APPENDIX A

PRECEDENTIAL

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

Nos. 20-1061; 20-1062 and 20-1063

In re: VENOCO LLC, d/b/a Venoco, Inc., et al.,

Debtors

EUGENE DAVIS, in his capacity as Liquidating Trustee of the Venoco Liquidating Trust

v.

STATE OF CALIFORNIA;
CALIFORNIA LANDS COMMISSION,

Appellants

Appeal from the United States District Court
for the District of Delaware
(D.C. Civil Action Nos. 1-19-mc-00007;
1-19-mc-00011 and 1-19-cv-00463)
District Judge: Honorable Colm F. Connolly

Argued September 23, 2020

Before: AMBRO, PORTER, and ROTH, Circuit Judges

(Opinion filed: May 24, 2021)

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OPINION OF THE COURT

AMBRO, Circuit Judge

States can generally assert sovereign immunity to shield themselves from lawsuits, but bankruptcy proceedings are one of the exceptions. The Supreme Court held in *Central Virginia Community College v. Katz*, 546 U.S. 356, 378 (2006), that, by ratifying the Bankruptcy Clause of the U.S. Constitution, states waived their sovereign immunity defense in proceedings that further a bankruptcy court's exercise of its jurisdiction over property of the debtor and its estate (called "*in rem* jurisdiction"). Here, we apply *Katz* to a bankruptcy adversary proceeding brought by a liquidating trustee for the debtors' assets seeking compensation from the State of California and its Lands Commission for the alleged taking of a refinery that belonged to the

debtors. Because that proceeding asks the Bankruptcy Court to enforce rights in the property of the debtors and their estates[1] and will facilitate the fair distribution of their assets to creditors, it furthers the Court's *in rem* functions. *Katz* thus forecloses the assertion of sovereign immunity by both California and its Lands Commission, and we affirm the District Court's order affirming the Bankruptcy Court's decision.

I. FACTS AND PROCEDURAL HISTORY

Venoco, LLC and its affiliated debtors (collectively, "Venoco" or the "Debtors")[2] operated the Platform Holly drilling rig in the South Ellwood Oil Field (the "Offshore Facility") off the coast of Santa Barbara, California. After extraction, the oil and gas were transported three miles north to the Ellwood Onshore Facility (the "Onshore Facility") for processing and refining. Venoco did not own the Offshore Facility and instead leased it from the State of California (the "State") acting through its Lands Commission (together with the State, the "California Parties"). Unlike the Offshore Facility, Venoco owns the Onshore Facility and holds the air permits to use it.

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[1] "Under the Bankruptcy Code . . . a petition 'creates an estate' that, with some exceptions, comprises 'all legal or equitable interests of the debtor in property as of the commencement of the case.' " *City of Chicago v. Fulton*, 141 S. Ct. 585, 589 (2021) (quoting 11 U. S.C. § 541(a)(1)).

[2] The parties do not distinguish the various debtor entities.

Following a pipeline rupture in 2015, Venoco could no longer get its oil and gas to the market. It was unable to reactivate the pipeline after it emerged from an initial bankruptcy filing in 2016, and it filed for Chapter 11 bankruptcy again on April 17, 2017 (the latter colloquially known as a "Chapter 22"). That same day, Venoco quitclaimed (*i.e.*, abandoned) its leases, thereby relinquishing all rights and interests in the Offshore Facility, including the wells and the Platform Holly drilling rig. Concerned about public safety and environmental risks, the Commission took over decommissioning the rig and plugging the abandoned wells. It initially agreed to pay Venoco approximately $1.1 million per month to continue operating the Offshore and Onshore Facilities. In September 2017, a third-party contractor took over operations from Venoco. In place of the previous agreement, the Commission and Venoco entered into a Gap Agreement, under which the Commission agreed to pay $100,000 per month, as well as additional compensation, for access to and use of the Onshore Facility. Meanwhile, the Commission also asserted its rights as Venoco's creditor. In October 2017, it filed an estimated $130 million contingent claim against Venoco for reimbursement of plugging and decommissioning costs, including $29 to $35 million for the cost to operate the Onshore Facility and the rig at the Offshore Facility.[3]

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[3] In October 2018, the Commission also filed in the Bankruptcy Court an "Assertion of Administrative Expense Claim and Reservation of Setoff Rights," which sought to preserve the Commission's right to "set off its allowable administrative claim

The Gap Agreement, as its name suggests, was not a permanent solution. For several months before the Bankruptcy Court confirmed the Debtors' plan of liquidation (the "Plan") in May 2018, Venoco and the Commission negotiated over a potential sale of the Onshore Facility to the Commission. When those negotiations failed, the Commission stopped paying what it owed under the Gap Agreement. Invoking its police powers to take necessary actions to protect the environment and public safety, the Commission argued it could continue using the Onshore Facility without payment.

Once the Plan became effective on October 1, 2018, the estates' assets, including the Onshore Facility, were transferred to a liquidation trust (the "Trust"). Eugene Davis, the court-appointed liquidation trustee (the "Trustee"), became responsible for collecting, holding, liquidating and distributing the Trust's assets for the benefit of Venoco's creditors.

After the Gap Agreement was terminated on October 15, 2018, the Trustee filed in the Bankruptcy Court an adversary proceeding against the California Parties (the "Adversary Proceeding"). It is primarily a claim for inverse condemnation, "a cause of action against a governmental defendant to recover the value of property which has been taken in fact by the governmental defendant." *Knick v. Twp. of Scott*, 139 S. Ct.

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against any claims that have been or may be asserted [against it] by the [Trustee]." JA 594-610. That document was withdrawn in September 2019.

2162, 2168 (2019) (citation omitted). It "stands in contrast to direct condemnation, in which the government initiates proceedings to acquire title under its eminent domain authority." *Id.* The Trustee argues that, under the U.S. and California Constitutions as well as § 105 of the Bankruptcy Code,[4] the Trust is entitled to just compensation for the taking of its property by the California Parties. While the Trustee's claims are primarily against the Commission, he also sued the State "out of an abundance of caution." Trustee's Br. at 40.

The California Parties filed motions to dismiss, claiming, among other things, they as sovereigns are immune from suits. The Bankruptcy Court denied the motions. The District Court granted leave for the California Parties to appeal only the Bankruptcy Court's ruling on their sovereign immunity defense and did not allow interlocutory appeal of other issues. It affirmed the Bankruptcy Court's rejection of the California Parties' assertion of Eleventh Amendment sovereign immunity and held that they forfeited their argument on state law immunity from liability (often called "substantive immunity") when they failed to raise the argument before the Bankruptcy Court. The California Parties appeal to us, arguing they can assert both Eleventh Amendment and substantive immunity defenses.

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[4] 11 U.S.C. § 105 is an "omnibus provision phrased in such general terms as to be the basis for a broad exercise of power in the administration of a bankruptcy case." 2 Collier on Bankruptcy ¶ 105.01 (16th ed. 2021).

II. JURISDICTION AND STANDARD OF REVIEW

The District Court had jurisdiction under 28 U.S.C. § 158(a)(3) over the appeal of the Bankruptcy Court's decision. For the appeal to our Court, the denial of a claim of sovereign immunity is "immediately appealable under the collateral order doctrine [which permits appeals of some non-final orders], imbuing us with jurisdiction under 28 U.S.C. § 1291." *See Maliandi v. Montclair State Univ.*, 845 F.3d 77, 82 (3d Cir. 2016); *see also P.R. Aqueduct & Sewer Auth. v. Metcalf & Eddy, Inc.*, 506 U.S. 139, 141 (1993). We exercise plenary review of the Bankruptcy and District Courts' legal determinations, *see In re Goody's Family Clothing Inc.*, 610 F.3d 812, 816 (3d Cir. 2010), which includes their denial of governmental immunity, *see Maliandi*, 845 F.3d at 82.

III. LEGAL BACKGROUND

This case reduces to one question: Under *Katz*, can the California Parties assert a defense of sovereign immunity in the Adversary Proceeding? Given disagreement on the scope of proceedings covered by *Katz*, we first summarize how the case law developed and then distill the analytical framework.

A. Case Law Before *Katz*

In our constitutional structure, states "maintain certain attributes of sovereignty, including sovereign immunity." *In re PennEast Pipeline Co.*, 938 F.3d 96,

103 (3d Cir. 2019), *cert. granted, PennEast Pipeline Co. v. New Jersey*, 141 S. Ct. 1289 (Mem.) (2021) (quoting *P.R. Aqueduct*, 506 U.S. at 146). This includes, but is not limited to, their immunity from suit in federal court recognized by the Eleventh Amendment, which reads in part that "[t]he Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State." U.S. Const. amend. XI.[5] This shelter from suit is a "fundamental aspect of the sovereignty which the [s]tates enjoyed before the ratification of the Constitution, and which they retain today." *PennEast*, 938 F.3d at 103 (quoting *Alden v. Maine*, 527 U.S. 706, 713 (1999)).

However, the sovereign immunity states enjoy is not absolute. They can expressly consent to suit in federal court by voluntarily invoking the jurisdiction of federal courts. *See Lombardo v. Pennsylvania, Dep't of Pub. Welfare*, 540 F.3d 190, 196 (3d Cir. 2008). Congress can abrogate states' immunity from suit by unequivocally expressing its intent to do so per valid constitutional authority. *See Seminole Tribe of Fla. v. Florida*, 517 U.S. 44, 55 (1996). Also, by ratifying the U.S. Constitution, states consented to certain waivers of their sovereign immunity in the "plan of the convention," including suits by the federal government against them

[5] In *Hans v. Louisiana*, 134 U.S. 1, 10 (1890), the Supreme Court decided that the Eleventh Amendment also covers suits by in-state plaintiffs. Thus the Eleventh Amendment "bar[s] all private suits against non-consenting [s]tates in federal court." *Lombardo v. Pennsylvania, Dep't of Pub. Welfare*, 540 F.3d 190, 194 (3d Cir. 2008).

in federal court. *PennEast*, 938 F.3d at 103-04 (quoting *Blatchford v. Native Vill. of Noatak*, 501 U.S. 775, 779 (1991)).

Before *Katz*, courts faced with the assertion of sovereign immunity in bankruptcy proceedings focused on the scope of congressional (that is, statutory) abrogation. *See Seminole Tribe*, 517 U.S. at 72 n.16 ("[I]t has not been widely thought that the federal antitrust, bankruptcy, or copyright statutes abrogated the [s]tates' sovereign immunity."); *Hoffman v. Conn. Dep't of Income Maint.*, 492 U.S. 96, 104 (1989) (holding that the Bankruptcy Code "did not abrogate the Eleventh Amendment immunity of the [s]tates"); *see also United States v. Nordic Vill., Inc.*, 503 U.S. 30, 39 (1992) (holding that the Bankruptcy Code did not clearly abrogate the federal government's immunity from suits for monetary relief). In these cases, the question was mainly one of statutory interpretation—whether Congress unequivocally expressed its intent to end immunity. *Seminole Tribe*, 517 U.S. at 55; *Hoffman*, 492 U.S. at 104 ("[W]e need not address whether [Congress] had the authority to [abrogate sovereign immunity] under its [constitutional] bankruptcy power.").

In 1994, Congress amended the Bankruptcy Code in an attempt to overrule the decisions in *Hoffman* and *Nordic Village. See In re Sacred Heart Hosp.*, 133 F.3d 237, 242 n.8 (3d Cir. 1998). Some circuits, including our own, concluded that although Congress now "unequivocally expressed its intent to abrogate the states' Eleventh Amendment immunity under the Bankruptcy Code," the Constitution's "Bankruptcy Clause [which

authorizes Congress to enact "uniform Laws on the subject of Bankruptcies throughout the United States"] is not a valid source of abrogation power." *Id.* at 243. These holdings, while never explicitly overturned, were soon displaced by subsequent Supreme Court case law.

In 2004, the Court set out to resolve a circuit split on the validity of the Bankruptcy Code's purported abrogation of sovereign immunity but ended up avoiding the issue altogether. In *Tennessee Student Assistance Corp. v. Hood*, 541 U.S. 440, 448 (2004), it rejected an assertion of sovereign immunity involving the discharge of student debt guaranteed by an arm of the State of Tennessee, concluding that when the "bankruptcy court's jurisdiction over the res is unquestioned, . . . the exercise of its *in rem* jurisdiction to discharge a debt does not infringe state sovereignty." *Id.* (internal citation omitted).[6] The Court did not address the Sixth Circuit's holding that the Bankruptcy Code validly abrogated state sovereign immunity. *See id.* at 445 ("Because we hold that a bankruptcy court's discharge of a student loan debt does not implicate a [s]tate's Eleventh Amendment immunity, we do not reach the broader question addressed by the Court of Appeals."). To make the limited reach of its opinion clear, the Court explained that its decision "is not to say[ ] a bankruptcy court's *in rem* jurisdiction overrides

[6] In the bankruptcy context, the debtor's estate is often referred to as the "res" to be administered by the bankruptcy court. *See, e.g.*, *In re Phila. Ent. & Dev. Partners, L.P.*, 549 B.R. 103, 145 (Bankr. E.D. Pa. 2016); *In re Metromedia Fiber Network, Inc.*, 299 B.R. 251, 273 (Bankr. S.D.N.Y. 2003) ("The debtor's estate is a res.").

sovereign immunity. . . . [n]or . . . that every exercise of a bankruptcy court's *in rem* jurisdiction will not offend the sovereignty of the State." *Id.* at 451 n.5 (internal quotation marks and citation omitted).

B. *Katz*

The Supreme Court expanded *Hood's* narrow holding two years later in *Katz*, which clarified federal power over states in bankruptcy cases. There the liquidating supervisor of a bookstore that filed for Chapter 11 bankruptcy sought to recover preferential transfers[7] made to Virginia educational institutions that were arms of the Commonwealth otherwise entitled to sovereign immunity. *Katz*, 546 U.S. at 360. The Court sided with the supervisor and rejected the assertion of sovereign immunity. We start with three non-controversial observations about *Katz*.

First, under the Constitution's Bankruptcy Clause, states are deemed to have waived their sovereign immunity in certain bankruptcy proceedings. *Id.* at 378 ("In ratifying the Bankruptcy Clause, the [s]tates acquiesced in a subordination of whatever sovereign immunity they might otherwise have asserted in proceedings necessary to effectuate the *in rem* jurisdiction of the bankruptcy courts."). Thus we look to the scope

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[7] Preferential transfers are defined in 11 U.S.C. § 547(b). They are basically payments made by the debtor to a creditor within a short time before the bankruptcy filing that improve (hence "prefer") the creditor's recovery from what it would otherwise receive in the bankruptcy.

of constitutional waiver recognized by *Katz* instead of congressional abrogation through the Bankruptcy Code (though, as a theoretical matter, Congress could still through legislation "exempt [states] from operation of [certain bankruptcy] laws," *id.* at 379).

Second, *Katz* did not foreclose the sovereign immunity defense in all bankruptcy proceedings. *See id.* at 378 n.15 ("We do not mean to suggest that every law labeled a 'bankruptcy' law could, consistent with the Bankruptcy Clause, properly impinge upon state sovereign immunity.").[8] Still, at least one later opinion suggests a broader reading of *Katz*. In *Allen v. Cooper*, 140 S. Ct. 994, 1002 (2020), the Supreme Court held

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[8] At least one court has relied on this language to suggest that *Katz* only applies to claims "created by the Bankruptcy Code." *Shieldalloy Metallurgical Corp. v. N.J. Dep't of Env't Prot.*, 743 F. Supp. 2d 429, 439 (D.N.J. 2010). We disagree because *Katz* repeatedly referenced bankruptcy "proceedings." *See Katz*, 546 U.S. at 362; *see also Allen v. Cooper*, 140 S. Ct. 994, 1002 (2020) ("[W]e held that Article I's Bankruptcy Clause enables Congress to subject nonconsenting [s]tates to *bankruptcy proceedings*." (emphasis added)); *see also* Ralph Brubaker, *Explaining Katz's New Bankruptcy Exception to State Sovereign Immunity: The Bankruptcy Power as a Federal Forum Power*, 15 Am. Bankr. Inst. L. Rev. 95, 129 (2007) (suggesting *Katz* gave Congress the power to "bind states to[ ] uniform federal judicial [bankruptcy] process" (emphasis omitted)). In any event, focusing on claims "created" by the Bankruptcy Code is an unworkable approach, considering the Code often incorporates applicable state laws. *See, e.g.*, 11 U.S.C. § 544(b)(1) (permitting the trustee to recover transfers that are voidable under state laws); *In re DBSI, Inc.*, 463 B.R. 709, 718 (Bankr. D. Del. 2012) (explaining that, when applying *Katz*, "[t]he fact that various state laws are implicated is no ground for constitutional concern").

that the Constitution's Intellectual Property Clause[9] did not authorize Congress to abrogate states' Eleventh Amendment immunity from copyright infringement suits. To distinguish that case from *Katz*, the Court emphasized that the Bankruptcy Clause was unique among Article I's grant of authority, explaining that "[i]n bankruptcy, we decided[ ] sovereign immunity has no place," as "the Bankruptcy Clause embraced the idea that federal courts could impose on state sovereignty." *Id.* However, we do not think that *dictum* in *Allen* means sovereign immunity can never be asserted before a bankruptcy court, for *Katz* was clear that it was deemed waived in some but not all bankruptcy proceedings.

Finally, while *Katz* discussed the bankruptcy court's *in rem* jurisdiction as the historical underpinning for waiving state sovereign immunity, it does not require a proceeding to be technically *in rem*. 546 U.S. at 370. Indeed, although the preference action in *Katz* was not squarely *in rem*, sovereign immunity still could not be asserted where any court order issued in the action would be "ancillary to and in furtherance of the court's *in rem* jurisdiction, [even if it] might itself involve *in personam* process." *Id.* at 372. The focus is on function and not form, the benefit being that courts do not need to struggle with the "blurred distinctions and perplexing case law [that confuse] *in*

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[9] Congress has the power "[t]o promote the Progress of Science and useful Arts, by securing for limited Times to Authors and Inventors the exclusive Right to their respective Writings and Discoveries." U.S. Const. art. I, § 8, cl. 8.

rem, ancillary to *in rem*, and even *in personam* proceedings in many respects." *In re DBSI, Inc.*, 463 B.R. 709, 714 (Bankr. D. Del. 2012).

We therefore summarize *Katz's* holding as follows: States cannot assert a defense of sovereign immunity in proceedings that further[10] a bankruptcy court's *in rem* jurisdiction no matter the technical classification of that proceeding.

C. Analytical Framework for Applying *Katz*

Katz did not define the range of proceedings that further a bankruptcy court's *in rem* jurisdiction, but it did tell us bankruptcy's three critical functions: "[1] the exercise of exclusive jurisdiction over all of the debtor's property, [2] the equitable distribution of that property among the debtor's creditors, and [3] the ultimate discharge that gives the debtor a 'fresh start' by releasing him, her, or it from further liability for old debts." *In re Diaz*, 647 F.3d 1073, 1084 (11th Cir. 2011) (quoting *Katz*, 546 U.S. at 363-64). We agree with the Eleventh Circuit and several bankruptcy courts that "[t]hese guidelines provide a useful starting point." *Id.*; *see, e.g.*, *In re Univ. of Wis. Oshkosh Found., Inc.*, 586 B.R. 458, 465 (Bankr. E.D. Wis. 2018); *In re Odom*, 571 B.R. 687,

[10] At various places the *Katz* opinion described proceedings where sovereign immunity is deemed waived as "merely ancillary to," "in furtherance of," or "necessary to effectuate" the bankruptcy court's *in rem* jurisdiction. 546 U.S. at 371-72, 378. We think these are similar concepts and use "further" as a shorthand to summarize *Katz*'s holding.

695 (Bankr. E.D. Pa. 2017). Indeed, at oral argument counsel for the Trustee and the Commission agreed that the proper framework analyzes whether a proceeding furthers any of these three functions. Oral Arg. Tr. 7:19-23, 24:4-9; *accord Diaz*, 647 F.3d at 1084.

Under this framework, courts must focus on function and not form when testing a proceeding's connection to the bankruptcy court's *in rem* jurisdiction. The first function asks whether the proceeding decides and affects interests in the res, the property of the debtor and its estate. Unsurprisingly, courts in our Circuit have already been asking this question when applying *Katz*. *See, e.g.*, *In re La Paloma Generating Co.*, 588 B.R. 695, 730 (Bankr. D. Del. 2018) (Sontchi, J.) ("[A] bankruptcy court's *in rem* jurisdiction would still need to focus[] on adjudications of interests in the underlying res."); *In re Phila. Ent. & Dev. Partners, L.P.*, 549 B.R. 103, 123 (Bankr. E.D. Pa. 2016), *aff'd*, 569 B.R. 394 (E.D. Pa. 2017), *rev'd on other grounds*, 879 F.3d 492 (3d Cir. 2018) (asking whether the claims "[i]mplicate an [i]dentifiable [r]es"). Relying on the first function, courts have found that states are deemed to waive sovereign immunity in most (i) turnover actions,[11] *see Philadelphia Entertainment*, 549 B.R. at 123 (holding "sovereign immunity [is] generally inapplicable to turnover actions"); *In re Kids World of America, Inc.*, 349 B.R. 152, 165-66 (Bankr. W.D. Ky. 2006) (same),

[11] Under 11 U.S.C. §§ 542 and 543, anyone in possession of the debtor's property may be required to return it—that is, turn it over—to the debtor or its trustee.

(ii) fraudulent transfer actions,[12] *see DBSI*, 463 B.R. at 713-15 (explaining the clear parallels between preferences and fraudulent transfers), and (iii) contract disputes, *see In re DPH Holdings Corp.*, 448 F. App'x 134, 138 (2d Cir. 2011) (unpublished) ("The contracts, which include potential liabilities and responsibilities . . . , are part of [the debtor's] estate.").[13]

The second function captures proceedings where the connection to a specific piece of property may be lacking, but there is broader effect on the equitable distribution of the debtor's property. A violation of the automatic stay, where one creditor seeks to enforce remedies against the debtor's property despite the injunctive bar of the bankruptcy filing, is one such example due to the disruptive effects on orderly administration of the estate. *See Diaz*, 647 F.3d at 1086 ("[W]e have no difficulty concluding that contempt motions alleging that a creditor has violated the automatic stay *generally* qualify as 'proceedings necessary

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[12] Fraudulent transfers are defined in 11 U.S.C. § 548 and involve transfers made (1) with the intent to defraud creditors or (2) while the debtor was insolvent and for which the debtor did not receive "reasonably equivalent value." *See* 11 U.S.C. § 548(a)(1)(B)(i). 11 U.S.C. § 544(b)(1) also incorporates state fraudulent transfer laws. The principal goal is to prevent the debtor from "stiffing" creditors by giving away its property before filing for bankruptcy.

[13] To be clear, a sovereign immunity defense is not categorically foreclosed in those proceedings. *See, e.g.*, *Phila. Ent.*, 549 B.R. at 124 (explaining that a fraudulent transfer action relating to revocation of a slot machine license does not further a bankruptcy court's *in rem* jurisdiction because the license is not the debtor's property).

to effectuate the *in rem* jurisdiction of the bankruptcy courts.'" (emphasis in original) (quoting *Katz*, 546 U.S. at 378)). Of course, there is also significant overlap between the first two functions. *Id.* at 1085-86 (explaining that the automatic stay implicates both functions).

The third function simply acknowledges the holding of *Hood* that "[s]tates, whether or not they choose to participate in the [bankruptcy] proceeding, are bound by a bankruptcy court's discharge order no less than other creditors." *See Hood*, 541 U.S. at 448; *see also People v. Irving Trust Co.*, 288 U.S. 329, 333 (1933) (holding that states must comply with deadlines to file claims like other creditors because, "otherwise, orderly and expeditious proceedings would be impossible and a fundamental purpose of [bankruptcy] would be frustrated").

Courts thus analyze correctly if they ask whether a proceeding directly relates to one or more of these three functions. *See Diaz*, 647 F.3d at 1084 ("At a minimum, then, a proceeding must directly relate to one or more of these functions."). We do not offer a one-size-fits-all test because claims and proceedings in bankruptcy are varied and fact-specific.

IV. APPLICATION

With the framework for analysis set, we apply it here and conclude the California Parties cannot assert sovereign immunity in the Adversary Proceeding.

A. The Adversary Proceeding Furthers Two of Bankruptcy's Critical Functions.

At the outset, the Adversary Proceeding furthers the Bankruptcy Court's exercise of jurisdiction over property of the Debtors and their estates, as it seeks a ruling on rights in the Onshore Facility. The California Parties repeatedly emphasize that the inverse condemnation claim is primarily one for money damages. But that alone is irrelevant, for even if the action "may resemble money damage lawsuits in *form*, it is their *function* that is critical." *Diaz*, 647 F.3d at 1085 (internal quotations and citation omitted) (emphases in original). And while the Adversary Proceeding may not be clearly *in rem* in form, its function is to decide rights in Venoco's property. *See United States v. Sid-Mars Rest. & Lounge, Inc.*, 644 F.3d 270, 286 (5th Cir. 2011) (Dennis, J., dissenting) ("Although I have not found cases explicitly declaring that inverse condemnation suits are *in rem* proceedings, . . . they are substantially equivalent to condemnation actions and essential to the self-executing constitutional protection of private property owners from governmental takings without just compensation."). At its core, the Adversary Proceeding is about whether the California Parties can use Venoco's property for free. *See* JA 129, Complaint ¶ 37 ("Plaintiff is entitled to just compensation, including the fair market and fair rental value of the [Onshore Facility]."); *R & J Holding Co. v. Redevelopment Auth.*, 670 F.3d 420, 433 n.10 (3d Cir. 2011) (explaining that seeking "compensation for . . . inability to fully

utilize, develop, and sell their property. . . . *are rights inhering in the property itself*" (emphasis added)).

The Adversary Proceeding also furthers the second critical function—facilitating equitable distribution of the estate's assets. The Onshore Facility is a significant asset for Venoco and its creditors. Indeed, the Plan's liquidation analysis acknowledged the Commission was "receiving significant value from the use of the Debtors' assets" and that the "value of the use of those assets [was] being negotiated between the parties." JA 589. Further, the Commission is a major creditor and filed a proof of claim against Venoco, so the California Parties have a stake in how the Trust's assets are liquidated and distributed. And consider the consequences: If the California Parties could assert sovereign immunity in the Adversary Proceeding, they would have a win-win—able to recover from the Trust on account of their claims against Venoco while preventing any judicial scrutiny over whether they can use the Onshore Facility without payment. And they would improve their status vis-à-vis other creditors solely owing to their status as a state that can invoke sovereign immunity, just the kind of result *Katz* wanted to avoid. *See DBSI*, 463 B.R. at 713 ("[The aim of equitable distribution of the res], and the desire for uniform application of the bankruptcy laws, would be jeopardized if the states were able to draw resources from the *res* or retain estate property when other creditors were unable to do so." (citing *Katz*, 546 U.S. at 362-64)).

The California Parties urge that sovereign immunity is fundamental to our constitutional design and the exercise of eminent domain power is especially central to their sovereignty. Though true as a general matter, bankruptcy is a different ball game, and the effect on state sovereignty is not the focus of our analysis. The focus is instead on ensuring that sovereign immunity will not interfere with the bankruptcy court's jurisdiction over the estate's property as well as its orderly administration. The driving principle of the *Katz* decision is that the Bankruptcy Clause has a "unique history" and is "*sui generis* . . . among Article I's grants of authority," the result being "that federal courts could impose on state sovereignty" in bankruptcy proceedings. *Allen*, 140 S. Ct. at 1002 (internal citations omitted).

We are also unpersuaded that we must consider that the Adversary Proceeding is a type of action both "anomalous and unheard of when the Constitution was adopted." *Fed. Maritime Comm'n v. S.C. State Ports Auth.*, 535 U.S. 743, 755 (2002) (internal quotation and citation omitted). This simply asks for a duplicative and unnecessary historical analysis. *Katz* explained that the "Framers would have understood that laws 'on the subject of Bankruptcies' included laws providing, in certain limited respects, for more than simple adjudications of rights in the res. . . . More generally, courts adjudicating disputes concerning bankrupts' estates historically have had the power to issue ancillary orders enforcing their *in rem* adjudications." 546 U.S. at 370. Thus we do not need to analyze whether the exact

proceeding existed at the Founding, for *Katz* already concluded that drawing the line at whether a proceeding furthers the bankruptcy court's *in rem* jurisdiction is consistent with the historical understanding of the scope of sovereign immunity waiver. *Id.*; *cf. Hood*, 541 U.S. at 452-53.

B. The Deemed Waiver of Sovereign Immunity in *Katz* Can Apply to Post-Confirmation or Post-Effective Date Claims.

The California Parties also argue that the Adversary Proceeding relates only to claims after the Plan was confirmed and became effective,[14] when the Debtors' estate ceased to exist, so there is no res for the bankruptcy court's jurisdiction to attach. The Trustee disputes this premise, explaining that, due to the

[14] The parties often use the terms "confirmation date" and "effective date" interchangeably, but there is a meaningful difference. Typically "the debtor's estate ceases to exist once confirmation [of a plan] has occurred." *In re Resorts Int'l, Inc.*, 372 F.3d 154, 165 (3d Cir. 2004) (citation omitted); *see also* 11 U.S.C. § 1141(b) ("Except as otherwise provided in the plan or the order confirming the plan, the confirmation of a plan vests all of the property of the estate in the debtor."). However, that is not the case here where the order confirming the Plan provided that Venoco's assets were vested in the Trust as of the Plan's effective date, not the confirmation date. *See* JA 459. While the effective date typically occurs shortly after confirmation, there was a nearly five-month delay here between confirmation in May 2018 and the Plan going effective in October 2018. Thus the relevant date for the California Parties' argument is the effective date, not the confirmation date, though this distinction does not affect the result we reach.

nature of the Gap Agreement, the Adversary Proceeding also seeks to recover amounts owed for the improper taking of the Onshore Facility before the effective date. We do not need to decide whether the Adversary Proceeding only pertains to post-effective date claims, as we reject the California Parties' argument even if it were true.

The California Parties essentially ask us to read *Katz* narrowly to carve out all claims that occurred after Venoco's estate was vested in the Trust. We decline to do so. In *In re Resorts International, Inc.*, 372 F.3d 154, 166 (3d Cir. 2004), we held that a bankruptcy court could have jurisdiction over a proceeding even when the "estate" no longer technically exists, so long as the proceeding has a "close nexus to the bankruptcy plan or proceeding." To refresh, the issue of bankruptcy statutory jurisdiction is not before us because the District Court did not grant leave to the California Parties to appeal it. Still, the reasoning of *Resorts International* is of aid. There, we followed our precedent in *Pacor, Inc. v. Higgins*, 743 F.2d 984, 994 (3d Cir. 1984), which held bankruptcy courts have statutory jurisdiction over a proceeding "related to" bankruptcy if the outcome could affect "the estate being administered in bankruptcy." In that context, we refused to apply the "'effect on the bankruptcy estate' test so literally as to entirely bar post-confirmation bankruptcy jurisdiction." *Resorts Int'l*, 372 F.3d at 165.

Here, the Bankruptcy Court's critical *in rem* functions did not end when the Plan became effective, as the Trust exists primarily to facilitate the "equitable

distribution of [the debtor's property] among the debtor's creditors." *Katz*, 546 U.S. at 364. Indeed, the Bankruptcy Court retained substantial control over the Trust assets, which were in essence a continuation of the estate.[15] As the Plan was one of liquidation, there was no reorganized debtor that continued to do business, the Debtors did not receive a discharge, *see* 11 U.S.C. § 1141(d)(3), and the Bankruptcy Court continued to oversee the Trust's administration and distribution of the estate's assets under the Plan, *see* 11 U.S.C. § 1142(b). *See also In re Boston Reg'l Med. Ctr., Inc.*, 410 F.3d 100, 107 (1st Cir. 2005) ("[A] liquidating

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[15] The Confirmation Order states that the Trustee "has been fully disclosed in the" Trust Agreement in compliance with Bankruptcy Code § 1129(a)(5), which requires debtors to "disclose[ ] the identity and affiliations of any individual proposed to serve, after confirmation of the plan, as . . . a successor to the debtor under the plan." JA 448; *see* 11 U.S.C. § 1129(a)(5). The Trust Agreement further appointed Davis "as a representative of the Contributing Debtors' Estates pursuant to sections 1123(a)(5), (a)(7), and (b)(3)(B)," JA 302, and authorized him to "[a]llow, settle, object to or reconcile any Claims against the Contributing Debtors' Estates." JA 305. The Confirmation Order provides that the Court retained jurisdiction over, *inter alia*, actions "[t]o recover all assets of the Debtors and property of the Debtors' Estates, which shall be for the benefit of the Liquidating Trust, wherever located." JA 473. Moreover, the Trust Agreement provides that the Bankruptcy Court has jurisdiction over the Trust and Trustee, JA 316; requires court approval before selling or abandoning trust assets, JA 305; and states that "[a]ll funds in the Liquidating Trust shall be deemed in *custodia legis* [in the custody of the law] until" they are paid out, "and no Beneficiary . . . can bind, pledge, encumber, execute upon, garnish, or attach the Liquidating Trust Assets or the Liquidating Trustee in any manner or compel payment from the Liquidating Trustee except by order of the Bankruptcy Court," JA 317.

debtor exists for the singular purpose of executing an order of the bankruptcy court.").

Our holding is limited, and we do not try to define the entire scope of the Bankruptcy Court's *in rem* jurisdiction, which the *Katz* Court described as "premised on the debtor and his estate." 546 U.S. at 370 (quoting *Hood*, 541 U.S. at 447). We only hold that, in this case, the Bankruptcy Court's *in rem* jurisdiction extends to the estate's property transferred to the Trust for the purpose of liquidation and distribution to Venoco's creditors, and over which the Bankruptcy Court retained substantial control under the Plan. And, contrary to the California Parties' parade of horribles, our conclusion does not mean sovereign immunity is waived in every bankruptcy proceeding brought by a post-confirmation trustee. A court must still undertake the proper analysis under *Katz*, and it must also have statutory jurisdiction over the proceeding under *Resorts International*.

C. The California Parties Cannot Assert Eleventh Amendment Immunity or State-Law Substantive Immunity from Liability.

As the Adversary Proceeding is the type of bankruptcy proceeding where states are deemed to waive their sovereign immunity, does that waiver extend to both defenses raised by the California Parties? To refresh, they assert Eleventh Amendment immunity and state-law substantive immunity from liability. In

Lombardo, 540 F.3d at 199, we explained the difference between these two defenses. The first bars all private suits against non-consenting states in the federal courts. *See* U.S. Const. amend. XI; *Seminole Tribe*, 517 U.S. at 72-73; *Hans v. Louisiana*, 134 U.S. 1, 10 (1890). Second, seeing that the Eleventh Amendment does not define the entire scope of sovereign immunity, states may also have substantive immunity from liability defined under their own law. *See Lombardo*, 540 F.3d at 195. As the District Court aptly summarized, "[t]he question raised by substantive immunity from liability is whether the state has agreed to subject itself to liability. The question raised by Eleventh Amendment immunity is whether the state has consented to be sued in a federal court." *In re Venoco, LLC*, 610 B.R. 239, 247 (D. Del. 2020). The parties here do not dispute that *Katz* reaches a state's assertion of Eleventh Amendment immunity, so the California Parties' defense of Eleventh Amendment immunity fails. As explained below, we also reject their assertion of state-law substantive immunity from liability.

At the outset, we agree with the District Court that the California Parties forfeited the argument they have immunity from liability when they failed to raise it in the Bankruptcy Court. *See In re Kaiser Grp. Int'l Inc.*, 399 F.3d 558, 565 (3d Cir. 2005) (noting the "general rule that when a party fails to raise an issue in the bankruptcy court, the issue . . . may not be considered by the district court on appeal"). The California Parties argue that the immunity-from-liability defense is jurisdictional and therefore can be raised at any time. We

reject this view, as "[a] defense rooted in state law cannot define the jurisdiction of the federal courts, which derives from the Constitution and acts of Congress." *Green v. Graham*, 906 F.3d 955, 964 (11th Cir. 2018). The California Parties' reliance on *Edelman v. Jordan*, 415 U.S. 651, 678 (1974), is also misplaced, for that case only discussed Eleventh Amendment immunity, which "sufficiently partakes of the nature of a jurisdictional bar so that it need not be raised in the trial court." *Id.* And the Supreme Court never even decided "that Eleventh Amendment immunity is a matter of subject-matter jurisdiction," *see Wis. Dep't of Corrs. v. Schacht*, 524 U.S. 381, 391 (1998), and certainly never suggested that the immunity-from-liability defense could be jurisdictional.

Had we reached the merits, the California Parties would still not have prevailed, for it is well settled they can be sued in California courts for the alleged violation of the Takings Clause under the U.S. or California Constitutions; so they are not actually immune from liability under California law. *See* U.S. Const. amend. V ("[P]rivate property [shall not] be taken for public use, without just compensation."); Cal. Const. art. 1, § 19 ("Private property may be taken or damaged for a public use and only when just compensation, ascertained by a jury unless waived, has first been paid to, or into court for, the owner."). The Supreme Court recognizes that the Takings Clause of the Fifth Amendment is "self-executing" without statutory recognition, so "states [must] provide a specific remedy for takings in their own courts." *See Seven Up Pete Venture v. Schweitzer*, 523 F.3d 948, 954 (9th Cir. 2008) (citing

First Eng. Evangelical Lutheran Church v. County of Los Angeles, 482 U.S. 304, 315 (1987)). Similarly, the California Constitution's takings provision is also self-executing without the need for more state legislation, meaning the State already indicated its consent to be sued when adequate payment to an owner did not follow a taking. *See Rose v. State*, 123 P.2d 505, 513 (Cal. 1942) ("[I]f no statute exists, liability still exists.").

Indeed, the California Parties as much as conceded they are not categorically immune from liability under California law and argue only that any suit against the State alleging an unconstitutional taking must be litigated in its own courts. Comm'n's Op. Br. at 53 n.21. But this is an argument about the forum for suit and not liability. To the extent they are invoking a third defense—a state law immunity-from-*suit* defense—we and other circuits have not recognized it. *See Lombardo*, 540 F.3d at 194; *see also Meyers ex rel. Benzing v. Texas*, 410 F.3d 236, 250-55 (5th Cir. 2005). Further, allowing the California Parties to assert a state law immunity-from-suit defense separate from Eleventh Amendment immunity would make the decision in *Katz* a dead letter. If that argument prevails, state legislation can easily end-run the deemed waiver of state sovereign immunity effected by the Bankruptcy Clause and recognized in *Katz*. Tellingly, *Katz* never limited its reach to only Eleventh Amendment immunity. 546 U.S. at 378 ("In ratifying the Bankruptcy Clause, the [s]tates acquiesced in a subordination of *whatever sovereign immunity they might overwise have asserted*." (emphasis added)); *id.* at 377 ("States agreed . . . not to assert *any*

sovereign immunity defense they might have had." (emphasis added)).[16]

Thus the California Parties' assertion of substantive immunity from liability under state law also fails. Because we reject the asserted sovereign immunity defenses, we do not reach whether the Commission also waived its sovereign immunity defenses by filing a proof of claim in the Bankruptcy Court and whether that waiver can be attributed to the State.

* * * * *

State sovereign immunity is a critical feature of the U.S. Constitution, but it is not absolute. When they ratified the Constitution, states waived their sovereign immunity defense in bankruptcy proceedings that further a bankruptcy court's exercise of its *in rem* jurisdiction. We have such a proceeding here, which seeks a ruling on rights in the Debtors' property and will affect the distribution of assets to the Debtors' creditors. We affirm the District Court's affirmance of the Bankruptcy Court's ruling and reject the California Parties' assertion of sovereign immunity in the Adversary Proceeding.

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[16] We do not go as far as holding that the substantive-immunity-from-liability defense is deemed waived in every proceeding where sovereign immunity is rejected under *Katz*. We hold off because the California Parties do not have immunity from liability here, and there may be potential daylight between the two defenses when applying *Katz* to a state-law cause of action. *See* Brubaker, *supra*, at 132 (describing potential complications with applying *Katz* to state-law causes of action).

APPENDIX B

IN THE UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF DELAWARE

IN RE VENOCO, LLC, *et al.*, Debtors.	: Chapter 11 : Bankr. No. 17-10828-JTD : (Jointly Administered)
STATE OF CALIFORNIA, Appellant, v. EUGENE DAVIS, in his capacity as Liquidating Trustee of the Venoco Liquidating Trust, Appellee.	: Civ. No. 19-mc-07-CFC
CALIFORNIA STATE LANDS COMMISSION, Appellant, v. EUGENE DAVIS, in his capacity as Liquidating Trustee of the Venoco Liquidating Trust, Appellee.	: Civ. No. 19-mc-11-CFC

MEMORANDUM OPINION

January 3, 2020
Wilmington, Delaware

/s/ Colm F. Connolly
CONNOLLY, UNITED
STATES DISTRICT JUDGE

The Liquidating Trustee of the Venoco Liquidating Trust filed this post-confirmation adversary proceeding in the Bankruptcy Court against the State of California and the California State Lands Commission (collectively, "the State Defendants"). The two-count Complaint alleges "inverse condemnation" claims under the Takings Clauses of the United States and California Constitutions (Count I) and § 105(a) of the Bankruptcy Code, 11 U.S.C. § 105(a) (Count II). Adv. D.I. 1 ¶¶ 35-41.[1] Inverse condemnation is "a cause of action against a governmental defendant to recover the value of property which has been taken in fact by the governmental defendant." *United States v. Clarke*, 445 U.S. 253, 257, 100 S. Ct. 1127, 63 L.Ed.2d 373 (1980) (quoting D. Hagman, Urban Planning and Land Development Control Law 328 (1971)). It "stands in

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[1] The docket of the Chapter 11 cases, captioned *In re Venoco, LLC*, No. 17-10828-JTD, is cited herein as "B.D.I. ___." The docket of the adversary proceeding, captioned *Davis v. State of California*, Adv. No. 18-50908-JTD, is cited herein as "Adv. D.I. ___." The Appendix to Trustee's Memorandum of Law Opposing Each Appellant's Appeal Regarding Sovereign Immunity (19-mc-07-CFC D.I. 35) is cited herein as "B ___."

contrast to direct condemnation, in which the government initiates proceedings to acquire title under its eminent domain authority." *Knick v. Township of Scott, Pennsylvania*, 139 S. Ct. 2162, 2168 (2019).

The State Defendants moved to dismiss the Complaint pursuant to Federal Rule of Civil Procedure 12(b)(6) and Federal Rule of Bankruptcy Procedure 7012(b). Adv. D.I. 8; Adv. D.I. 12. In support of their motions, they argued, among other things, that the claims were barred by the State Defendants' sovereign immunity. The Bankruptcy Court denied their motions to dismiss. *In re Venoco, LLC*, 596 B.R. 480 (Bankr. D. Del. 2019).

The sole issue in this appeal is whether the Bankruptcy Court erred in rejecting the State Defendants' sovereign immunity arguments. By separate Memorandum Order, I denied the State Defendants' requests for leave to appeal on an interlocutory basis the other rulings made by the Bankruptcy Court in denying the motions to dismiss. Civ. No. 19-463-CFC, D.I. 37.

I have jurisdiction over this appeal pursuant to 28 U.S.C. § 158(a)(3) and *Puerto Rico Aqueduct and Sewer Authority v. Metcalf & Eddy, Inc*, 506 U.S. 139, 143-44 (1993) (holding that Eleventh Amendment sovereign immunity is an immunity from suit, the denial of which is appealable as a collateral order). As I am assessing the merits of a Rule 12(b)(6) motion to dismiss, I accept as true all factual allegations in the Complaint and view those facts in the light most favorable to the Liquidating Trustee. *See Umland v. Planco Fin. Servs.*,

542 F.3d 59, 64 (3d Cir. 2008). I have considered in addition to the Complaint only "document[s] integral to or explicitly relied upon" in the Complaint, *Schmidt v. Skolas*, 770 F.3d 241, 249 (3d Cir. 2014) (internal quotation marks omitted); any "undisputedly authentic document" attached as an exhibit to the motions to dismiss if the Trustee's claims are based on the document, *Pension Ben. Guar. Corp. v. White Consol. Indus., Inc.*, 998 F.2d 1192, 1196 (3d Cir. 1993); and "any matters incorporated by reference or integral to the claim[s], items subject to judicial notice, [and] matters of public record," *Buck v. Hampton Twp. Sch. Dist.*, 452 F.3d 256, 260 (3d Cir. 2006). I have ignored the substantial portions of both sides' briefing in which facts not set forth in documents meeting these criteria are recited and argued. *See In re Burlington Coat Factory Sec. Litig.*, 114 F.3d 1410, 1426 (3d Cir. 1997) (A district court "may not consider matters extraneous to the pleadings" when ruling on a motion to dismiss.).

I. BACKGROUND

Venoco was the principal debtor in the Chapter 11 case from which this adversary proceeding arose. The other debtors were affiliates of Venoco. As the parties do not distinguish Venoco from the other debtors either individually or collectively, I will refer to the debtors collectively as Venoco.

Venoco was an oil and gas company that operated the Platform Holly drilling rig in the South Ellwood Oil Field off the coast of Santa Barbara, California. It held

rights, title, and interests to wells in the South Ellwood Field by virtue of certain leases (the SEF leases) it obtained from Mobil Oil Company in 1997. The SEF leases were issued by the State of California, acting by and through the Lands Commission.

Venoco processed the oil and gas it obtained from Platform Holly at the Ellwood Onshore Facility (the EOF), which sits on a half-acre lot on the California coast about three miles north of the platform. Venoco held title to the EOF and the air permits necessary to use the EOF.

Venoco's economic demise can be traced to 2015, when a ruptured pipeline cut off the only conduit for the Platform Holly's oil to get to market. Adv. D.I. 1 ¶ 26. The pipeline rupture and subsequent refusal of the Land Commission to allow Venoco to pursue alternative means to extract and process oil from the South Ellwood Field led to Venoco's filing for bankruptcy on April 17, 2017. *Id.* That same day, Venoco quitclaimed its SEF leases, thereby relinquishing its rights, title, and interests in the South Ellwood Field, including its ownership of the Platform Holly. *Id.* ¶ 2. As a result of that relinquishment, the Land Commission became responsible for decommissioning the Platform Holly and plugging the abandoned wells in the South Ellwood Field. *Id.*

The decommissioning of an oil platform and the plugging of offshore wells are expensive undertakings fraught with safety and environmental hazards. To facilitate an orderly and safe transition of the South

Ellwood decommissioning and plugging operations to a third-party contractor designated by the Land Commission, Venoco and the Land Commission entered into an Agreement for Reimbursement of Temporary Services on the eve of Venoco's bankruptcy. Adv. D.I. 1-1. The reimbursement agreement provided in relevant part that the EOF was "necessary for the continued operation and anticipated plugging and abandonment" of the SEF leases and that the Land Commission would pay Venoco approximately $1.1 million a month to operate the Platform Holly, South Ellwood wells, and EOF in a safe and responsible manner until the new contractor designated by the Land Commission was ready to assume operational control.

On September 15, 2017, the third-party contractor took over the decommissioning and plugging operations, and the reimbursement agreement was terminated. Adv. D.I. 1 ¶ 28. At that point, Venoco and the Land Commission entered into a "Gap Agreement" pursuant to which the Land Commission agreed to pay Venoco $100,000 per month for the non-exclusive access and use of the EOF. *Id.* ¶ 29.

Under the terms of the SEF leases and California law, the Land Commission has the right to obtain reimbursement for its decommissioning and plugging efforts from Venoco and from Venoco's predecessor lessees, including Mobil Oil (and Mobil's successor-in-interest, Exxon Mobil). Accordingly, on October 13, 2017, the Land Commission filed a proof of claim with the Bankruptcy Court for an estimated $130 million contingent claim against Venoco for the recovery of

amounts the Land Commission will have incurred in plugging the South Ellwood wells and decommissioning the Platform Holly and other facilities used to extract and process oil and gas from the wells during the plugging process. B001682. The contingent claim included $29 million to $35 million for the cost to operate and maintain the EOF in connection with the plugging and decommissioning efforts. B001751.

On May 23, 2018, the Bankruptcy Court entered an order confirming Debtor's Plan of Liquidation, effective as of October 1, 2018. As part of the Plan and the Litigation Trust Agreement it incorporates, the Court created a Liquidating Trust and transferred to that Trust assets (the Liquidating Trust Assets) from the bankruptcy estate. Those assets include the EOF and any claims Venoco had against the State Defendants. The Bankruptcy Court appointed Plaintiff to serve as the Liquidating Trustee and ordered him to "collect[], hold[], distribut[e] and liquidat[e] the Liquidating Trust Assets for the benefit" of Venoco's creditors that filed claims against the bankruptcy estate and "to otherwise administer[] the wind-down" of the estate. B.D.I. 879-1, Liquidating Trust Agreement at 2; B.D.I. 893, Notice of Appointment of Liquidating Trustee; B.D.I. 922-1, Combined Disclosure Statement and Plan, Art. XI.C. (governing "Rights, Powers and Duties of the Debtors and Liquidating Trustee"); *id.*, Art. XIII.D (governing "Payments and Distributions for Disputed Claims"); B.D.I. 922, Confirmation Order ¶¶ 10-11).

In the months leading up to confirmation, Venoco "sought to negotiate with the [Land Commission] for a purchase price and ultimate disposition of the EOF, its equipment, and [environmental] permits." Adv. D.I. 1 ¶ 30. The Land Commission, however, refused to purchase these assets and also refused to pay Venoco the amounts it owed Venoco under the Gap Agreement. *Id.* On August 22, 2018, Venoco notified the Land Commission that it intended to terminate the Gap Agreement on October 15, 2018 if certain conditions, including the payment of $950,000 in past due payments under the Gap Agreement and "substantial progress towards settlement" of the parties' outstanding claims against each other were not met. *Id.* ¶ 31.

On October 1, 2018, the Plan became effective and the EOF, its permits, and Venoco's potential claims against the State Defendants were transferred to the Liquidating Trust. On October 15, 2018, the Gap Agreement was terminated.

The State Defendants have informed the Liquidating Trustee that they will not compensate the Liquidating Trust for their use of the EOF but will "remain on the EOF under the veil of police powers authorizing them to take actions necessary to protect the environment." *Id.* ¶ 1. The State Defendants intend to use the EOF over the next five years to process and sell for tens of millions of dollars the oil and gas obtained during their decommissioning and plugging efforts. *Id.* ¶¶ 33, 34.

On October 16, 2018, the Liquidating Trustee filed the Complaint and thereby initiated this adversary proceeding. The Liquidating Trustee alleges in the Complaint that the State Defendants' continued use of the EOF constitutes a taking under the United States and California Constitutions and that the Liquidating Trust is therefore entitled to "just compensation, including the fair market and fair rental value of the EOF, its equipment, its permits and [the State] Defendants' special use and operations thereon." *Id.* ¶ 37. By its Complaint, the Liquidating Trustee seeks "to maximize [the] distributable value" of the Liquidating Trust "in accordance with" the Plan. *Id.* ¶ 41.

The State Defendants filed motions to dismiss to the Complaint. The Bankruptcy Court denied the motions. The Court based its decision in relevant part on its conclusion that "the *in rem* jurisdiction of the bankruptcy court defeats a claim of sovereign immunity." *Venoco*, 596 B.R. at 487.

II. DISCUSSION

The State Defendants make two arguments on appeal. First, they argue that they are immune from suit in federal court under the Eleventh Amendment of the United States Constitution. 19-mc-07-CFC, D.I. 32 at 13. The Amendment literally reads: "The Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign

State"; but the Supreme Court has extended the Amendment's reach to cover suits by in-state plaintiffs, *Hans v. Louisiana*, 134 U.S. 1, 14-15, 20 (1890), and thus the Amendment bars all private suits against non-consenting States in the federal courts.

Second, the State Defendants contend that they enjoy "substantive immunity" under the California Tort Claims Act that extends "beyond" their Eleventh Amendment immunity.

A. Standard of Review

A district court "review[s] [a] bankruptcy court's legal determinations de novo, its factual findings for clear error and its exercise of discretion for abuse thereof." *In re Trans World Airlines, Inc.*, 145 F.3d 124, 130-31 (3d Cir. 1998) (citation omitted). The district court "review[s] de novo whether an entity is entitled to sovereign immunity." *Patterson v. Pa. Liquor Control Bd.*, 915 F.3d 945, 950 (3d Cir. 2019) (citation omitted).

B. Eleventh Amendment Immunity

The State Defendants' argument that they are entitled to Eleventh Amendment immunity is foreclosed by the Supreme Court's decision in *Central Virginia Community College v. Katz*, 546 U.S. 356 (2006). The Court held in *Katz* that "[i]n ratifying the Bankruptcy Clause [of the Constitution], the States acquiesced in a subordination of whatever sovereign immunity they might otherwise have asserted in proceedings

necessary to effectuate the *in rem* jurisdiction of the bankruptcy courts." *Id.* at 378. *See also id.* at 373 ("Insofar as orders ancillary to the bankruptcy courts' *in rem* jurisdiction, like orders directing turnover of preferential transfers, implicate States' sovereign immunity from suit, the States agreed in the plan of the [Constitutional] Convention not to assert that immunity."); *id.* at 377 ("[The] States agreed in [ratifying] the plan of the [Constitutional] Convention not to assert any sovereign immunity defense they might have had in proceedings brought pursuant to Laws on the subject of Bankruptcies." (internal quotation marks and citation omitted)). As the four dissenters noted in *Katz*, the Court's majority "f[oun]d[ ] a surrender of the States' immunity from suit in Article I of the Constitution, which authorizes Congress '[t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States[,]'" *id.* at 381 (quoting U.S. Const. Art. I § 8, cl. 4), and thus the majority's opinion "ma[d]e[ ] clear that *no action* of Congress is needed [to abrogate the States' sovereign immunity in bankruptcy proceedings] because the Bankruptcy Clause itself manifests the consent of the States to be sued[,]" *id.* at 383 (emphasis in original).

In this case, the Litigation Trustee's inverse condemnation claims effectuate the Bankruptcy Court's *in rem* jurisdiction. The Trustee brought the claims to fulfill his obligations under the Court-ordered Plan to collect and liquidate the Trust's assets for the benefit of Venoco's creditors and to administer the wind-down of the bankruptcy estate. B.D.I. 879-1 at 2. Thus, the

claims affect directly the administration and distribution of the res—the core of the Bankruptcy Court's *in rem* jurisdiction.

The State Defendants argue that "[a]lthough a State's sovereign immunity may be abrogated by Congress in narrow circumstances, . . . the Third Circuit has held that the purported abrogation of state sovereign immunity contained in 11 U.S.C. § 106(a) was beyond Congress's power under the Bankruptcy Clause." 19-mc-07-CFC D.I. 32 at 14 (citing *Sacred Hart Hosp. v. Dep't of Pub. Welfare*, 133 F.3d 237, 245 (3d Cir. 1998)). But this argument misses the point. It is true that the Third Circuit held in *Sacred Heart—eight* years before *Katz*—that Congress's attempt to abrogate States' sovereign immunity pursuant to § 106(a) was unconstitutional. *Id*.[2] But *Katz* made the question of Congressional abrogation irrelevant. The Court was explicit in *Katz* that the States waived their sovereign immunity by ratifying the Bankruptcy Clause in the Constitution. Thus, as the dissent in *Katz* noted, "*no action* of Congress is needed" to abrogate the States' sovereign immunity in bankruptcy proceedings. *Katz*, 546 U.S. at 383 (emphasis in original).

The State Defendants next argue that inverse condemnation claims are "for dollars, not particular dollars," and thus such claims are not *in rem* and not subject to *Katz*. 19-mc-07-CFC D.I. 32 at 17-18. But

[2] Section 106(a) provides that "[n]otwithstanding an assertion of sovereign immunity, sovereign immunity is abrogated as to a governmental unit to the extent set forth in this section with respect to" certain sections of the Bankruptcy Code.

whether the inverse condemnation claims themselves are *in rem* is of no moment. The relevant question is whether the claims are asserted in proceedings that are ancillary to or give effect to the bankruptcy court's *in rem* jurisdiction. *See Katz*, 546 U.S. at 373 ("Insofar as orders ancillary to the bankruptcy courts' *in rem* jurisdiction . . . implicate States' sovereign immunity from suit, the States agreed in the plan of the [Constitutional] Convention not to assert that immunity."). As the Court explained in *Katz*:

> The ineluctable conclusion[] . . . is that [the] States agreed in the [ratification of the] plan of the [Constitutional] Convention not to assert any sovereign immunity defense they might have had in proceedings brought pursuant to "Laws on the subject of Bankruptcies." The scope of this consent was limited; the jurisdiction exercised in bankruptcy proceedings was chiefly *in rem*—a narrow jurisdiction that does not implicate state sovereignty to nearly the same degree as other kinds of jurisdiction. But while the principal focus of the bankruptcy proceedings is and was always the res, some exercises of bankruptcy courts' powers—issuance of writs of habeas corpus included—unquestionably involved more than mere adjudication of rights in a res. In ratifying the Bankruptcy Clause, the States acquiesced in a subordination of whatever sovereign immunity they might otherwise have asserted in proceedings necessary to effectuate the *in rem* jurisdiction of the bankruptcy courts.

546 U.S. at 377-78 (citations omitted).

Lastly, quoting *In re Resorts International, Inc.*, 372 F.3d 154,165 (3d Cir. 2004), the State Defendants argue that there is no res connected to this post-confirmation adversary proceeding because "[t]he debtor's estate ceases to exist once confirmation has occurred." 19-mc-07-CFC D.I. 32 at 17 (quoting *Resorts Int'l*, 372 F.3d at 165). But this quotation from *Resorts International* is misleadingly truncated and taken out of context. The Third Circuit expressly held in *Resorts International* that "post-confirmation bankruptcy jurisdiction is normally appropriate" when the asserted claims have "a close nexus to the bankruptcy plan or proceeding, as when a matter affects the interpretation, implementation, consummation, execution, or administration of a confirmed plan or incorporated litigation trust agreement." 372 F.3d at 168-69; *see also id.* at 165 (noting that "[*a*]*t its most literal level*, it is impossible for the bankrupt debtor's estate to be affected by a post-confirmation dispute because the debtor's estate ceases to exist once confirmation has occurred[,] but that "courts *do not usually apply* [that] test *so literally* as to entirely bar post-confirmation bankruptcy jurisdiction") (emphasis added).

In this case, the claims have the requisite close nexus to the bankruptcy plan. Under the express terms of the court-ordered Plan and the Liquidating Trust Agreement it incorporated, the Liquidating Trustee is obligated to collect, hold, and distribute the estate's assets—including the EOF and its permits and Venoco's claims against the State Defendants—for the benefit of the estate's creditors. The Complaint thus implements,

executes, and, if successful, will consummate the Plan. Thus, the claims asserted in the adversary proceeding are directly connected to the res that lies at the heart of the Bankruptcy Court's jurisdiction. Accordingly, under *Katz*, the Complaint is not barred by Eleventh Amendment immunity.[3]

C. Immunity under The California Tort Claims Act

The State Defendant next argue that the California Tort Claims Act affords them "substantive immunity from liability" that "exists independent of constitutional protections relating to federal jurisdiction." 19-mc-07-CFC D.I. 32 at 27. The State Defendants are correct that substantive immunity from liability is distinct from the jurisdictional immunity conferred by the Eleventh Amendment. *See Lombardo v. Pennsylvania, Dept. of Public Welfare*, 540 F.3d 190, 194 (3d Cir. 2008) ("We can discern two distinct types of state sovereign immunity: immunity from suit in federal court and immunity from liability"); *id.* at 194-95 ("[I]mmunity from suit in the federal courts[] [is] also known as Eleventh Amendment immunity."). But the State Defendants did not argue before the

[3] Because I agree with the Bankruptcy Court's determination that Eleventh Amendment sovereign immunity does not bar the Liquidating Trustee's claims, I need not address, and express no opinion with respect to, the parties' arguments regarding whether the State Defendants waived Eleventh Amendment immunity by filing their $130 million claim and participating in the bankruptcy proceedings. 19-mc-07-CFC D.I. 32 at 19-26; *id.*, D.I. 34 at 25-44.

Bankruptcy Court that the Complaint should be dismissed based on sovereign immunity derived from the California Tort Claims Act (or any other source of state law). Accordingly, they have waived the issue and I may not consider it on appeal. *In re Kaiser Grp. Int'l Inc.*, 399 F.3d 558, 565 (3d Cir. 2005) ("[W]hen a party fails to raise an issue in the bankruptcy court, the issue is waived and may not be considered by the district court on appeal.").

I do not agree with the State Defendants' argument that the issue of substantive immunity is "jurisdictional and may be raised at any time, including on appeal." 19-mc-07-CFC D.I. 32 at 27. Although "the Eleventh Amendment defense sufficiently partakes of the nature of a jurisdictional bar so that it need not be raised in the trial court[,]" *Edelman v. Jordan*, 415 U.S. 651, 677-78 (1974), the question of a state's substantive immunity from liability does not similarly implicate the jurisdiction of federal courts. The question raised by substantive immunity from liability is whether the state has agreed to subject itself to liability. The question raised by Eleventh Amendment immunity is whether the state has consented to be sued in a federal court. The latter, to use the State Defendants' words, affords "constitutional protection[] relating to federal jurisdiction," 19-mc-07-CFC D.I. 32 at 27. That jurisdictional bar is "separate and distinct" from sovereign immunity from liability. *Lombardo* 540 F.2d at 199. Accordingly, having failed to raise the issue of substantive immunity from liability with the Bankruptcy

Court, the State Defendants have waived their right to argue the issue on appeal.[4]

III. CONCLUSION

For the reasons discussed above, I will affirm the Bankruptcy Court's denial of the State Defendants' motion to dismiss.

The Court will issue an Order consistent with this Memorandum Opinion.

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[4] I note nonetheless for the benefit of the parties on remand that the Court held in *Katz* that "[i]n ratifying the Bankruptcy Clause [of the Constitution], the States acquiesced in a subordination of *whatever sovereign immunity they might otherwise have asserted* in proceedings necessary to effectuate the *in rem* jurisdiction of the bankruptcy courts." 546 U.S. at 378 (emphasis added). Thus, the Court did not limit its holding to Eleventh Amendment immunity.

APPENDIX C

IN THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF DELAWARE

In re	)	Chapter 11
VENOCO, LLC, *et al.*,	)	Case No. 17-10828 (KG) (Jointly Administered)
Debtors.	)	
EUGENE DAVIS, in his capacity as Liquidating Trustee of the Venoco Liquidating Trust,	)	
Plaintiffs,	)	
v.	)	Adv. Pro. No. 18-50908 (KG)
STATE OF CALIFORNIA, and CALIFORNIA STATE LANDS COMMISION,	)	
Defendants.	)	**Re: D.I. 8 and 12**

OPINION

(Filed Jan. 2, 2019)

The issue before the Court is jurisdiction. Does the Court which presided over Debtors'[1] Chapter 11 bankruptcy case and entered the Order which confirmed the plan of liquidation have jurisdiction to decide a post-confirmation dispute in an adversary proceeding? Jurisdiction is the seminal question in every case and sometimes the final question. Here, the Court is

[1] Debtors are: Venoco, LLC, TexCal Energy (LP) LLC, Whittier Pipeline Corporation, TexCal Energy (GP) LLC, Ellwood Pipeline, Inc. and TexCal Energy South Texas, L.P.

satisfied that it has jurisdiction, and it will not abstain from hearing the adversary proceeding for reasons which follow.

FACTS[2]

The Debtors filed their bankruptcy petitions on April 17, 2017 (the "Petition Date"). The Court entered its Order confirming Debtors' Plan of Liquidation (the "Plan") on May 23, 2018, and the Plan became effective on October 1, 2018. Complaint, ¶¶ 21-23. On October 16, 2018, the day after the Plan became effective, the Liquidating Trustee (the "Trustee") on behalf of the Liquidating Trust (the "Trust"), filed Plaintiff's Original Complaint for Inverse Condemnation (the "Complaint") as an adversary proceeding. The Trustee named as defendants the State of California (the "State") and California State Lands Commission (the "Commission," and collectively with the State, the "Defendants").

Debtor Venoco LLC ("Venoco") was a party to leases with the Defendants for drilling rights in the South Ellwood Field ("SEF") off the coast of California. Venoco owned Platform Holly, an offshore oil platform which it used to conduct drilling operations in the SEF. *Id.*, ¶ 2. An onshore facility known as the Ellwood

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[2] For purposes of deciding the motions to dismiss, the Court will accept all of the factual allegations in the Complaint – not conclusions – as true and construe the Complaint in the light most favorable to plaintiff. *Fowler v. UPMC Shadyside*, 578 F. 3d 203, 210 (3d Cir. 2009).

Onshore Facility ("EOF")[3], was used to process oil and gas from Platform Holly. *Id.*, Exhibit E, Attachment 1. The EOF is located on land approximately 2.8 miles north of Platform Holly. Platform Holly and the EOF are integrated components of the oil production in the SEF. *Id.*, ¶¶ 24-35.

Now, the integrated components are needed to plug and abandon the Platform Holly wells. *Id.*, Exhibit A, page 2. On April 17, 2017, Debtors quitclaimed the SEF Leases back to the Commission and thereby relinquished all of their right, title and interest in the SEF. The relinquishment included Platform Holly. *Id.*, ¶ 2. Afterwards, Debtors no longer had an interest in the SEF Leases, the wells or the real property underlying the SEF Leases. *Id.* The Commission then became responsible for decommissioning Platform Holly and the SEF. *Id.* The Commission could seek to recover the costs from Debtors' estate, or perhaps from predecessors who had operated the SEF such as ExxonMobil Corporation. *Id.*

Three days before the quitclaims, Venoco and the Commission entered into a Reimbursement for Temporary Services Agreement ("RTSA") which provided that the Commission would reimburse Venoco for the cost to operate the SEF Leases on an interim basis and the Commission received access and use rights to the EOF. *Id.*, ¶ 3. The RTSA terminated on September 15, 2017,

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[3] The EOF is situated on a triangular-shaped .46 acre site which Venoco acquired from Mobil Oil Company in 1997. *Id.,* ¶ 24.

and Debtors transitioned the operations of the SEF to the Commission's third-party contractor. *Id.*

After the RTSA terminated, Venoco and the Commission entered into an agreement (the "Gap Agreement") giving the Commission the temporary use of the EOF to continue to decommission Platform Holly and the SEF. *Id.*, ¶ 4. The Commission agreed to pay Venoco for its use of the EOF. Later, by its terms, Debtors terminated the Gap Agreement, as amended, effective October 15, 2018, and initiated the adversary proceeding the next day. *Id.* The Defendants have not fully paid Debtors for Defendants' use and occupancy of the EOF, which in part led to Debtors filing the instant adversary proceeding. *Id.*, Exhibit D.

It appears that any interruption in the maintenance and operation of the EOF is a threat to the public health, safety and the environment. *Id.*, ¶ 5. The substantive issue in the adversary proceeding is whether the Commission has the right to continue occupying and using the EOF without buying it from or paying rent to Debtors.

DISCUSSION

On their face, the Defendants' motions to dismiss misleadingly appear to be straightforward and uncomplicated. The plaintiff is the post-confirmation Trustee who is asserting the Trust's state law claims of inverse

condemnation.[4] Further, the defendants are the State of California, which appears to be clothed in sovereign immunity, and one of its agencies. The Court would readily dismiss the adversary proceeding were it not for the facts that the adversary proceeding is an *in rem* matter and that the Commission, on behalf of the State, has filed a proof of claim with the Court seeking approximately $130 million. The Trustee is seeking "just compensation" for the taking of the EOF and, by necessity, the proof will require a fair market valuation. Further, the adversary proceeding is an *in rem* proceeding. *See*, *e.g.*, *U.S. v. 645 Acres of Land*, 409 F. 3d 139,145-46 3d Cir. (2005) (condemnation proceedings are *in rem*). Therefore, a closer look is warranted.

The Defendants make several arguments in support of their position that the Court lacks subject matter jurisdiction over Debtors' adversary proceeding.

1. The Court does not have jurisdiction over the State because of the Eleventh Amendment to the Constitution of the United States (the "Constitution") and sovereign immunity.

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[4] "Inverse condemnation" is a term describing the situation in which the government takes but does not pay for private property. The "condemnation" is inverse because it is the reverse of the normal situation where the government is the plaintiff and the land owner is the defendant. "An inverse condemnation action is a constitutionally adequate procedure for obtaining just compensation when the government seizes property without initiating formal condemnation procedures." *Peduto v. City of North Wildwood*, 878 F. 2d 725, 728 (3d Cir. 1989).

2. The Court lacks "arising" in or "related to" jurisdiction.

3. Jurisdiction is lacking for "just compensation" under the Fifth Amendment to the Constitution and Section105(a) of the Bankruptcy Code.

4. The Trustee failed to complete his state law remedies.

5. The Court should decline to exercise jurisdiction.

Finally, if they do not prevail on the jurisdiction defenses, Defendants argue that the Complaint fails to state a claim.

The Court is satisfied that it has subject matter jurisdiction, sovereign immunity does not apply or Defendants have waived sovereign immunity, the other defenses are unremitting and Debtors have stated a claim in the Complaint. The Court will discuss those issues and others within. First, the Court will address Defendants' Eleventh Amendment arguments.

The Eleventh Amendment – Sovereign Immunity

The Eleventh Amendment to the Constitution of the United States provides that:

> The Judicial power of the United States shall not be construed to extend to any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of

> another State, or by Citizens or Subjects of any Foreign State.

U.S. Const. amend. XI. The principal modern case which addresses the Eleventh Amendment and sovereign immunity held that a statute which permitted Indian tribes to sue states in federal court was unconstitutional. *Seminole Tribe of Florida v. Florida*, 517 U.S. 44 (1996). The Supreme Court held that "[e]ven when the Constitution vests in Congress complete law-making authority over a particular area, the Eleventh Amendment prevents congressional authorization of suits by private parties against unconsenting states." *Id.* at 72. Should Congress wish to enact a statute to end sovereign immunity that a state enjoys, it must do so by an unequivocal expression that it intended to overturn immunity, and must be acting pursuant to a valid grant of power in the Constitution. *Seminole Tribe*, 517 U.S. at 72-73.

Section 106 of the Bankruptcy Code provides that "sovereign immunity is abrogated as to a governmental unit" with respect to many sections of the Bankruptcy Code. While it would appear that Section 106 defeats many claims of sovereign immunity, the Third Circuit disagrees. In a carefully written opinion, the Third Circuit ruled that Section 106 is unconstitutional. *See Sacred Heart Hospital v. Dep't of Public Welfare* (*In re Sacred Heart Hospital*), 133 F. 3d 237, 243 (3d Cir. 1998). Accordingly, Section 106 is unavailable to support Debtors' case against the State.

Earlier this year, Chief Judge Christopher S. Sontchi of the Delaware Bankruptcy Court, issued a "scholarly opinion" with "intricate dissection"[5] of the law in which he clarified the intersection of bankruptcy law and sovereign immunity. *See In re La Paloma Generating Company*, 588 B.R. 695 (Bankr. D. Del. 2018). The Court reads *La Paloma* and Chief Judge Sontchi's careful analysis of Supreme Court and Third Circuit precedents to stand for the proposition that the *in rem* jurisdiction of the bankruptcy court defeats a claim of sovereign immunity. *Id.*, 588 B.R. at 727-32. The condemnation case is an *in rem* proceeding to which the Court's jurisdiction attaches. *Peduto*, 878 F. 2d at 728.

There are several other reasons which cause the Court at the motion to dismiss stage to deny dismissal on account of sovereign immunity. First, the Commission and the State are both at risk for liability because the Commission was acting on behalf of the State.[6] At this early stage before there has been any discovery, the Court views the State and the Commission as one and the actions of the Commission are attributable to the State. Second, the Commission filed a $130 million

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[5] The quoted words are the view of William Rochelle, Editor at Large of the American Bankruptcy Institute. The praise appears in Mr. Rochelle's August 1, 2018 column. The Court fully agrees with Mr. Rochelle's assessment.

[6] *See*, *e.g.*, *City of Long Beach v. Mansell*, 3 Cal. 3d 462, 468 n. 3 (1970) (the State of California acted through the State Lands Commission); *State of California ex rel. State Lands Comm'n v. County of Orange*, 134 Cal. App. 3d 20, 22 (1982) (making reference to the State of California acting through the State Lands Commission).

proof of claim in the bankruptcy case for matters related to the Defendants' abandonment of Platform Holly and the EOF. It is impossible to make sense of proceeding with the Defendants' claim in Delaware and the inverse condemnation case proceeding across the country in California. Third, this is an inverse condemnation case. Governmental bodies (and often states) are natural parties in such suits given the very nature of the action. *See*, *e.g.*, *Palazzolo v. Rhode Island*, 533 U.S. 606 (2001). For these reasons, sovereign immunity does not command the Defendants' dismissal.

Jurisdiction

The State and the Commission have raised several jurisdiction related defenses which the Court will now address.

a. Core "Arising In" Jurisdiction

Case law has greatly clarified the principles of core – "arising in" and non-core – "related to" jurisdiction. The State and the Commission argue that neither principle applies to them. The Court disagrees. There are many decisions which address the issues. One of the leading decisions on the history of confirmation, releases and jurisdiction can be found in this district from the learned and thorough decisions in *In re Millennium Lab Holdings II, LLC*, 575 B.R. 252 (Bankr. D. Del. 2017), *aff'd*, 591 B.R. 559 (D. Del. 2018). In *Millenium*, the bankruptcy court and the district court on

appeal discussed at length bankruptcy jurisdiction and core and non-core jurisdiction and the effectiveness of non-consensual third-party releases. The bankruptcy court and the district court agreed that the bankruptcy court had jurisdiction to grant third-party releases.

Core versus noncore and "arising in" and "related to" principles were fully addressed by the Third Circuit in *Resorts Int'l Inc. v. Price Waterhouse & Co., LLP* (*In re Resorts Int'l, Inc.*), 372 F. 3d 154 (3d Cir. 2004)[7]. *Resorts* explains that bankruptcy courts have jurisdiction over cases under title 11, matters arising under title 11, proceedings which arise in a case under title 11 and proceedings which are related to a case under title 11. *Id.* at 162. The first three categories are considered core, and those in the final category are considered non-core. In *Resorts*, the Third Circuit held that:

1. A core proceeding raises rights which the Bankruptcy Code enumerates or which by their very nature would only arise in a bankruptcy case. *Id.* at 162-163, citing *Torkelson v. Maggio,* (*In re the Guild and Gallery Plus, Inc.*) 72 F. 3d 1171, 1178 (3d Cir. 1996). The Third Circuit noted that 28 U.S.C. § 157(b)(2) provides examples of core proceedings, including proceedings that affect the liquidation of assets of the estate. *Resorts*, 372 F. 3d at 162. The Third Circuit further explained that a core proceeding "'invokes a substantive right provided by title 11'" or one

[7] In *Resorts*, the issue was whether post-confirmation the bankruptcy court had jurisdiction over an accounting malpractice case.

that " 'by its nature could only arise in the context of a bankruptcy case.' " *Id.*, 372 F. 3d at 162-63, *quoting In re Guild & Gallery Plus*, 72 F. 3d at 1178, *quoting In re Marcus Hook Dev. Park, Inc.*, 943 F. 2d 261, 264 (3d Cir. 1991).

2. Bankruptcy courts have jurisdiction if the outcome could "conceivably have an effect on the bankruptcy estate. *Id.* at 164. A matter of this nature is "related to" the bankruptcy case. *See Pacor, Inc. v. Higgins*, 743 F. 2d 984, 994 (3d Cir. 1984). The Third Circuit stated that:

> With "related to" jurisdiction, Congress intended to grant bankruptcy courts "comprehensive jurisdiction" so that they could "deal efficiently and expeditiously" with matters connected with the bankruptcy estate.

Resorts, 372 F. 3d at 163-64, *citing Celotex Corp. v. Edwards*, 514 U.S. 300, 308 (1995) which in turn, quoted *Pacor*, 743 F. 2d at 994. One of these "effects" is a challenge to the fundamental integrity of the bankruptcy process. *See Emerald Cap. Advisors Corp. v. Karma Automotive, LLC* (*In re FAH Liquidating Corp.*), 567 B.R. 464 (Bankr. D. Del. 2017), in which the Court found that "arising in" jurisdiction applied because the claims suggested an issue with the integrity of the bankruptcy process.

3. Bankruptcy courts have jurisdiction if the proceeding could "conceivably" have "any effect" on the bankruptcy estate and its administration, *quoting Pacor*, 743 F. 2d at 994.

4. After plan confirmation, jurisdiction is more tenuous but "the essential inquiry appears to be whether there is a close nexus to the bankruptcy plan or proceeding sufficient to uphold bankruptcy court jurisdiction over the matter." *Resorts*, 372 F. 3d at 166-67.

The Trustee argues that the Court has core, "arising in" jurisdiction by virtue of the "intimate connection between this [Adversary] Proceeding and the underlying bankruptcy." Plaintiff's Answering Brief, page 20. For this proposition, the Trustee alleges that: (1) Defendants' actions gave Debtors no option except to protect their estate and (2) Defendants actively participated in and availed themselves of the Court and its processes. The Trustee asserts that the adversary proceeding addresses the administration of the estate and is therefore one of the "core" categories under 28 U.S.C. § 157(b)(2)(A). Next, the Trustee claims that Defendants continuing occupation and use of the EOF frustrates the liquidation of the estate's assets which qualifies as "core" under 28 U.S.C. § 157(b)(2)(A). Finally, the Trustee's Complaint constitutes a counterclaim which qualifies it for core treatment pursuant to 28 U.S.C. § 157(b)(2)(C).

The Defendants answer the Trustee's arguments by arguing themselves that the inverse condemnation action (1) belongs in state court, (2) is not a proceeding seeking to enforce or interpret a Plan provision, and (3) is not a counterclaim or in the nature of a counterclaim.

The Court turns to decisional law and concludes that the adversary proceeding is core. The *Resorts* decision backs the Court's conclusion. Surely the adversary proceeding is not collateral to the bankruptcy case, it is directly relevant to the Defendants' proof of claim. *Resorts* decided that the proceeding in question was not core because it would have only an incidental effect on the reorganized debtor. *Resorts*, 372 F. 3d at 169. Here, the Defendants' proof of claim and the adversary proceeding have an enormous affect on Debtors' estate. Further, and unlike *Resorts*, although the potential to add to the Trust's assets "does not necessarily create a close nexus sufficient to confer 'related to' bankruptcy court jurisdiction post-confirmation," (*id.* at 170), the adversary proceeding certainly and strongly bears weight on the Defendants' proof of claim. Although the quoted language refers to non-core "related to" jurisdiction, the point to be made also applies to "arising in" jurisdiction.

The adversary proceeding will not simply increase the Trust's assets if successful. Instead, the Trustee seeks either to compel a resolution of the ownership of the EOF or as a counter to Defendants' proof of claim. Estate counterclaims against persons filing claims is a category enumerated as providing core "arising in" jurisdiction. In *Penson Technologies LLC v. Schonfeld Grp. Holdings LLC* (*In re Penson Worldwide*), 587 B.R. 6, 12-13 (Bankr. D. Del. 2018), a matter recently decided, a creditor filed a proof of claim based on a contract, to which the debtor filed an adversary proceeding. The creditor-defendant asked the court "to dismiss the

matter, enforce a forum selection clause, abstain or otherwise transfer the case to a court in New York." 587 B.R. at 8. The court held that an adversary proceeding based on the same contract was a core proceeding under 28 U.S.C. § 157(b)(2)(C) and quoted the Supreme Court, which had written that, "He who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance must abide the consequences of that procedure." *Stern v. Marshall*, 131 S. Ct. 2594, 2616 (2011). It is clear that Defendants have sought the bankruptcy court's assistance and therefore should answer to the Complaint in Delaware bankruptcy court.

In ResCap Liq. Trust v. PHH Mortg. Corp., 518 B.R. 259, 264 (S.D.N.Y. 2014), the district court ruled that an adversary proceeding which the debtor filed in response to a creditor's proof of claim was a counterclaim even though it was based on state – not bankruptcy – law and was not related to the proof of claim.[8] Both *Penson Techs.* and *ResCap* support the Court's finding that the adversary proceeding qualifies as a counterclaim to the Defendants' proof of claim. Therefore, the adversary proceeding is core and will almost certainly be resolved, or is resolvable, in the claim proceeding, i.e., Defendants' $130 million claim arising from Platform Holly and the EOF.

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[8] For reasons the Court does not find exist here, the district court withdrew the reference and transferred the adversary proceeding from New York to Minnesota.

It is for these reasons that the Court deems the adversary proceeding to "arise in" the bankruptcy case and that the Court has jurisdiction. The adversary proceeding draws on rights which in the context of the case could arise only in bankruptcy, has a significant affect on the administration of the estate and, finally, is a counterclaim to Defendants' proof of claim.

b. Non-Core "Related To" Jurisdiction

If the Court is mistaken and it does not have core "arising in" jurisdiction, it assuredly has "related to" jurisdiction. The concept of a matter sustaining "related to" jurisdiction is very important in the instant case. If the Trustee is successful in his suit and obtains a judgment, it would assuredly impact the outcome of the Defendants' proof of claim proceeding and any distribution to creditors, thus establishing that the adversary proceeding bears a close nexus to the Plan and to the administration of the estate. The test for "related to" jurisdiction is that a close nexus exists between the adversary proceeding and the bankruptcy plan. *Resorts*, 372 F. 3d at 166-67. The Third Circuit has ruled that a close nexus exists when the matter at hand affects "the interpretation, implementation, consummation, execution, or administration of a confirmed plan or incorporated litigation trust agreement." *Id.* at 168-69. Here, a decision on the Trust's claims in the Complaint will assuredly affect the administration of the Plan and Trust Agreement. In fact, there is a stark difference between *Resorts* in which the Third Circuit found there was no "related to" jurisdiction and the

present adversary proceeding. The litigation trustee filed the malpractice action in *Resorts* almost seven years after the debtor's plan went effective. In the adversary proceeding, the Trustee filed the case within one month of the Plan going effective, which leads the Court to believe that a close nexus exists between the adversary proceeding and the Plan.

In addition, helpful in the Court's thinking is the Supreme Court's decision in *Executive Benefits Insurance Agency v. Arkison*, 573 U.S. 25 (2014). There, a bankruptcy trustee sued under a fraudulent transfer theory to recover commissions paid to a noncreditor. The issue the Supreme Court addressed was how courts should proceed when they encounter a non-core claim. In discussing the differences between core and non-core claims, the Supreme Court ruled that with respect to noncore claims, a bankruptcy court can adjudicate such claims provided it issues proposed findings of fact and conclusions of law which a district court then reviews *de novo*. In other words, even a bankruptcy court's proposed findings of fact and conclusions of law in a non-core proceeding can be rectified by the district court's review and treatment of a decision as proposed findings of fact and conclusions of law. *Id.*, 573 U.S. at 39-40.

Other Arguments

Defendants make other arguments why the Trustee's adversary proceeding is futile.

a. Failure to State a Claim

In short, Defendants argue that the Trustee has failed to state a claim because the State and the Commission are separate entities and he has not pleaded a taking or damaging of the EOF. The Defendants argue that the Complaint must therefore be dismissed.

The Court finds that the Trustee has borne the burden which the Supreme Court established in *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009) and *Bell Atl. Corp. v. Twombly*, 550 U.S. 544, 570 (2007) and the Third Circuit in *Fowler*, 578 F. 3d at 210. The Trustee has stated in short and plain statements the plausible claim that Defendants are responsible for the inverse condemnation of the EOF such that discovery may establish the elements that Defendants complain do not appear in the Complaint. Further, the Third Circuit stated in a two-part test in applying *Iqbal*:

> First, the factual and legal elements of a claim should be separated. The [court] must accept all of the complaint's well-pleaded facts as true, but may disregard any legal conclusions. Second, a [court] must then determine whether the facts alleged in the complaint are sufficient to show that the plaintiff has a plausible claim for relief.

Fowler, 578 F. 3d at 210-11. The Trustee has adequately stated plausible claims and is entitled to establish the validity of the claims through discovery and, if necessary, through trial.

b. Failure to Exhaust State Law Remedies

Defendants argue that the Trustee cannot pursue his claim for just compensation, citing *Williamson County Regional Planning Comms'n v. Hamilton Bank of Johnson City*, 473 U.S. 172, 195 (1985). The Supreme Court held on the facts of *Williamson County* that until a land owner used a state's procedure, he could not claim the absence of just compensation. But as the Trustee counters, *Williamson County*[9] was not a bankruptcy case and to find that the Trustee has not exhausted his state court remedies would deprive the Trustee of his choice of forum. In *PVI Assocs. v. Redevelopment Corp.* (*In re PVI Assocs.*), 181 B.R. 210, 218 (Bankr. E.D. Pa. 1995), the court did not apply *Williamson County.* The Court denied a motion to dismiss an inverse condemnation case in which the defendant argued that debtor failed to exhaust state remedies. Defendants counter that other courts have continued to follow *Williamson County* – but do not cite a case from the Third Circuit. Defendants also argue that *PVI* was decided as it was because dismissal could have affected debtor's reorganization while here the Court has already confirmed the Plan. The Court is satisfied on balance that the Court does not have the basis to deny the Debtors their choice of forum based upon *Williamson County* to which there are questions of its reliability

[9] The Trustee wrote that the requirements in *Williamson County* and "forcing a plaintiff to pursue piecemeal litigation or manipulation by defendants might weigh against applying *Williamson*," *citing Knick v. Twp. of Scott*, 862 F. 3d 310, 327 (3d Cir. 2017), *cert. granted in part sub nom. Knick v. Twp. Of Scott, P.A.*, 138 S. Ct. 1262 (2018). Trustee's Brief, page 18.

and impact. Accordingly, the Trustee was not required to exhaust state procedures.

c. Police Powers

The State argues that the California Police Powers Doctrine bars the adversary proceeding because a valid exercise of the State's police powers *often* (not *always*) does not require compensation even if the State damages the property. The State cites *Customer Co. v. City of Sacremento*, 10 Cal. 4th 368, 383 (Cal. 1995). Cases, however, establish that the Police Powers doctrine applies only in narrow circumstances and when government acts because of "public necessity and to avert impending peril." *See Holtz v. Superior Court of San Francisco*, 3 Cal. 3d 296, 305. Whether the Defendants' use of the EOF satisfies the test is an issue of fact which the Court is fully capable of determining.

Abstention

The judicially created doctrine of "abstention" dictates that a federal court will decline to exercise its jurisdiction and will defer to a state court which will then have the opportunity to decide the issue. The Court recognizes that abstention is an extraordinary exception to its responsibility to rule on matters before it. The Court is therefore generally reluctant to abstain from a case properly before it. The instant matter represents a unique set of facts upon which the Court bases its decision not to abstain.

The applicable statute is 28 U.S.C. § 1334(c)(1) which states:

> Except with respect to a case under chapter 15 of title 11, nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11.

The Court considers twelve factors in determining whether or not to abstain. The factors are:

(1) the effect or lack thereof on the efficient administration of the estate if the Court abstains;

(2) extent to which state law issues predominate over bankruptcy issues;

(3) difficult or unsettled nature of applicable law;

(4) presence of related proceeding commenced in state court or other nonbankruptcy proceeding;

(5) jurisdictional basis, if any, other than § 1334;

(6) degree of relatedness or remoteness of proceeding to main bankruptcy case;

(7) the substance rather than the form of an asserted core proceeding;

(8) the feasibility of severing state law claims from core bankruptcy matters to allow judgments to be entered in state court with enforcement left to the bankruptcy court;

(9) the burden of the bankruptcy court's docket;

(10) the likelihood that the commencement of the proceeding in bankruptcy court involves forum shopping by one of the parties;

(11) the existence of a right to a jury trial;

(12) the presence in the proceeding of non-debtor parties;

DHP Holdings II Corp. v. Peter Skop Industries, Inc., (*In re DHP Holdings II Corp.*) 435 B.R. 220, 223-24 (Bankr. D. Del. 2010). Evaluating the factors is not "merely a mathematical exercise." *Id.* at 234, quoting from *Trans World Airlines, Inc. v. Karabu Corp.* (*In re Trans World Airlines, Inc.*) 196 B.R. 711, 715 (Bankr. D. Del. 1996). Of the twelve factors, most important are (1) the effect on the administration of the estate, (2) whether the claim involves only state law issues, and (7) whether the proceeding is core or non-core. *See*, *e.g.*, *Fruit of the Loom, Inc. v. Magnetek, Inc.* (*In re Fruit of the Loom, Inc.*), 407 B.R. 593, 600 (Bankr. D. Del. 2009).

In evaluating the factors, it is clear to the Court that some of the factors favor the Trustee while others favor Defendants. The Court will not just mathematically add the factors to determine the party which has

the most factors in their column. Instead, the Court will take into consideration and discuss what it considers to be the more important factors in this case.

1. Effect on Administration of the Estate if the Court Abstains

This factor clearly weighs in the Trust's favor and against abstention. The Defendants have a claim pending and the Trustee has the adversary proceeding which, if successful, will negate some or all of the claim.

2. Extent to Which State Law Issues Predominate Over Bankruptcy Issues

Clearly, state law issues predominate, which favors the Defendants. The Court is, however, very accustomed to deciding state law issues which somewhat reduces the significance of this factor.

3. Core v. Non-Core Status

The Court has found that the adversary proceeding is core which therefore gives the advantage to Debtors. However, even if the adversary proceeding is non-core, the relationship to the Chapter 11 case is such strength that the advantage remains with Debtors.

4. Degree of Relatedness or Remoteness of the Adversary Proceeding to the Main Bankruptcy Case

There is a close relationship between the adversary proceeding and the main bankruptcy case, which favors not abstaining.

5. Commencement in Bankruptcy Court Involves Forum Shopping

The Court is of the view that many, if not most, filings involve forum shopping. Parties file cases where they think they will do best. Here, however, the Court is satisfied that the Trustee filed the adversary proceeding in the bankruptcy court because there was a case and a proof of claim already present here. The Court finds that the Trustee did not forum shop when he filed here. This factor favors the Trustee.

6. The Existence of a Right to Jury Trial

It is not clear that the right to a jury trial of the adversary proceeding exists because it is a core proceeding. If, however, the District Court should withdraw the reference, it is beyond a mere possibility that the District Court would direct the Court to oversee pretrial matters. This factor is a draw.

The Court will not abstain. After analyzing all of the twelve factors and especially the factors it considers most important, the Court concludes that it would

be inappropriate to abstain. The Penson court stated the Court's conclusion very aptly when it wrote:

> Fundamentally, this adversary proceeding involves an objection to a proof of claim. That it involves resolution of state law issues is thus unremarkable. The state law issues are not complex, and judicial economy suggests that the objection to the proof of claim and Plaintiff's counter-claims – which are inextricably interlinked with Defendant's proof of claim – be resolved by one court. That court should be the bankruptcy court as the claim allowance process is a quintessential bankruptcy court function. None of the factors that favor abstention convince me that, in this particular case, the interests of justice merits a different outcome. As a result, I decline to abstain.

Penson, 587 B.R. at 24. The Court could not state its conclusion any better.

CONCLUSION

The Court finds that it has jurisdiction over the adversary proceeding. The Court will also not abstain. The parties should commence their discovery promptly, because the Court has scheduled trial to begin on March 19, 2019.

Dated:
January 2, 2019

/s/ Kevin Gross
KEVIN GROSS, U.S.B.J.