Constitutionality of Non-Uniform Quarterly Fees

Michael Francis Pecorella

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Michael Francis Pecorella, J.D. Candidate 2023

Cite as: Constitutionality of Non-Uniform Quarterly Fees, 14 St. John’s Bankr. Research Libr. No. 27 (2022).

INTRODUCTION

In the United States, there are two different government entities entrusted with overseeing the administration of cases under title 11 of the United States Code (the “Bankruptcy Code”). In all but two states, the Office of the United States Trustee, which is a part of the Department of Justice, oversees the administration of bankruptcy cases. In North Carolina and Alabama, the two states that do not have a United States Trustee system, a Bankruptcy Administrator, which is funded by and housed in the Judicial Conference, oversees the administration of bankruptcy cases. The U.S. Trustees and the Bankruptcy Administrators generally have the same role in bankruptcy cases. Moreover, both collect quarterly fees based on quarterly disbursements that debtors in cases under Chapter 11 of the Bankruptcy Code make to their creditors. From 2002 until January 2018 Chapter 11 debtors all paid the same fees in both systems based on the same disbursement formula.

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1 See Siegel v. Fitzgerald (In re Cir. City Stores, Inc.), 996 F.3d 156, 160 (4th Cir. 2021).
2 Id.
3 Id.
4 Id. at 160–61.
5 Id. at 161.
6 Id.
In 2017, Congress changed the quarterly fee calculation for disbursements, codified in 28 U.S.C. § 1930(a)(6)(B) (the “2017 Amendment”) which increased quarterly fees in Chapter 11 cases only in those districts operating under the U.S. Trustee program. The Judiciary Committee report indicates this increase was because of the decline in bankruptcy filings that have traditionally funded a surplus of the U.S Trustee program. Congress, however, did not mandate this fee increase in those districts operating under the Bankruptcy Administrator program. Instead, Congress left the decision to the Judicial Conference to impose such fees in their discretion.

This divergent fee increase has resulted in numerous Constitutional challenges by debtors and the United States Supreme Court has granted certiorari to resolve the Constitutionality issue. This memorandum summarizes the Constitutional conflict between the courts that has arisen when addressing the uniformity issue under the Bankruptcy Clause of the Constitution. Part I discusses Congressional authority over bankruptcy laws under the Bankruptcy Clause. Parts II and III discuss the limitation on Congressional bankruptcy power. Part IV discusses the circuit split that has arisen over the 2017 Amendment.

DISCUSSION

I. Congressional Authority Over Bankruptcy Laws

Congress has broad authority under the Bankruptcy Clause of the Constitution, which grants Congress the authority “[t]o establish . . . uniform laws on the subject of bankruptcies throughout the United States.” The United States Supreme Court has adopted a broad and expansive

10 11 U.S.C. § 1930(a)(7) (“In districts that are not a part of a United States trustee region . . . the Judicial Conference of the United States may require . . .”).
11 See Siegel, 996 F.3d at 156, cert. granted, 142 S. Ct. 752 (U.S. Jan. 10, 2022) (No. 21-441).
II. Affirmative Limitation of Uniformity Still Allows Flexibility

Prior to 1982, the United States Supreme Court never struck down a bankruptcy law for failing to be uniform. The court has stated “[t]he uniformity requirement is not a straitjacket that forbids Congress to distinguish among classes of debtors, nor does it prohibit Congress from recognizing that state laws do not treat commercial transactions in a uniform manner.” Furthermore “[t]he Uniformity provision does not deny Congress the power to take into account differences that exist between different parts of the country, and to fashion legislation to resolve geographically isolated problems.” Thus, while there is a uniformity requirement explicit in the Constitution, Congress has flexibility to address problems they find in non-uniform ways.

III. Outer Limits on Uniformity Requirement

The first and only time the Supreme Court struck down a law on a bankruptcy uniformity challenge was in 1982 when Congress adopted a law that applied to only one debtor. This case
was distinguished from an earlier case that addressed a similar uniformity challenge in the *Reg’l Rail Reorganization Act Cases*. In that case the court upheld a law that applied only to railroads in the Northeast. The court found that the law applied uniformly because there were no other reorganization proceedings pending outside of that defined area and was addressing a “geographically isolated problem.” Whereas in *Ry. Lab. Executives’ Ass’n*, “The employee protection provisions of RITA cover neither a defined class of debtors nor a particular type of problem, but a particular problem of one bankrupt railroad.” The court stated that “[t]o survive scrutiny under the bankruptcy clause, a law must at least apply uniformly to a defined class of debtors.”

IV. Circuit Split Over Uniformity of the 2017 Amendment

A. The Fourth and Fifth Circuit’s decision to uphold the 2017 Amendment as Constitutionally uniform within the “geographically isolated problem” exception

The first circuit court to rule on the Constitutionality of the 2017 Amendment was the Fifth Circuit in the case of *In re Buffets*. The court started its Constitutionality analysis by rejecting the argument the 2017 Amendment is not a law on bankruptcies and thus not subject to the uniformity requirement. However, the court noted that this is an argument that has not been readily accepted. The court concluded, bankruptcy is essentially “the relation[] between an insolvent or nonpaying or fraudulent debtor, and his creditors extending to his and their relief” which the 2017 Amendment directly implicates such relationship.

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21 *Reg’l Rail Reorganization Act Cases*, 419 U.S. at 159.
22 *Id.*
24 *Id.* at 473.
25 *In re Buffets*, L.L.C., 979 F.3d 366 (5th Cir. 2020).
26 *Id.* at 377.
27 *Id.* (finding that “the fee increase has a direct effect on what creditors receive—less than before”).
28 *Id.* (quoting *Wright v. Union Cent. Life Ins. Co.*, 304 U.S. 502, 513-14 (1938)).
The Buffets Court went on to analyze the question of uniformity and found no such uniformity issue.\textsuperscript{29} The court’s reasoning are the same arguments advanced in the \textit{Reg’l Rail Reorganization Act Cases} and \textit{Ry. Lab. Executives’ Ass’n} that call for “flexibility” in congressional power.\textsuperscript{30} The court rejected the argument advanced by \textit{In re Buffets} that geographic uniformity is demanded by the Constitution and made clear that geographical differences will only violate the Constitution when they are “arbitrary.”\textsuperscript{31}

Again, the court advanced the argument derived from \textit{Reg’l Rail Reorganization Act Cases} that put forth the “geographically isolated problem” exception.\textsuperscript{32} The court saw the “geographically isolated problem” as the underfunding in the Trustee District.\textsuperscript{33} Therefore, because this underfunding was a problem in those districts that used the Trustee and not those in the Administrator Districts, Congress provided sufficient justification that addressed the funding in those districts.\textsuperscript{34} The fact that there was a geographical difference was merely incidental to the program specific distinction Congress drew.\textsuperscript{35} Subsequent to the Fifth Circuit’s ruling, other courts have followed this same analytical framework.

Following the structure of the Fifth Circuit’s decision in the \textit{Buffets} case, the Fourth Circuit similarly upheld the 2017 Amendment against a Constitutional challenge.\textsuperscript{36} The Fourth Circuit, like the Fifth, rejected the claim that the 2017 Amendment was not a law on the subject of bankruptcies.\textsuperscript{37} Thus, they likewise had to address the uniformity problem raised and did so in

\begin{itemize}
\item \textsuperscript{29} Id.
\item \textsuperscript{30} Id. at 378 (quoting Reg’l Rail Reorganization Act Cases, 419 U.S. at 158).
\item \textsuperscript{31} Id. (citing \textit{In re Reese}, 91 F.3d 37, 39 (7th Cir. 1996)).
\item \textsuperscript{32} Id.
\item \textsuperscript{33} Id. at 378.
\item \textsuperscript{34} Id.
\item \textsuperscript{35} Id.
\item \textsuperscript{36} See \textit{Siegel}, 996 F.3d 156.
\item \textsuperscript{37} Id. at 164.
\end{itemize}
the same manner as the Fifth Circuit.\textsuperscript{38} The Fourth Circuit again relied on the “geographically isolated problem” exception derived from the \textit{Reg’l Rail Reorganization Act Cases} to counter the arbitrary claim.\textsuperscript{39} The court found that Congress permissibly tailored the solution to meet the problem of the underfunded districts “to ensure that the U.S. Trustee program is sufficiently funded by its debtors rather than by the taxpayers.”\textsuperscript{40} The Fourth Circuit like the Fifth Circuit saw this distinction not as a geographic one but one that is “program-specific distinction that only indirectly has a geographic impact.”\textsuperscript{41}

B. The Eleventh Circuit has upheld the 2017 Amendment as Constitutionally uniform on other grounds

The Eleventh Circuit also upheld the Constitutionality of the 2017 Amendment but recognized that it departed from the reasoning employed by the Fourth and Fifth Circuits.\textsuperscript{42} While the court made clear it is not relying on the “geographically isolated problem” exception it noted that those circuit courts that have held that “failure to qualify for the geographically isolated problem exception necessarily means that a uniformity violation has occurred” is inconsistent with the “inherent flexibility of the uniformity requirement . . . .”\textsuperscript{43}

The Eleventh Circuit rested its conclusion as to the Constitutionality on numerous other factors.\textsuperscript{44} As made clear by the Fourth and Fifth Circuit decisions, the court reiterated the inherit flexibility for Congressional action under the Bankruptcy Clause.\textsuperscript{45} The court stated that the Bankruptcy Clause is a limitation on Congresses power and inaction by another branch of
government doesn’t modify or repeal Congressional acts.\textsuperscript{46} The court further articulated that if there was to be a Constitutional problem, that problem must be attributed to the actions of the Judicial Conference or their inaction in applying fees to the Administrator Districts.\textsuperscript{47} Thus, the court found that because the Judicial Conference was charged with the legal authority to implement the increased fees and failed to do so immediately after the 2017 Amendment passed by Congress did not violate the Bankruptcy Clause.\textsuperscript{48} The court further held that the Judicial Conference’s inaction did not violate the Constitution because there is “well-established” precedent that allows for different treatment of similar debtors in different states.\textsuperscript{49} The “well-established” principals the court spoke of are state exemptions prescribed by state law.\textsuperscript{50} In both circumstances of state law exemptions and of the disparity caused by the 2017 Amendment, the problem was with an actor other than Congress and Congress could not have foreseen the Judicial Conferences inaction.\textsuperscript{51}

More persuasive for the Eleventh Circuit was the temporary nature of the disparity that pales in comparison to the ongoing disparity due to state exemptions.\textsuperscript{52} The court saw this as \textit{a fortiori}.\textsuperscript{53} “[E]ven that ongoing and permanent disparity does not violate the flexible uniformity requirement, we believe it follows, \textit{a fortiori}, that there is no violation in the context of the instant temporary disparity which was promptly remedied by Congress when it unexpectedly occurred.”\textsuperscript{54} Thus, the Eleventh Circuit justified its Constitutionality decision first because the

\textsuperscript{46} Id. at *61.
\textsuperscript{47} Id.
\textsuperscript{48} Id.
\textsuperscript{49} Id.
\textsuperscript{50} Id. (quoting Ry. Lab. Executives’ Ass’n v. Gibbons, 455 U.S. 457, 469 (1982)) (“Congress can give effect to the allowance of exemptions prescribed by state law without violating the uniformity requirement.”).
\textsuperscript{51} Id. at *62.
\textsuperscript{52} Id.
\textsuperscript{53} Id.
\textsuperscript{54} Id. at *63.
inaction of the Judicial Conference in adopting the fees was not a result of congressional actions violating uniformity.\(^{55}\) Second, because of state exemptions that already allow for the different treatment of different debtors.\(^{56}\) Finally, because of the relatively short time disparity for which the debtors were treated differently.\(^{57}\)

C. Lower court decisions upholding the 2017 Amendment as Constitutional

Numerous lower courts have also upheld the constitutionality of the 2017 Amendment.\(^{58}\) The discussion below is an examination of the lower courts that have upheld the constitutionality of the 2017 Amendment for similar reasons as the Fourth and Fifth Circuits.

The Bankruptcy Court for the District of Delaware upheld the constitutionality of the 2017 Amendment on the grounds that it did apply uniformly to a class of debtors and used the “geographically isolated problem” exception.\(^{59}\) In asserting that the law did apply uniformly to a class of debtors it distinguished the 2017 Amendment from the law in \textit{Ry. Lab. Executives’ Ass’n}.\(^{60}\) Whereas the law in that case applied to only one debtor, here the 2017 Amendment applied uniformly to a class of debtors.\(^{61}\) Like the Eleventh Circuit, the court also narrowed the question as to whether the 2017 Amendment was uniform.\(^{62}\) The court answered this question in the affirmative, holding that the 2017 Amendment is uniform because it applies “with the same force and effect in every place where the subject of it is found . . . all UST districts.”\(^{63}\) Like the Fourth and Fifth Circuits, the court found that it was appropriate for Congress to address the

\(^{55}\) \textit{Id.} at *61.  
\(^{56}\) \textit{Id.} at *62.  
\(^{57}\) \textit{Id.} at *63.  
\(^{59}\) \textit{In re Exide Techs.}, 611 B.R. at 36–37.  
\(^{60}\) \textit{Id.} at 36.  
\(^{61}\) \textit{Id.}  
\(^{62}\) \textit{Id.} at 37.  
\(^{63}\) \textit{Id.}
“geographically isolated problem” of the underfunding of the U.S. Trustee system with an increase in fees in those districts.64

Likewise, the bankruptcy court for the Southern District of Ohio upheld the 2017 Amendment as constitutional.65 The Ohio bankruptcy court relied on the “geographically isolated problem” exception just as a majority of other courts have done so and on the same reasoning as the Eleventh Circuit that the action Congress took did not present a uniformity problem.66 The “geographically isolated problem” was the underfunding in the U.S. Trustee system fund and only existed in those districts that used the U.S. Trustee.67 Thus, because of the flexibility that Congress has in fashioning legislation to address such problems, “Congress had the power to fix the underfunding problem where it found it.”68 Persuasive also for the court was that the 2017 Amendment applied uniformly to a class of debtors and is not like the single debtor targeted from *Ry. Lab. Executives’ Ass ’n*.69 Finally, just as the Eleventh Circuit did the court here did not blame Congress for the divergent fees, but the Judicial Conference.70 “[A]ctions that were or were not taken as part of the implementation of the statute do not make the statute non-uniform.”71 The Judicial conference treated the debtors differently and did not modify what Congress had done when they enacted the 2017 Amendment.72

The Court of Federal Claims has also ruled as to the Constitutionality of the 2017 Amendment and adopted the same reasoning set forth in the *Buffets* case.73 The court did not

64 *Id.*
65 *In re ASPC Corp.*, 631 B.R. 18.
66 *Id.* at 33–35.
67 *Id.*
68 *Id.*
69 *Id.*
70 *Id.* at 34.
71 *Id.*
72 *Id.* at 35.
analyze the 2017 Amendment with their own analysis but simply adopted the reasoning directly from the Fifth Circuit’s opinion.\textsuperscript{74}

D. The Second and Tenth Circuits decision that the 2017 Amendment is unconstitutionally non uniform

The Second Circuit and the Tenth Circuit have ruled that the 2017 Amendment is unconstitutional because it violates the Bankruptcy Clause of the Constitution.\textsuperscript{75} The Second Circuit was the first circuit court to declare the amendment unconstitutional and criticized the Fourth and Fifth Circuits for finding otherwise.\textsuperscript{76}

The Second Circuit rejected the argument that Congress mandated equal fees when it adopted the 2017 Amendment across both systems, and it was simply the Judicial Conferences delay in implementing the increased fees that led to the uniformity issues.\textsuperscript{77} The court declined this argument because it “asks [] [the court] to ignore the distinction between the ‘shall’ used in § 1930(a)(6) and the ‘may’ used in § 1930(a)(7).”\textsuperscript{78} The court found that the language was chosen for a specific reason, setting apart different fees, and Congress did so intentionally.\textsuperscript{79} Thus, the grant of such permissive authority violated the uniformity requirement, and the court had to declare it unconstitutional.\textsuperscript{80}

The Second Circuit also addressed the “geographically isolated problem” exception and likewise rejected that argument.\textsuperscript{81} Even failing to accept this argument, the court does recognize

\textsuperscript{74} See id. at 131 (“The court therefore applies the Fifth Circuit’s reasoning to each of plaintiffs’ claims in this case.”).
\textsuperscript{75} See Clinton Nurseries of Md., Inc. v. Harrington (In re Clinton Nurseries, Inc.), 998 F.3d 56; In re John Q. Hammons Fall 2006, LLC, 15 F.4th 1011 (10th Cir. 2021).
\textsuperscript{76} See Clinton Nurseries of Md., Inc., 998 F.3d at 68 (“We are concerned, however, that the bankruptcy courts and the Buffets and Circuit City opinions have overlooked a critical distinction.”).
\textsuperscript{77} Id. at 65.
\textsuperscript{78} Id. at 66.
\textsuperscript{79} Id.
\textsuperscript{80} Id. at 67.
\textsuperscript{81} Id.
the flexibility that exists in the Bankruptcy Clause.\textsuperscript{82} Even recognizing that such flexibility exits
the court found that this exception was limited by \textit{Ry. Lab. Executives’ Ass’n}. and “must at least
apply uniformly to a defined class of debtors.”\textsuperscript{83} Therefore, because the 2017 Amendment
applied to debtors whose disbursements exceed a million dollars and those classes exist across
both district systems the 2017 Amendment does not meet the “geographically isolated problem”
exception.\textsuperscript{84} “Two debtors, identical in all respects save the geographic locations in which they
filed for bankruptcy, are charged dramatically different fees.”\textsuperscript{85}

The Tenth Circuit similarly declared the 2017 Amendment unconstitutional for reasons that
come from the reasoning of the Second Circuit.\textsuperscript{86} The court rejected the application of the
“geographically isolated problem” exception for the same reason the Second Circuit did, because
the same class of debtors existed in both Trustee Districts and Bankruptcy Administrator
Districts.\textsuperscript{87}

E. Lower court decisions striking down the 2017 Amendment as unconstitutional

The District Court for the Central District of California adopted similar reasoning employed
by the Second Circuit.\textsuperscript{88} “The Court is not persuaded by the UST’s argument, or, respectfully, by
the reasoning of other courts, that the relevant class of debtors for the purpose of the 2017
Amendment is Chapter 11 debtors in UST districts.”\textsuperscript{89} The district court admonished Congress
for failing to provide “any justification at all for enacting a non-uniform bankruptcy law” and

\textsuperscript{82} Id. at 67–68 (quoting Reg’l Rail Reorganization Act Cases, 419 U.S. 102, 159 (1974)) (“[T]he uniformity clause
was not intended to hobble Congress by forcing it into nationwide enactments to deal with conditions calling for
remedy in certain regions.”).
\textsuperscript{83} Id. at 68 (quoting Ry. Lab. Executives’ Ass’n v. Gibbons, 455 U.S. 457, 473 (1982)).
\textsuperscript{84} Id. at 69.
\textsuperscript{85} Id.
\textsuperscript{86} See \textit{In re John Q. Hammons Fall 2006, LLC}, 15 F.4th 1011 (10th Cir. 2021).
\textsuperscript{87} Id. at 1024.
\textsuperscript{89} Id. at 946.
thus “regardless of the standard of scrutiny under the Bankruptcy Clause, Congress’s’ decision can only be considered to be irrational and arbitrary.”

CONCLUSION

Courts are divided as to the constitutionality of the 2017 Amendment. The majority of courts have upheld the 2017 Amendment finding no Constitutional uniformity issue. Other courts, however, disagree and found a Constitutional uniformity issue. In June of 2022 the Supreme Court of the United States issued the court’s unanimous opinion and found the fee increase was not geographically uniform. The court remanded the case back to the Fourth Circuit to address the remedy regarding the fees.

90 Id. (citations omitted).
92 Id.