’g en banc granted, 828 F.3d 1012 (9th Cir. 2016), and on reh’g en banc, 841 F.3d 810 (9th Cir. 2016), cert. denied sub nom. Ozenne v. Chase Manhattan Bank, 137 S. Ct. 1589(2017).
56 In re Ozenne, 841 F.3d 810 (9th Cir. 2016) (en banc), cert. denied sub nom. Ozenne v. Chase Manhattan Bank, 137 S. Ct. 1589 (2017).
57 2 COLLIER ON BANKRUPTCY ¶ 105.02[1][a] (Richard Levin & Henry Summers, eds., 2019). As stated in a recent case from the Eleventh Circuit: “Accordingly, any court—bankruptcy court included—has inherent powers to punish contempt against it, as a means of protecting itself as an institution.” Green Point Credit, LLC v. McLean (In re McLean), 794 F.3d 1313, 1324 (11th Cir. 2015).
59 See, e.g., Alderwoods Grp., Inc. v. Garcia, 682 F.3d 958, 967 n.18 (11th Cir. 2012) (“Civil contempt power is inherent in bankruptcy courts since all courts have authority to enforce compliance with their lawful orders.”) (citation omitted); Joubert v. ABN Mortg. Group, Inc. (In re Joubert), 411 F.3d 452, 455 (3d Cir. 2005) (stating that section 105 provides bankruptcy courts with a contempt remedy); Jones v.
have looked at section 105 and found that it preserves (if you believe in inherent powers)60 or grants (if you are a textualist) at least civil contempt power to bankruptcy courts.61 And this residual contempt power is used to justify such actions as remedying discharge violations to levying fines on errant lawyers to penalizing creditors for noncompliance with the Bankruptcy Rules.62

Section 105 could, however, be broader. For one thing, it does not specifically grant express contempt powers to bankruptcy judges — something Congress thought necessary or appropriate for non-Article III magistrate judges. Section 636(e) of title 28 states that:

(1) In general.—A United States magistrate judge serving under this chapter shall have within the territorial jurisdiction prescribed by the appointment of such magistrate judge the power to exercise contempt authority as set forth in this subsection.63

Bank of Santa Fe (In re Courtesy Inns, Ltd., Inc.), 40 F.3d 1084, 1089, 32 C.B.C.2d 498, 506 (10th Cir. 1994) (“We believe, and hold, that [Section] 105 intended to imbue the bankruptcy courts with the inherent power recognized by the Supreme Court in [Chambers v. NASCO, Inc., 501 U.S. 32, 111 S. Ct. 2123, 115 L. Ed. 2d 27 (1991)].”); Mapother & Mapother, P.S.C. v. Cooper (In re Downs), 103 F.3d 472, 477 (6th Cir. 1996) (“Bankruptcy courts, like Article III courts, enjoy inherent power to sanction parties for improper conduct.”).

60 The inherent powers of federal courts are those which “are necessary to the exercise of all others.” United States v. Hudson, 7 Cranch 32, 34, 3 L.Ed. 259 (1812). The most prominent of these is the contempt sanction, “which a judge must have and exercise in protecting the due and orderly administration of justice and in maintaining the authority and dignity of the court . . . .”


61 See, e.g., Alderwoods Grp., Inc. v. Garcia, 682 F.3d 958, 967 n.18 (11th Cir. 2012) (“Civil contempt power is inherent in bankruptcy courts since all courts have authority to enforce compliance with their lawful orders.”) (citation omitted); Price v. Lehtinen (In re Lehtinen), 564 F.3d 1052, 1058 (9th Cir. 2009); Joubert v. ABN Mortg. Group, Inc. (In re Joubert), 411 F.3d 452, 455 (3d Cir. 2005) (stating that section 105 provides bankruptcy courts with a contempt remedy); Jones v. Bank of Santa Fe (In re Courtesy Inns, Ltd., Inc.), 40 F.3d 1084, 1089, 32 C.B.C.2d 498, 506 (10th Cir. 1994) (“We believe, and hold, that [Section] 105 intended to imbue the bankruptcy courts with the inherent power recognized by the Supreme Court in [Chambers v. NASCO, Inc., 501 U.S. 32, 111 S. Ct. 2123, 115 L. Ed. 2d 27 (1991)].”); Mapother & Mapother, P.S.C. v. Cooper (In re Downs), 103 F.3d 472, 477 (6th Cir. 1996) (“Bankruptcy courts, like Article III courts, enjoy inherent power to sanction parties for improper conduct.”).

The Ninth Circuit seems to find power to impose punitive penalties so long as they are not “serious.” Knupfer v. Lindblade (In re Dyer), 322 F.3d 1178, 1193 (9th Cir. 2003) (“Although “relatively mild” non-compensatory fines may be necessary under some circumstances, . . . the language of § 105(a) simply does not allow for the serious punitive penalties here assessed (a minimum of $50,000 and, under the trustee’s theory, over $200,000). As we did in Hanshaw, we leave for another day the development of a precise definition of the term “serious” punitive (criminal) sanctions.”).


This power includes “the power to punish summarily by fine or imprisonment, or both, such
contempt of the authority of such magistrate judge constituting misbehavior of any person in the
magistrate judge’s presence so as to obstruct the administration of justice,” as well as the
ability to “exercise the civil contempt authority of the district court.”

Scary Issues

Even if contempt powers were provided for bankruptcy judges by statute, there would remain a
problem: to what extent are contempt and other inherent powers essential and nonassignable
components of the judicial power of the United States? When viewed in this light, issues
seemingly simple become maddeningly complex. Does a bankruptcy judge have the power to
impose the broad range of penalties associated with the contempt power? In Chowdhury v
Hansmeier, for example, the Minnesota Bankruptcy Judge had found parties in contempt for
refusing to comply with post-judgment discovery, and, after many hearings, imposed a daily fine
for compliance, to be paid to an opposing party. The bankruptcy court also ordered civil
incarceration until compliance, but had prepared a report and recommendation for the district
court judge. The District Court reversed the daily fine to the extent payable to a party (coercive
fines, it noted, are payable only after certain findings are made, and then only into the court’s
registry), but accepted the incarceration recommendation and issued warrants for the
contemnor. Evidently, the bankruptcy court drew the line at jailing parties, but without any
clear reason why, perhaps deciding that loss of physical freedom is something reserved to those
wielding the judicial power of the United States.

This suggests that certain punitive sanctions, short of incarceration, might be permissible if
specifically granted. For example, does it matter if any penalty imposed is specifically
authorized by a text, such as Rule 9011? Does it matter if the penalty is authorized by text and
relates to something that could only exist in bankruptcy? If a bankruptcy judge possess inherent
powers, do those powers reach a limit if exercise of them results in a penalty authorized only by
common law and not by statute?

Finally, and this is the scary, elemental issue, does the judicial power include the power to find
facts that are entitled to deference by courts wielding the judicial power? That is, can a
bankruptcy judge find malign intent, and have that finding reviewed under a clear error or clearly
erroneous standard by a reviewing district judge? Have it respected in another action involving

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64 28 U.S.C. § 636(e)(2). Significantly, the criminal contempt power is limited by paragraph (5)
which states that “The sentence imposed by a magistrate judge for any criminal contempt provided for in
paragraphs (2) and (3) shall not exceed the penalties for a Class C misdemeanor as set forth in sections
3581(b)(8) and 3571(b)(6) of title 18.” 28 U.S.C. § 636(e)(5).


69 See, e.g., Bessette v. Avco Financial Services, 230 F.3d 439, 445 (1st Cir. 2000) (noting that
“bankruptcy courts across the country have appropriately used their statutory contempt powers [to award]
actual damages, attorney fees, and punitive damages” for violations of § 524); In re Perviz, 302 B.R. 357,
372 (Bankr. N.D. Ohio 2003) (“Bankruptcy courts have the inherent power to punish parties for their
contumacious violation of the discharge injunction through the imposition of punitive damages.”); In re
Vazquez, 221 B.R. 222, 231 (Bankr. N.D. Ill. 1998) (awarding punitive damages pursuant to § 105).
common facts? I leave these questions for another time, as the simple designation of a collection of bankruptcy judges as a “bankruptcy court” does not answer these questions. Nor, as will next be seen, does applying the modifier “of equity” to the term “court.”

**Summary of the Powers of a Bankruptcy Judge**

Bankruptcy judges from a particular district form a tribunal Congress designated as a court. Congress gave these judges the jurisdiction and power to decided matters of bankruptcy, a subject alien to the common law. Bankruptcy involves matters such as the application of the automatic stay to existing and potential litigation, and the vindication of the discharge; these courts can enter final orders in these matters, with their factual findings subject only to clearly erroneous review.

These collection of judges, these courts, have not only the specifically delegated powers in title 28, but also inherent powers to run their tribunals. Much as the Supreme Court has found that Congress, a non-judicial body, has inherent powers to achieve its goals, bankruptcy courts have inherent powers to run their courts. These powers either come from their very existence as a body or tribunal charged with administering the bankruptcy laws, or from referral by district courts — referrals provided for and blessed by Congress.

In addition, Congressionally-delegated bodies have given to bankruptcy courts the power to manage discovery, to compel testimony, and to take evidence, all subject to the same rules applicable to district courts.

**EQUITY**

As noted above, bankruptcy courts and their predecessors are often been called “courts of equity.” The “courts” part of that locution has been discussed above. The addition of the words “of equity” have lead to much discussion and debate.

One cause of this confusion is that “equity” does not have a unique or standard definition. A good start on the many definitions of equity is Professor Samuel Bray’s definition in *A Student’s Guide to the Meanings of “Equity.”* In this short piece, Professor Bray sets out three variations of the definition of equity:

- **equity, n.**
  1. The recognition of an exception to a general rule.
  3. The doctrines and remedies developed in the English courts of equity, especially the Court of Chancery.

I will take these in reverse order in an effort to discern whether bankruptcy courts are courts “of equity” as this definition describes.

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70 A bankruptcy judge, for example, could find a debt non dischargeable for fraud, but not liquidate the claim. One of the elements of fraud typically is injury. Would a state court in a later action in which the amount was at issue have to give issue preclusive effect to the bankruptcy court’s finding that there was injury? Or a court could find a home’s value fit within a homestead exception – what would be the issue preclusive effect on state taxing agencies of that finding of value?

Equity's Doctrines and Remedies

Professor Bray’s third definition of “equity” is that of “doctrines and remedies developed in the English courts of equity, especially the Court of Chancery.” In this sense, bankruptcy courts are indisputably courts of equity. This is shown by the scope of the definition of property of the estate, the definition of “claim,” and by the claims resolution process.

Upon commencement of a case, an estate is created. So says section 541(a).72 That estate, in turn, is comprised of “all legal or equitable interests of the debtor in property.”73 As a result, to the extent that the doctrines developed in equity create property rights,74 section 541(a)(1) transfers those property rights into the bankruptcy estate. They then within the exclusive jurisdiction of the bankruptcy court.75

Bankruptcy courts not only have jurisdiction over the debtor’s equitable interests in property, but also over equitable claims that may be asserted against the debtor and the estate created by section 541(a). Section 101(5)’s definition of “claim” includes all “equitable” claims, and the discharges granted under the various chapters cover all “claims.”76

Finally, Congress set up the claims resolution process to allow bankruptcy judges to apply equitable doctrines to defeat or reduce asserted claims, both in the allowance process77 and otherwise.78 Section 502(b)(1), for example, states that a bankruptcy judge may disallow a claim if “such claim is unenforceable against the debtor and property of the debtor, under any agreement or applicable law for a reason other than because such claim is contingent or unmatured.”79 One class of objections under nonbankruptcy law would be those objections a

72 “(a) The commencement of a case . . . creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held: [¶] (1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.” 11 U.S.C. § 541(a)(1).

73 11 U.S.C. § 541(a)

74 An exception lies in section 541(d), which excludes any equitable interest in property from passing into the estate if the debtor held only legal title, without also possessing any equitable interest in the property to which the debtor held title. 11 U.S.C. § 541(d).

75 28 U.S.C. § 1334(e)(1) (district court has exclusive jurisdiction “of all the property, wherever located, of the debtor as of the commencement of such case, and of property of the estate.”). This of course assumes that the district court has referred (and can refer) its jurisdiction over such property to the bankruptcy court under the referral authorization contained in 28 U.S.C. § 157(a).

76 11 U.S.C. §§ 727(b) (“a discharge under subsection (a) of this section discharges the debtor from all debts that arose before the date of the order for relief under this chapter, and any liability on a claim that is determined under section 502 of this title as if such claim had arisen before the commencement of the case”); 1141(d)(1)(A) (“the confirmation of a plan—[¶] (A) discharges the debtor from any debt that arose before the date of such confirmation.”); 1228(a) (“after completion by the debtor of all payments under the plan, . . . the court shall grant the debtor a discharge of all debts provided for by the plan, allowed under section 503 of this title, or disallowed under section 502 of this title”); 1328(a) (“as soon as practicable after completion by the debtor of all payments under the plan, . . . the court shall grant the debtor a discharge of all debts provided for by the plan or disallowed under section 502 of this title”).

Section 101(12) states that “The term ‘debt’ means liability on a claim.”

77 11 U.S.C. § 502(b)(2)


nonbankruptcy court, sitting in or apply equity, could employ to reject the claim or reduce its amount. Put another way, the broad phrasing of section 502(b)(1) gives a bankruptcy judge access to the same panoply of reasons to disallow a claim as would be available to a state court judge or a federal district court judge. This broad vesting of powers to decide claims on the same basis as under nonbankruptcy law thus vests bankruptcy judge with the powers of a court of equity, including invocation of such traditional equitable defenses as fraud, duress, and mistake.

**Equity's Moral Readings**

Professor Bray’s second entry for equity is that of “[a] moral reading of the law.” I take this to mean that a court, acting under this sense of “equity,” has the power to create rights and remedies responsive to particular situations even though no legislation addresses it, and no precedent supports it. The right or remedy responds to a need to adjust rights or expectations so that relations or rights are just and fair. Professor Bray’s example is *Moses v. Macferlan,* in which an endorser of four notes paid the amount of the notes into court, and then sought to enforce an oral indemnity to compel return of the funds, as the indemnity was given to induce him to give the endorsements in the first place. The endorser could not find a right at common law or a remedy in a statute to address his particular case, but Judge Mansfield, speaking for Kings’ Bench, nonetheless held that “the gist of this kind of action is, that the defendant, upon the circumstances of the case, is obliged by the ties of natural justice and equity to refund the money.” The *Restatement (Third) of Restitution and Unjust Enrichment* describes the explanation of *Moses* as

Explaning restitution as the embodiment of natural justice and equity gives the subject an undoubted versatility, an adaptability to new situations, and

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80 There is likely an argument here that, in some cases, only a court with the “judicial power of the United States” could hear or determine such equitable claims. That argument, separate from whether a jury should hear such claims, raises the issue of the effect of a disallowance on nonbankruptcy proceedings. If all a bankruptcy judge is doing is determining who shares in property of the estate, that would seem to be within the bankruptcy power allocated to Congress. If, however, there are affects outside of bankruptcy, such as issue or claim preclusion against third parties, there are significant questions raised. See generally Crowell v. Benson, 285 U.S. 22, 50-51 (1932) (upholding use of administrative agency fact-finder as adjunct to district court); United States v. Raddatz, 447 U.S. 667, 682-84 (1980) (upholding use of magistrates as adjunct to district court); see generally N. Pipeline Const. Co. v. Marathon Pipe Line Co., 458 U.S. 50, 77 (1982) (plurality) (referring to *Crowell* and *Raddatz* as “cases in which we approved the use of administrative agencies and magistrates as adjuncts to Art. III courts”). See also Wellness Intern. Network, Ltd. v. Sharif:

“If the judges should sit to hear ... controversies [beyond ...their cognizance], they would not sit as a court; at the most they would be arbitrators only, and their ... decision could not be binding as a judgment, but only as an award.”


(in the eyes of many observers) a special moral attractiveness. Restitution in this view is the aspect of our legal system that makes the most direct appeal to standards of equitable and conscientious behavior as a source of enforceable obligations.84

Although this justification is legitimately objectionable given its arbitrary nature,85 there are circumstances in which bankruptcy courts are asked to apply similar standards, and thus can be considered courts of equity in this second sense. These circumstances include direct instructions from Congress for bankruptcy judges to reach equitable results. The most obvious example of this type of grant appears in section 510(c)(1). That section states that “the court may—[¶] (1) under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim . . . .”86 This section allows a bankruptcy court to alter distributions based on the “principles of equitable subordination.” The legislative history to this section suggest that it essentially codified existing judge-made law,87 but also permitted courts, presumably courts sitting in bankruptcy, to continue to refine and shape these equitable principles.88 Indeed, the legislative history describes section 510(c) as “recogniz[ing] the inherent equitable power of the court under current law, and the practice followed with respect to contractual provisions.”89 Other provisions also grant equitable discretion to, more or less, “do the right thing” to bankruptcy judges. In particular, Congress included in the Code direction to bankruptcy judges to to make “equitable” divisions of estate and non debtor assets in such diverse cases as grain

84 RESTATEMENT (THIRD) OF RESTITUTION AND UNJUST ENRICHMENT § 1, com. b (2011).
85 Id. (“In numerous cases natural justice and equity do not in fact provide an adequate guide to decision, and would not do so even if their essential requirements could be treated as self-evident.”).
88 124 Cong. Rec. 32,398 (1978) (statement of Rep. Edwards); and id. at 33,998 (statement of Sen. De Concini). In lieu of a Conference Report, members of Congress read virtually identical statements into both the House and Senate records on the bill that became current title 11. 124 Cong. Rec. 32,391 (1978) (statement of Rep. Rousselot). As noted at the time, Congress believed that this procedure imbued such remarks with “the effect of being a conference report.” Id. The Supreme Court has agreed with this characterization. See Begier v. IRS, 496 U.S. 53, 64 n.5 (1990) (“Because of the absence of a conference and the key roles played by Representative Edwards and his counterpart floor manager Senator DeConcini, we have treated their floor statements on the Bankruptcy Reform Act of 1978 as persuasive evidence of congressional intent.”).
storage, customer property in stockbroker liquidations, excess partnership assets, and community property. Congress also conditioned the right to convert a case to chapter 12 on the conversion being “equitable.” Finally, the legislative history indicates that in fashioning adequate protection, an elemental concept in most bankruptcies, it was “expected that the courts will apply the concept [of adequate protection] in light of facts of each case and general equitable principles.” These are just a few of the instances of direct grant of equitable powers in this second, moral, sense.

Equity’s Exceptions to General Rules

Professor Bray’s first example of “equity” — “[t]he recognition of an exception to a general rule” — is probably the sense of equity that most people think of when thinking about courts of equity. “Equity” in this sense is often heedlessly used to describe or justify deviation from the consequence of the application of an accepted rule or standard when the application would be deemed unjust or unfair. In its best application, however, it is a reflection of the notion that not all consequences of general rules can be anticipated, and when confronted with an unanticipated consequence, individual justice should trump the need to extend a brittle general rule.

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92 11 U.S.C. § 723(d). The Senate Report stated that “Subsection (d) provides for the case where the total recovery from all of the bankrupt general partners is greater than the deficiency of which the trustee sought recovery. This case would most likely occur for a partnership with a large number of general partners. If the situation arises, the court is required to determine an equitable redistribution of the surplus to the estate of the general partners.” S. Rep. 989, 95th Cong., 2d Sess. 95 (1978).
93 11 U.S.C. § 726(c).
94 11 U.S.C. § 1112(d). Indeed, initially Congress drafted the list of “causes” for a motion to dismiss or convert to be non-exhaustive, and open to equitable additions. “This list is not exhaustive. The court will be able to consider other factors as they arise, and to use its equitable powers to reach an appropriate result in individual cases.” S. Rep. 989, 95th Cong., 2d Sess. 117 (1978). See also H.R. Rep. No. 595, 95th Cong., 1st Sess. 406 (1977).
96 Other examples might include 11 U.S.C. § 523(d), in which a court assess attorneys’ fees and costs against a creditor who unsuccessfully seeks to declare a debt nondischargeable unless “special circumstances would make the award unjust.” As originally enacted, the statute read “clearly inequitable” instead of unjust; the legislative history gives no reason for the change.

I do not include section 1129(b)(1)’s requirement that a cramdown plan be “fair and equitable” as to a dissenting class. The history of the statute indicates that Congress first required nonconsensual plans to be “fair” and only added “and equitable” several years later as part of an effort to construct a statute that would mirror judicial decisions of that time. See Bruce A. Markell, Fair Equivalents and Market Prices: Bankruptcy Cramdown Interest Rates, 33 Emory Bankr. Dev. J. 92 (2016).
This sense of “equity” is ancient. Aristotle observed that “the very nature of the equitable [is] a rectification of law where law falls short by reason of its universality.” In law, the “rectification” can manifest in many ways: clarifying an ambiguous statutory term; creating a new remedy for an acknowledged wrong; or even developing a new right where none previously existed. When a bankruptcy judge engages in any of these activities, the justification for the actions ultimately taken is often that the bankruptcy court is acting as a “court of equity.”

**Discretion and Equity**

One common thread in these activities is the exercise of discretion; that is, the taking of action or of a position when two or more choices are each reasonable, lawful and possible. This insight distills into the notion that discretion to act in this sense is the essence of equity.

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97 NICOMACHEAN ETHICS 114 (Martin Ostwald, trans., 1962). The quotation is from Book Five, Chapter 10, 1137b, at lines 26-27. A more recent translation renders the line as: “This is the nature of what is decent, a setting straight of a law, insofar as it leaves something out as a result of being universal.” NICOMACHEAN ETHICS 100 (Joe Sachs, trans., 2002). Yet another translation is “[T]he nature of the equitable is a correction of law where it is defective owing to its universality.” NICOMACHEAN ETHICS 99 (D. Ross, transl., 2009). This latter translation was recently used by Justice Breyer. Petrella v. Metro-Goldwyn-Mayer, Inc., 572 U.S. 663, 688 (2014) (Breyer, J., dissenting).

98 E.g., Hecht Co. v. Bowles, 321 U.S. 321, 329 (1944) (“The essence of equity jurisdiction has been the power of the Chancellor to do equity and to mould each decree to the necessities of the particular case”).

99 In the bankruptcy contest, one might look at first day motion practice in chapter 11, when many orders are entered not anticipated by the Code but deemed necessary to the success of the case, such as orders regarding payment of employees for prepetition periods or for roll-ups of repayment debt to be replaced by postpetition financing.

100 Similar to “equity,” there are many shades of meaning contained with “discretion,” including the quality of being discreet. The meaning stated in text is close to the definition 3b in Webster’s Unabridged Dictionary: “power of free decision or choice within certain legal bounds.”

101 Coke famously discussed judicial discretion as follows:

For discretion is a science or understanding to discern between falsity and truth, between wrong and right, between shadows and substance, between equity and colourable glosses and pretences, and not to do according to their wills and private affections; for as one saith, talis discretionem confundit.

Rooke’s Case, 5 Co. Rep. 99b, 77 Eng. Rep. 207 (C.P. 1598). Not all English judges saw discretion in such even terms. Lord Camden is reported to have said:

The Discretion of the Judge is the Law of Tyrants; it is always unknown; it is different in different Men; it is casual, and depends on the Constitution, Temper, and Passion. In the best, it is oftentimes Caprice, in the worst it is every Vice, Folly and Passion to which Human Nature is liable.

**LORD CAMDEN’S ARGUMENT IN DOE, ON THE DEMISE OF HINDSON & UX, ET. AL. V KERSEY, WHEREIN LORD MANSFIELD’S ARGUMENT IN WYNDHAM V. CHETWYND IS CONSIDERED AND ANSWERED 53 (1766).**

Chief Judge Marshall impliedly rejected Lord Camden’s view. In Osborn v. Bank of the United States, 22 U. S. 738, 866 (1824), he said:

Judicial power, as contradistinguishing from the power of the laws, has no existence. Courts are the mere instruments of the law, and can will nothing. When they are said
In bankruptcy the discretion to act is, well, complicated. As noted above, we can start with the proposition that bankruptcy judges have certain powers to act, some of which are delegated by district courts, some of which are inherent.

**Discretion Limited By the Source of Jurisdiction: The Boundaries Set By the Code**

But the power to act does not provide the rules to apply. In bankruptcy, those rules come from acts of Congress, such as title 11 and the jurisdictional provisions of title 28. As noted since Aristotle, however, positive law often is less than complete. If equity exists to fill the gaps necessary to achieve the goals of positive law, then bankruptcy judges should have equity powers to achieve the goals of title 11 and related statutes. Although simply stated, this is a tough proposition to maintain, given the catholic reach of bankruptcy over every aspect of a debtor’s financial life, and given the sometimes discordant provisions and goals of title 11.

But a bankruptcy judge’s equity power in these areas — the power to create exceptions to the general rules of title 11 — rises or falls on the breadth of the corpus of text and rules to be applied. A bankruptcy judge, indeed even a judge invested with the judicial power, does not have the power to enter orders contrary to express provisions of title 11. As stated by the Supreme Court, “[W]hatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code.”

In section 105(a), which is part of the Code, however, Congress permitted courts to enter orders in aid of their bankruptcy jurisdiction. This recursive incorporation of powers and jurisdiction beyond the Code’s operative sections gives rise to questions of how far a court can go to achieve an “equitable” result.

The mediation between these two propositions thus far has been the province of statutory interpretation. How far a court can go to reach a just or fair result in the absence of text prohibiting the desired result is an issue of the scope of the shadow cast by the text itself. The Court recently took this approach in *Law v. Siegell.*

In that case, Law, a debtor, had fabricated a fictitious deed of trust on his house to preclude Siegal, his chapter 7 trustee, from selling the house and distributing to Law’s creditors the excess of sales proceeds over Law’s homestead exemption. Siegal discovered the fabrication and avoided the fraudulent mortgage, but only after much litigation. The trustee, much aggrieved by the debtor fraudulent actions, sought to surcharge Law’s statutory homestead exemption. There was no basis in section 522, the section governing exemptions permitting such a surcharge.

The lower courts approved the surcharge. The Court reversed. It saw no room for equity-influenced exceptions to a detailed statutory scheme. As the Court stated: “The Code’s meticulous—not to say mind-numbingly detailed—enumeration of exemptions and exceptions to those exemptions confirms that courts are not authorized to create additional exceptions.”

In short, the Court was convinced that there were no gaps in coverage, no room to reach a just result since Congress presumably had thought about the total coverage already. On this point, the

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Court was clear. Siegal had “suggest[ed] that [some lower court] decisions reflect[ed] a general, equitable power in bankruptcy courts to deny exemptions based on a debtor’s bad-faith conduct. For the reasons we have given, the Bankruptcy Code admits no such power.”

Law relied much on Congress “meticulous” scheme to find no room for equity to create exceptions. But simple schemes also can preclude individual exceptions. In *Popular Auto, Inc v. Reyes-Colon (In re Reyes-Colon)*, the creditors had been long pursuing a slippery debtor. The problem was that only two creditors filed the involuntary, and those creditors could not obtain other parties to join. After many years of litigation, the bankruptcy court found that the debtor had more than 11 creditors, but the creditors sought an exception for “special circumstances.” Relying on Law, the First Circuit denied the request. As it stated:

> “[T]he Supreme Court held that bankruptcy courts “may not contravene specific statutory provisions” when they exercise their statutory and inherent powers. . . . The Court acknowledged that its holding “may produce inequitable results for trustees and creditors in other cases,” but recognized that Congress, in creating the Bankruptcy Code, “balanced the difficult choices that exemption limits impose on debtors with the economic harm that exemptions visit on creditors.” . . . [Law] forecloses employing equity to waive this plain statutory requirement.”

**The Range of Permissible Discretion and Equity**

Although the Code is a hard boundary on equitable discretion in bankruptcy, there is still space in which a court can legitimately find exceptions to general rules. Given the nature of equity, and the breadth of bankruptcy, a detailed and definitive outline may not yet be possible, but areas in which exceptions can legitimately be made can be sketched. In particular, equitable discretion can be exercise when necessary to correct errors caused by the court system itself, when courts and counsel work to achieve bankruptcy goals through methods and practices not explicitly provided in the Code, and even when new rights are necessary to achieve specific goals of the Code. I explore instances of each of these below.

**Obvious Uses of Equity to Create Exceptions: Correcting Court-Induced Errors**

The most obvious exception courts can make to general rules is when compliance with the rules is thwarted or precluded by mistakes or errors that the court itself makes. Under these circumstances, almost all courts permit exceptions to rules regarding claim filing deadlines if the late filing is due to a error of the court or the court clerk. As stated by the Ninth Circuit, “[t]he equitable power given to courts by 11 U.S.C. § 105(a) would be meaningless if courts were

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105 922 F.3d 13 (1st Cir. 2019).
106 Id. at 21-22. See also Sunbeam Prod., Inc. v. Chi. Am. Mfg., LLC, 686 F.3d 372, 375 (7th Cir. 2012) (“What the Bankruptcy Code provides, a judge cannot override by declaring that enforcement would be ‘inequitable.’”).
unable to correct their own mistakes."\(^{108}\) In short, “bankruptcy courts may call upon principles of equity to shield unwitting parties and correct their own errors.”\(^{109}\)

**Tolerable Uses of Equity to Create Exceptions: Fashioning Better Remedies for Existing Rights**

Beyond equitable powers to correct mistakes, the analysis becomes less uniform. But courts and counsel have use equity’s exceptions to fashion procedures and practices designed to implement the Code’s policies while not being explicitly stated. In particular, and with no real surprise, many of these exceptions deal with paying lawyers’ fees.

In one sense, the self-interest of lawyers is no surprise. In another, however, good lawyering permits the bankruptcy system to operate more efficiently, and thus it is in the interest of bankruptcy court to ensure that rigid rules do not preclude ethical and efficient lawyers from being paid for their services. Two practices are useful to examine: so called “nunc pro tunc” approvals of employment; and interim fee orders in large chapter 11 cases.

It is generally accepted that no lawyer may be paid from estate funds until his or her employment is approved by the court as consistent with section 327 of the Code. If followed literally, however, courts in cases of any size would be inundated with employment applications on the first day, and lawyers might not work on cases until those applications were approved. As a consequence, courts often retroactively approve employment applications at least to the date of filing, if not to an earlier date when work commenced.\(^{110}\) This exception to the general rule of “no approval/no pay” has much to commend it, and little to nothing to object to, especially if the application is on notice to parties in interest. It is an exception that thus make sense.\(^{111}\)

Another practice is similar, although not as uncontroversial. In large chapter 11 cases, firms representing the debtor and committees will often incur time and costs in excess of millions per

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\(^{109}\) Ward v. Yaquinto (In re Ward), 585 B.R. 806, 819 (N.D. Tex. 2018). See also Francis v. Riso (In re Riso), 57 B.R. 789, 793 (D.N.H. 1986) (“[A] bankruptcy court cannot create substantive rights in exercising its equity powers.... Allowing [the creditor] to go forward with his objection, however, will not create a substantive right ... but merely allow him to exercise that substantive right.”).

When the late filing is the fault of the participants and not the court, courts hold that section 105 cannot be used to extend time limits. Omni Mfg., Inc. v. Smith (In re Smith), 21 F.3d 660, 665 (5th Cir. 1994) (debtor applied for extension of bar date to add to mailing matrix creditor omitted from original filing; court held that section 105 cannot be used to justify such action, and that bankruptcy court should have simply declared debt to be nondischargeable due to omission of creditor).

\(^{110}\) See, e.g., In re Jarvis, 53 F.3d 416, 419-420 (1st Cir. 1995) (“In light of the purposefully nonmechanical nature of equity, we think it is appropriate that bankruptcy courts should be permitted to entertain post facto applications for professional services under section 327(a).”). See also

\(^{111}\) Often, this nunc pro tunc standard is modified if the application is made long after the work started. In In re Arkansas Co., Inc., 798 F.2d 645, 650 (3d Cir.1986), the court noted the following factors for approval of such a process: 1) whether the applicant or some other person bore responsibility for applying for approval; 2) whether the applicant was under time pressure to begin service without approval; 3) the amount of delay after the applicant learned that initial approval had not been granted; 4) the extent to which compensation to the applicant will prejudice innocent third parties; and 5) other relevant factors. See also Lazo v. Rose Hill Bank (In re Schupbach Investments, L.L.C.), 808 F.3d 1215, 1220 (10th Cir. 2015); In re Sedgwick, 560 B.R. 786, 795 (C.D. Cal. 2016).

Most courts that have addressed the issue have held that ignorance, negligence, and oversight do not constitute extraordinary circumstances. See 2 Collier on Bankruptcy ¶ 327.03[3] (Richard Levin & Henry J. Sommer eds., 16th ed. 2019).
Section 331 of the Code, however, would seem to set up a rule generally that fee applications should be limited to one every three months, although there is an exception if the court approves, and if the fees are approved by appropriate hearings. This, however, often works a hardship on firms engaged in these representations. As a result, many courts will enter so-called “Knudsen” orders, under which firms submit bills on a monthly basis which are paid at 80%-90% of their face amount without court approval, subject to quarterly interim fee applications under which the “retainage” is approved and paid. The case upon which such orders are based, U.S. Trustee v. Knudsen Corp. (In re Knudsen Corp.), placed the following limitations on this practice:

However, in the rare case where the court can make the following findings, a fee retainer procedure like the one here may be authorized:

1. The case is an unusually large one in which an exceptionally large amount of fees accrue each month;
2. The court is convinced that waiting an extended period for payment would place an undue hardship on counsel;
3. The court is satisfied that counsel can respond to any reassessment in one or more of the ways listed above; and
4. The fee retainer procedure is, itself, the subject of a noticed hearing prior to any payment thereunder.

Note that this procedure allows for payment to a professional without court approval. That feature has drawn criticism that the procedure is “illegal.” But similar to the nunc pro tunc...
orders, the various means of ensuring that their is no discrepancy between what the court ultimately approves and what was paid — generally enforced through holdbacks of 20% to 30% — achieves the Code’s goals of ensuring that all fees and expenses paid for by the estate are, as required by section 330, reasonable and necessary. It assumes that most professionals are honest, and that not every penny need be accounted for before payment; assumptions that are not unreasonable and, most importantly, do not impair achievement of the goal of ensuring that fees and expenses paid are reasonable.

These are, of course, equitable concerns. The “rule,” although not expressly stated, is that nothing gets paid until the court approves everything; that, however, is impractical. If enforced strictly, the system would be less efficient and less able to meet the goal of reorganization though chapter 11. It is an example of not creating new rights, but rather adapting implementation of a rule to meet practical needs after consideration the ultimate interests of all parties. It is designed to ensure that, at the end of the process, the result is the same as if the rule were strictly followed. In short, it is an example of how equity modifies remedies — the fee approval process — in ways unspecified in the Code while at the same time leaving rights — that no professional is paid more than what is reasonable — unimpaired.

**Debatable Uses of Equity to Create Exceptions: New Rights**

There is little support for creating new rights as a consequence of making equitable exceptions. As aptly and famously put by one court, section 105 and equity powers do not “authorize the bankruptcy courts to create substantive rights that are otherwise unavailable under applicable law, or constitute a roving commission to do equity.”

It is tautological that rights, once created, are durable; they apply to all instances for which they were created. And they may be fair or just. But rights tend to be universal — by definition, they cover all instances of a specified action or situation — and thus are subject to the same objection and need for exceptions that Aristotle saw long ago. A right created as an exception to a rule may itself require exceptions within that exception to yield fair and just results.

In bankruptcy, this inherent limitation operates within the larger limitation of the Code itself; as indicated above, equity is restrained in bankruptcy by the Code’s text and by the outcomes that text implements. A key example of this limitation has been the use of equitable subordination under section 510(c). As examined above, this is an area in which Congress has given courts the power to define the scope of subordination. This power, however, is not plenary. The Supreme

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116 United States v. Sutton, 786 F.2d 1305, 1308 (5th Cir. 1986); see also Willms v. Sanderson, 723 F.3d 1094, 1103 (9th Cir. 2013) (“More generally, § 105(a) is not a ‘roving commission to do equity.’” quoting Pac. Shores Dev., LLC v. At Home Corp. (In re At Home Corp.), 392 F.3d 1064, 1070 (9th Cir. 2004) and Saxman v. Educ. Credit Mgmt. Corp. (In re Saxman), 325 F.3d 1168, 1175 (9th Cir. 2003)); Jamo v. Katahdin Fed. Credit Union (In re Jamo), 283 F.3d 392, 403 (1st Cir. 2002) (“But section 105(a) does not provide bankruptcy courts with a roving writ, much less a free hand. The authority bestowed thereunder may be invoked only if, and to the extent that, the equitable remedy dispensed by the court is necessary to preserve an identifiable right conferred elsewhere in the Bankruptcy Code.”); 2 C OLLIER ON BANKRUPTCY ¶¶ 105.01[2], .05 (Richard Levin & Henry Sommers, eds., 16th ed. 2019). For a possibly contrary, though generally disfavored, view as to the expansiveness of the power under section 105(a), see Sears, Roebuck & Co. v. Spivey, 265 B.R. 357, 371 (E.D.N.Y. 2001) (“Section 105 of the Bankruptcy Code bestows on bankruptcy courts a specific equitable power to act in accordance with principles of justice and fairness. Bankruptcy courts have broad latitude in exercising this power.”).
Court said as much in *United States v. Noland*, a case that indicated a restricted scope for section 510(c). In *Noland*, the lower courts had subordinated payment of an administrative claim—a nonpecuniary tax loss penalty claim—which had arisen upon conversion of the case from a chapter 11 case to one under chapter 7. This was “equitable” in that the amount of the claim did not represent any loss to the governmental taxing authority, and was a penalty designed with nonbankruptcy situations in mind. Further, every dollar paid to the tax collector was a dollar taken away from holders of prepetition claims. As stated by the Sixth Circuit:

The essence of bankruptcy is equity. . . . We do not see the fairness or the justice in permitting the Commissioner’s claim for tax penalties, which are not being assessed because of pecuniary losses to the Internal Revenue Service, to enjoy an equal or higher priority with claims based on the extension of value to the debtor, whether secured or not. Further, assessing tax penalties against the estate of a debtor no longer in existence serves no punitive purpose. . . . To hold otherwise would be to allow creditors who have supported the business during its attempt to reorganize to be penalized once that effort has failed and there is not enough to go around. Furthermore, to hold otherwise could result in rewarding the debtor-in-possession, the party who failed to pay the taxes on time, to the detriment of the creditors.

The Supreme Court nonetheless reversed. As it stated the issue:

The answer turns on Congress’s probable intent to preserve the distinction between the relative levels of generality at which trial courts and legislatures respectively function in the normal course. . . . But if the provision also authorized a court to conclude on a general, categorical level that tax penalties should not be treated as administrative expenses to be paid first, it would empower a court to modify the operation of the priority statute at the same level at which Congress operated when it made its characteristically general judgment to establish the hierarchy of claims in the first place. That is, the distinction between characteristic legislative and trial court functions would simply be swept away, and the statute would delegate legislative revision, not authorize equitable exception. We find such a reading improbable in the extreme.

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117 *517 U.S. 535 (1996).*

118 The Sixth Circuit held that “[b]ecause of the nature of postpetition, nonpecuniary loss tax penalty claims in a Chapter 7 case, we believe such claims are susceptible to subordination.” *United States v. Noland (In re First Truck Lines, Inc.), 48 F.3d 210, 218 (6th Cir. 1995), rev’d sub nom. United States v. Noland, 517 U.S. 535 (1996).* Given the postpetition nature of the claim, it would thus be entitled to payment in full as an administrative claim before any payment would be made to creditors holding prepetition claims.


120 *United States v Noland, 517 U.S. 535, 540-41 (1996).*
In short, a court cannot alter a legislature’s judgment on the relative fairness of a statutory priority scheme.\textsuperscript{121} But can a court alter or adjust a right if that action does not alter the scheme? The issue has arisen in so-called “equitable disallowance” or “recharacterization” of claims. This issue arises when insiders denominate funds transferred to a debtor as “debt,” thereby allowing them to argue that the insiders should be able to share pro rata with other creditors upon insolvency. Other creditors, who had no say in the initial characterization, object, raising traditional notions of equity holders’ risks and rewards.

Some courts have found a federal source for the disallowance of such insider claims based on “equity.” Others have denied that any federal right could exist, reasoning that section 502 contains no such grounds for disallowance, and that any alteration of a nonbankruptcy right automatically alters the distribution scheme Congress drafted.

Based on the above, it would seem that no such manner of disallowance would be permitted. But that may be a brittle application. In \textit{Whither Recharacterization},\textsuperscript{122} Dean Lawrence Ponoroff dismantles this argument. First, it may very well be that equitable recharacterization is a recognized doctrine under nonbankruptcy law used by nonbankruptcy courts to reduce or eliminate claims to an insolvent’s res.\textsuperscript{123} That would nestle with Congress grant of equitable powers to courts in section 502(b)(2).\textsuperscript{124} It also may be that an argument could be made for “no fault” equitable subordination as an anticipated and permitted extension of the law when section 510(c) was enacted in 1978.\textsuperscript{125} This would also be consistent with congressional efforts to bestow particular types of equitable discretion in discrete cases.\textsuperscript{126} [see above]

The general conclusion is that no maxim is without exception, which again draws on Aristotle’s ancient observation of equity’s essence. The intricate and labyrinthian construction of the Code — with its outright grants of equitable power in section 502(b)(2), to its incorporation of the power to protect jurisdiction in section 105 — provides legitimate grounds for many practice and procedures not explicitly set down in the Code’s text. These legitimate avenues of authorization ought not to be overlooked.

\textsuperscript{121} \textit{Noland}, 517 U.S. at 542-43 (stating that § 510(c) permits a court to make exceptions to a general rule only when justified by particular facts). The Court reaffirmed this position in \textit{United States v. Reorganized CF & I Fabricators of Utah}, 518 U.S. 213 (1996). It held there that even when a claim in question is not entitled to a statutory priority (as was the administrative claim in \textit{Noland}), subordination cannot be wholly based on the nature of the claim itself. \textit{Id.} at 228 (describing \textit{Noland} as having nothing to do with the fact that the claim in that case was entitled to administrative priority, but rather with the reordering of priority on a categorical basis).


\textsuperscript{123} \textit{Id.} at 1265-1271.

\textsuperscript{124} \textit{See Section 0 supra.}

\textsuperscript{125} Ponoroff, \textit{supra} note 122, at 1282-1288.

\textsuperscript{126} \textit{See Section 0 supra.}
CONCLUSION

Is a bankruptcy court a court of equity? There is, in my opinion, no crisp, clear answer. The bankruptcy judges in any district form a court. As I have argued, it is a court with inherent powers in addition to the statutory powers granted by Congress. These inherent powers cover matters from the mundane to the profound, from setting the hours of operation to jailing parties in civil contempt.

The bankruptcy court is also a court that has various equitable powers: it decides claims against the estate using equitable principles; it is granted the power to decide various matters using equitable principles; and it often creates practices and procedures unanticipated by the text of the Code, but which efficiently implement the Code’s policies. At all times, however, a court’s exercise of equity powers in bankruptcy cases is limited by the text of the Code.

Many of these limitations, however, are not unique to bankruptcy courts. The Code itself exerts limits on district court judges, judges who are possessed of the full judicial power of the United States. And as bankruptcy courts’ jurisdiction and powers under the Code are wholly derivative on the bankruptcy power vested in the district courts, it follows that limitations on district courts are limitation on bankruptcy courts.

Is there something a district court could do in a bankruptcy case under its general equitable powers that a bankruptcy court cannot? The clear answer is yes, and the line of cases from Stern to the present focus on the necessity of possessing the judicial power to decide certain types of disputes. Beyond that very significant limitation (and any specific limitation on referral of cases from district courts), however, bankruptcy courts have equitable powers parallel to those held by district courts which enable bankruptcy courts to shape their dockets and the remedies they provide to any other court. In the end, bankruptcy courts are courts with equitable powers.

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127 This may be why, in the words of one judge, “the bankruptcy court is a court of equity” is the most frequently uttered substantive phrase by attorneys in her courtroom. Marcia Krieger, “The Bankruptcy Court is a Court of Equity”: What Does that Mean?, 50 S.C. L. Rev. 275, 297 (1999).