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WHERE HAVE ALL OF THE EQUITIES GONE?

A Three-Part Examination of the Role of Equity in Modern Bankruptcy Courts

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The quality of mercy is not strained,
It droppeth as the gentle rain from heaven
Upon the place beneath. It is twice blest
It blesseth him that gives and him that takes.[1]

[1] WILLIAM SHAKESPEARE, THE MERCHANT OF VENICE, act 4, sc. 1. In this speech, Portia, disguised as a lawyer in the Venetian Court of Justice, requests a merciful and equitable approach over strict application of the law in favor of the lender.

PART ONE

I. THE LOTTERY OF OUR DESTINY:[2] A QUICK HISTORY OF THE DEVELOPMENT OF BANKRUPTCY COURTS AS COURTS OF EQUITY

It is axiomatic that bankruptcy courts are "courts of equity." But it has long been recognized that federal courts possess no equity jurisdiction absent statutory authorization.[3] Indeed, all federal courts are courts of limited jurisdiction that may only decide disputes to the extent authorized by legislation or the Constitution.[4] Thus, bankruptcy courts are courts of equity only to the extent authorized by statute.[5] This section outlines the development of the statutory authority for bankruptcy courts to act equitably.

A. What is a "Court of Equity"?[6]

Historically, "courts of equity" stood in contrast to "courts of law." The modern concepts of equity come from the English Court of Chancery, which developed to alleviate some of the perceived rigidity of the English common law writ system.[7] Among the key differences between law and equity were that courts of equity: (1) could grant specific relief and other remedies not allowed common law courts; (2) used a more flexible procedure; (3) did not require juries; and (4) decided matters based on individualized considerations of justice and principles of equity.[8]

The equitable nature of present-day bankruptcy courts concerns the fourth characteristic of historical courts of equity.[9] The availability of specific relief and procedural flexibility are non-issues after the merger of law and equity and the simplification of civil procedure in federal courts. And the necessity of a jury is a constitutional matter. But to what extent may bankruptcy courts base their decisions on the facts and equities of a particular case as opposed to rigid statutory application?[10]

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[2] WILLIAM SHAKESPEARE, THE MERCHANT OF VENICE, act 2, sc. 1.

[3] *Ex parte* Christy, 44 U.S. 292, 311-12 (1845) ("In the first place, then, as to the jurisdiction of the District Court in matters of bankruptcy. Independent of the Bankrupt Act of 1841, ch. 9, the District Courts of the United States possess no equity jurisdiction whatsoever; for the previous legislation of Congress conferred no such authority upon them. Whatever jurisdiction, therefore, they now possess is wholly derived from that act."); *see also* Millepede Mktg. Ltd. v. Harsley, 928 F. Supp. 2d 109, 122 (D.D.C. 2013); Sinisgallo v. Town of Islip Hous. Auth., 865 F. Supp. 2d 307, 324 (E.D.N.Y. 2012).

[4] Kokkonen v. Guardian Life Ins. Co. of Am., 511 U.S. 375, 377 (1994).

[5] Although the Constitution allows Congress to enact bankruptcy laws, it does not create a system of bankruptcy or give federal courts jurisdiction over bankruptcy disputes.

[6] Interested readers should see generally, Marcia S. Krieger, "*The Bankruptcy Court Is a Court of Equity": What Does That Mean?*, 50 S.C. L. REV. 275 (1999) and Timothy S. Haskett, *The Medieval English Court of Chancery*, 14 Law & Hist. Rev. 245 (1996).

[7] *See* Krieger *supra* note 6, at 278; Haskett *supra* note 6, at 251-52.

[8] *See* Krieger *supra* note 6, at 279.

[9] *Cf.* Kevin C. Kennedy, *Equitable Remedies and Principled Discretion: The Michigan Experience*, 74 U. DET. MERCY L. REV. 609 (1997) ("In a broad jurisprudential sense, equity means the power to do justice in a particular case by exercising discretion to mitigate the rigidity of strict legal rules. In this broad sense, equity means the power to adapt the relief to the circumstances of the particular case, 'individualized justice,' in effect.").

[10] Some commentators have concluded that bankruptcy courts are not "courts of equity" because their equitable-like powers are derived from statute. *See, e.g.*, Krieger *supra* note 6, at 310-11. But courts routinely call these equitable-like powers of bankruptcy courts "equitable powers" and say that bankruptcy courts are "courts of equity." And for

B. General Statutory Authorization of Equitable Authority before 1984.[11]

1. *The Bankruptcy Act of 1841*

The first time[12] bankruptcy courts (which, prior to the Bankruptcy Code, were district court judges deciding bankruptcy matters) were afforded general equitable power was via the Bankruptcy Act of 1841.[13] The provision gave the bankruptcy courts "jurisdiction to be exercised summarily, in the nature of summary proceedings in equity" and "full authority and jurisdiction to compel obedience to all orders and decrees passed by them in bankruptcy, by process of contempt and other remedial process, to the same extent the circuit courts may . . . in any suit pending therein in equity."[14]

Although there is debate about what equitable powers the 1841 Act granted,[15] one of its drafters, Justice Story, described a general equitable authority in several cases while serving as the Circuit Justice for the Districts of Massachusetts and Maine.[16] His opinion in *Ex parte Foster* was most sweeping:

> And here I lay it down as a general principle, that the district court is possessed of the full jurisdiction of a court of equity, over the whole subject-matters which may arise in bankruptcy, and is authorized by summary proceedings to administer all the relief which a court of equity could administer under the like circumstances, upon a regular bill and regular proceedings, instituted by competent parties. In this respect, the act of congress, for wise purposes, has conferred a more wide and liberal jurisdiction upon the courts of the United States than the lord chancellor, sitting in bankruptcy, was authorized to exercise. In short, whatever he might properly do, sitting in bankruptcy, or sitting in the court of chancery, under his general equity jurisdiction, the courts of the United States are by the act of 1841 competent to do. So that the question resolves itself, so far as the exercise of jurisdiction for relief in this case is concerned, into this, whether it is a fit case for interposition and relief by a court of equity.[17]

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the most part, it does not matter practically that the authority of bankruptcy courts to focus on the facts and equities of a particular case derives from statute.

[11] For a more detailed discussion, see generally 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, 12-22 (2005).

[12] The only previous bankruptcy-authorizing statute was enacted in 1800 and then repealed in 1803. *Ex parte Christy*, 44 U.S. 292, 311 (1845). It did not confer any equitable powers. *Id.*

[13] Bankruptcy Act of 1841, ch. 9, 5 Stat. 440 (repealed 1843).

[14] *Id.* at § 6.

[15] *See* Ahart *supra* note 11, at 13-14.

[16] *Id.* at 14.

[17] *Ex Parte* Foster, 9 F. Cas. 508, 512 (C.C.D. Mass. 1842) (No. 4960).

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