Obtaining Jurisdiction Over States in Bankruptcy Proceedings After Seminole Tribe

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Seminole Tribe of Florida v Florida, 1 marked a dramatic change in the Supreme Court’s Eleventh Amendment jurisprudence, holding that Congress may not abrogate states’ Eleventh Amendment immunity from suit in federal court pursuant to its powers under Article I. Seminole Tribe has sweeping implications because it renders unconstitutional every federal statute that was enacted under Congress’s Article I powers and purports to abrogate states’ Eleventh Amendment immunity. As Justice Stevens cautioned in his dissenting opinion, the decision “prevents Congress from providing a federal forum for a broad range of actions against States, from those sounding in copyright and patent law, to those concerning bankruptcy, environmental law, and the regulation of our vast national economy.”

Justice Stevens’s warning merits serious analysis in the bankruptcy context. Section 106 of the Bankruptcy Code,2 which purports to abrogate states’ immunity from suit in several circumstances, eliminated most barriers to a bankruptcy court’s assertion of jurisdiction over a state. Because Section 106 was enacted under Congress’s Article I powers, however, Seminole Tribe re-establishes these barriers by rendering its blanket abrogation unconstitutional. As a result, states now may invoke their Eleventh Amendment immunity in many factual scenarios where a bankruptcy trustee wants to involve the state in bankruptcy proceedings. For example, a trustee might allege that the state breached a contract to construct public highways, claim a tax refund from the state, or bring other tort or statutory claims against the state, including claims arising under the Bankruptcy Code. When an estate in bankruptcy has meritorious claims against the state, recovery on these claims will help creditors by

2 The Eleventh Amendment provides: “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.” US Const, Amend XI.
3 Seminole Tribe, 517 US at 77 (Stevens dissenting).
increasing the estate's assets. If the state invokes Eleventh Amendment immunity, however, the bankruptcy court may not be able to obtain jurisdiction over the state. Without such jurisdiction, the trustee cannot institute actions against the state in bankruptcy court—likely precluding recovery of these claims.

Justice Stevens's warning suggests that state immunity from bankruptcy proceedings may be a threat to the twin goals of the Bankruptcy Code: (1) maximization and equitable distribution of the assets of the bankruptcy estate and (2) a fresh start for the debtor. Indeed, there are numerous situations where this immunity could conceivably impair the bankruptcy process. With respect to the goal of maximizing the assets of the estate, if a bankruptcy court cannot force a state to turn over to the bankruptcy trustee property obtained as a preferential transfer, or fraudulent conveyance, or in violation of the automatic stay, the creditors will recover fewer assets. Also, if a bankruptcy court does not have jurisdiction over a state to enforce the discharge of the debts of the debtor, a state may continue collection efforts against a debtor after a discharge, precluding a fresh start.

However, while Seminole Tribe may cause the loss of some efficiencies in the bankruptcy process, this Comment argues that it will not seriously impair the bankruptcy system's ability to achieve its twin goals. Bankruptcy courts have a number of tools they can use to mitigate the effects of states' invocation of their Eleventh Amendment immunity, including waiver by the state and the Ex parte Young doctrine, which allows suits against state officials in federal court. These mechanisms alleviate concerns that Seminole Tribe will severely compromise the bankruptcy process. In fact, there is only one conceivable situation where bankruptcy courts' lack of jurisdiction over states could result in both failure to maximize the assets of the bankruptcy estate and inequitable distribution: if they were unable to force states to turn over property obtained in a fraudulent conveyance

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6 "Fresh start" is the policy through which a debtor is discharged by the bankruptcy court from paying his prepetition debts. Fresh start policies apply only to individuals; corporate debtors get no discharge in ordinary bankruptcy proceedings, 11 USC § 727(a)(1) (1994), and the discharge in Chapter 11, 11 USC § 1141 (1994), consummates the exchange of old claims for new claims. See Thomas H. Jackson and Robert E. Scott, On the Nature of Bankruptcy: An Essay on Bankruptcy Sharing and the Creditors' Bargain, 75 Va L Rev 155, 156 n 3 (1989).


9 The Bankruptcy Code provisions relating to discharge are 11 USC §§ 727, 1141, 1228(a)-(b), 1328(b) (1994).

10 209 US 123 (1908).
or preferential transfer. However, this inability does not pose a serious threat to the bankruptcy process because states are not likely to have the resources and information necessary to collect debts aggressively prior to a debtor's bankruptcy filing.

Part I of this Comment provides a brief overview of the Supreme Court's Eleventh Amendment jurisprudence, including a discussion of the *Ex parte Young* doctrine. Part II discusses *Seminole Tribe's* immediate implications for the Bankruptcy Code and concludes that Congress's blanket abrogation of Eleventh Amendment immunity in Section 106 of the Bankruptcy Code is unconstitutional. Part III examines the constitutional requirements for, and scope of, state waivers of Eleventh Amendment immunity. It argues that when a state files a proof of claim, it waives its Eleventh Amendment immunity with respect to claims of the debtor against it arising from the same transaction or occurrence. Finally, Part IV explores the various situations in which states' Eleventh Amendment immunity threatens to undermine the Bankruptcy Code's twin goals of equitable distribution and fresh start, where the state has not waived its immunity.

I. ELEVENTH AMENDMENT IMMUNITY

A. Development of Eleventh Amendment Immunity

In the 1793 case of *Chisholm v Georgia*, the Supreme Court allowed a citizen of South Carolina to sue the state of Georgia for monetary damages. *Chisholm* "literally shocked the Nation," in Chief Justice Rehnquist's words, because the Framers had disclaimed that a federal court could have jurisdiction over a state in light of the common law doctrine of sovereign immunity. In response to *Chisholm*, the states quickly ratified the Eleventh Amendment, which deprives federal courts of jurisdiction over suits against states by citizens of another state. Although schol-

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11 2 US (2 Dall) 419 (1793).
12 The Court reasoned: "If sovereignty be an exemption from suit in any other than the sovereign's own Courts, it follows that when a State, by adopting the Constitution, has agreed to be amenable to the judicial power of the United States, she has, in that respect, given up her right of sovereignty." Id at 452.
14 The Supreme Court has consistently held that an unconsenting state is immune from suits brought in federal court by its own citizens as well as citizens of another state. See *Hans v Louisiana*, 134 US 1, 9-10, 14-15 (1890). However, the Supreme Court has long recognized that municipalities and counties are outside the protection of the Eleventh Amendment and thus are subject to the congressional abrogation of any state law immunities they may enjoy. See *Mt. Healthy City School District Board of Education v Doyle*,
ars have expressed differing views on the Framers' intended scope of the Eleventh Amendment, the Supreme Court has held that the Eleventh Amendment is a constitutional limitation on the federal courts' subject matter jurisdiction in both diversity and federal question cases. According to the Court, "the [Eleventh Amendment] . . . is a specific constitutional bar against hearing even federal claims that otherwise would be within the jurisdiction of the federal courts."

One consequence of the Eleventh Amendment would seem to be that absent federal jurisdiction over states, states could violate with impunity the Constitution and federal law, because, even if a state violated the Constitution, federal courts would be powerless to hold the state accountable. The Supreme Court developed the Ex parte Young doctrine to address this problem.

B. The Ex parte Young Doctrine

The Ex parte Young doctrine allows a party to sue a state official to enjoin a violation of federal law or the Constitution, even when the Eleventh Amendment bars suit against the state itself. In Ex parte Young, shareholders of a railroad company sought to bring an action in federal court to enjoin the Attorney General of Minnesota from enforcing a statute fixing the rates that the railroad could charge. The stockholders alleged that the

429 US 274, 280-81 (1977) (holding that a school board is more like a city than a state and therefore has no Eleventh Amendment immunity); Lincoln County v Luning, 133 US 529, 530 (1890) (holding that only states, not counties, receive Eleventh Amendment immunity). The federal government can bring suit in federal court against a state. United States v Texas, 143 US 621, 644-45 (1892) (finding such power necessary to the "permanence of the Union"). For a more extensive discussion of the history of the Eleventh Amendment, see Doyle Mathis, The Eleventh Amendment: Adoption and Interpretation, 2 Ga L Rev 207, 215-30 (1968); John J. Gibbons, The Eleventh Amendment and State Sovereign Immunity: A Reinterpretation, 83 Colum L Rev 1889, 1890-1941 (1983).


Id at 120.

For a history of the development of the Ex parte Young doctrine through the Supreme Court's 1984 decision in Pennhurst, see David P. Currie, Sovereign Immunity and Suits Against Government Officers, 1984 S Ct Rev 149.

rates were set so high as to deprive them of property without due process of law, in violation of the Fourteenth Amendment of the Constitution. The Court held that the federal courts had jurisdiction over the Attorney General, distinguishing a suit against a state official from a suit against a state. The Court reasoned:

If the act which the state Attorney General seeks to enforce be a violation of the Federal Constitution, the officer in proceeding under such enactment comes into conflict with the superior authority of that Constitution, and he is in that case stripped of his official or representative character and is subjected in his person to the consequences of his individual conduct. The State has no power to impart to him any immunity from responsibility to the supreme authority of the United States.

While *Ex parte Young* itself involved a violation of the Constitution, the Court has applied it to violations of federal law as well. The Supreme Court has limited *Ex parte Young* to actions for prospective injunctive relief; the doctrine does not allow a suit against a state official for recovery of money damages. As the Court has explained:

Both prospective and retrospective relief implicate Eleventh Amendment concerns, but the availability of prospective relief of the sort awarded in *Ex parte Young* gives life to the Supremacy Clause. Remedies designed to end a continuing violation of federal law are necessary to vindicate the federal interest in assuring the supremacy of that law. . . . But compensatory or deterrence interests are insufficient to overcome the dictates of the Eleventh Amendment.

However, the Supreme Court has permitted plaintiffs in *Ex parte Young* actions to recover attorneys' fees on the theory that those

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20 Id.
21 Id at 159-60.
22 Id.
23 See, for example, *Edelman*, 415 US at 664 (involving compliance with federal rules for processing welfare applications).
24 See, for example, *Edelman*, 415 US at 665-69 (refusing to retroactively award benefits that had been withheld from recipients in violation of federal law because the funds to satisfy such an award would come from the state's general revenues); *Ford Motor Co v Department of Treasury of Indiana*, 323 US 459, 464 (1945) (holding that "when the action is in essence one for the recovery of money from the state, the state is the real, substantial party in interest and is entitled to invoke its sovereign immunity from suit even though individual officials are nominal defendants").
25 *Green v Mansour*, 474 US 64, 68 (1985) (citations omitted) (refusing to require the state to give notice to citizens whose benefits were withheld by a state in violation of federal law).
fees are ancillary to the bringing of the action. In *Seminole Tribe*, the Court further narrowed the *Ex parte Young* doctrine to instances where Congress has not established a detailed scheme for remedying violations of federal law.

If a federal court enjoins a state official from violating a federal law under *Ex parte Young* and that official violates the injunction, the court may issue a contempt order against that official. Because the initial *Ex parte Young* action establishes federal jurisdiction over the state official, the court can then impose monetary or other contempt penalties on the official. As the Supreme Court explained in *Hutto v Finney*:

In exercising their prospective powers under *Ex parte Young* and *Edelman v Jordan*, federal courts are not reduced to issuing injunctions against state officers and hoping for compliance. Once issued, an injunction may be enforced. ... Civil contempt may also be punished by a remedial fine, which compensates the party who won the injunction for the effects of his opponent's noncompliance.

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26 See *Missouri v Jenkins*, 491 US 274, 280-81 (1989) (awarding attorneys' fees in civil rights action); *Hutto v Finney*, 437 US 678, 695 (1978) ("[Attorneys' fees] have traditionally been awarded without regard for the States' Eleventh Amendment immunity.").

27 *Seminole Tribe*, 517 US at 73-75. The Court found that Congress had established such a remedial scheme in *Seminole Tribe*, and accordingly denied the federal court jurisdiction over the state official. Id. The Indian Gaming Regulatory Act, 25 USC §§ 2701-21 (1994), provides that if a state fails to negotiate in good faith with the Indian tribe, the only remedy is a court order directing the tribe and the state to agree on a compact within a certain time period. If the parties disregard that order, the only sanction is that each party must submit a proposal to a mediator. Finally, if the state refuses to accept the proposal selected by the mediator, the only sanction is that the mediator shall notify the Secretary of the Interior, who then must develop regulations to govern the issue. In light of this detailed remedial scheme, the Court rejected the idea that Congress intended to authorize *Ex parte Young* actions under the Act. "By contrast with this quite modest set of sanctions, an action brought against a state official under *Ex parte Young* would expose that official to the full remedial powers of a federal court...." Id at 75.

28 For this reason, courts cannot issue standing injunctions against state actors' violations of federal law (for example, a violation of the automatic stay in bankruptcy). In order to obtain jurisdiction over the state actor to issue such an injunction, *Ex parte Young* requires an antecedent violation of federal law. Only after a court establishes jurisdiction under *Ex parte Young* can it exercise its full contempt power. In one pre-*Seminole Tribe* bankruptcy case, however, a court allowed the debtor to recover damages for violation of the automatic stay by a state agency without first enjoining the official in an *Ex parte Young* action, conceiving of the initial violation as contempt of court. See *In re Colon*, 114 Bankr 890, 898 (Bankr E D Pa 1990). Such a conception, however, ignores the antecedent need of the bankruptcy court to acquire jurisdiction over the state official before awarding damages. The court could have issued an order against the state official in an *Ex parte Young* action, enjoining future violations of the automatic stay; if the state official violated that order, contempt damages would be appropriate.


30 Id at 690-91.
The award of damages under the contempt power is distinct from any award of damages for the underlying violation of federal law; the latter is prohibited by the *Ex parte Young* doctrine.

The remainder of this Comment considers the impact of Eleventh Amendment immunity and the *Ex parte Young* doctrine in the bankruptcy context in light of *Seminole Tribe*. A general theme emerges: what *Seminole Tribe* takes away from bankruptcy courts' jurisdiction over states that violate provisions of the Bankruptcy Code, the *Ex parte Young* doctrine replenishes to a substantial extent by allowing bankruptcy courts to assert jurisdiction over the state officials to enjoin those violations.

II. ABROGATION OF ELEVENTH AMENDMENT IMMUNITY

The first step in examining the impact of *Seminole Tribe* on the bankruptcy system is to evaluate the constitutionality of Section 106, the key provision of the Bankruptcy Code relating to bankruptcy courts' ability to assert jurisdiction over a state. Section 106(a) provides for a blanket abrogation of states' Eleventh Amendment immunity with respect to numerous provisions of the

31 11 USC § 106 provides:

(a) Notwithstanding 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 the following:

(1) [Enumerates sections]

(2) The court may hear and determine any issue arising with respect to the application of such sections to governmental units.

(3) The court may issue against such governmental unit an order, process, or judgment under such sections or the Federal Rules of Bankruptcy Procedure, including an order or judgment awarding a money recovery, but not including an award of punitive damages. Such order or judgment for costs and fees under this title or the Federal Rules of Bankruptcy Procedure against any governmental unit shall be consistent with the provisions and limitations of section 2412(d)(2)(A) of title 28.

(4) The enforcement of any such order, process, or judgment against any governmental unit shall be consistent with appropriate nonbankruptcy law applicable to such governmental unit and, in the case of a money judgment against the United States, shall be paid as if it is a judgment rendered by a district court of the United States.

(5) Nothing in this section shall create any substantive claim for relief or cause of action not otherwise existing under this title, the Federal Rules of Bankruptcy Procedure, or nonbankruptcy law.

(b) A governmental unit that has filed a proof of claim in the case is deemed to have waived sovereign immunity with respect to a claim against such governmental unit that is property of the estate and that arose out of the same transaction or occurrence out of which the claim of such governmental unit arose.

(c) Notwithstanding any assertion of sovereign immunity by a governmental unit, there shall be offset against a claim or interest of a governmental unit any claim against such governmental unit that is property of the estate.
Bankruptcy Code. Section 106(b) provides that states filing a proof of claim in the bankruptcy court waive their immunity with respect to claims by the trustee arising out of the same transaction or occurrence. Section 106(c) abrogates immunity with respect to offsetting claims of the trustee against claims of the state. To the extent Section 106 purports to abrogate a state's Eleventh Amendment immunity from suit, it will survive constitutional attack under Seminole Tribe only if Congress enacted it pursuant to its powers under Section 5 of the Fourteenth Amendment, which the Supreme Court held was a valid source of abrogation.

This Part first explains in more detail the Seminole Tribe holding and its relation to Congress's Article I powers. It then considers whether Congress enacted the Bankruptcy Code pursuant to its Fourteenth Amendment powers, and whether in any case Congress has the power under Section 5 to enact a bankruptcy law.

A. Seminole Tribe, Article I, and Section 106

If Congress enacted Section 106 pursuant to its Article I power to establish uniform laws on bankruptcy, Seminole Tribe instructs that its blanket abrogation of Eleventh Amendment immunity is unconstitutional as applied to states. Although Seminole Tribe involved Congress's power under the Indian Commerce Clause of Article I, the majority opinion left no doubt that its holding applied to all Article I powers: "The Eleventh Amendment restricts the judicial power under Article III, and Article I cannot be used to circumvent the constitutional limitations placed upon federal jurisdiction."

Section 106(a) abrogates a governmental unit's sovereign immunity with respect to certain sections of the Code and allows

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33 US Const, Art I, § 8, cl 4.
34 Section 106 does not refer specifically to states; it refers instead to "governmental units." 11 USC § 106. 11 USC § 101(27) (1994) defines "governmental units" to include states. Seminole Tribe does not impact the sovereign immunity of the federal government or any government unit except those protected by the Eleventh Amendment.
35 517 US at 63-66, overruling the plurality decision in Pennsylvania v Union Gas Co 491 US 1, 19 (1989) (holding that Congress could abrogate states' Eleventh Amendment immunity when legislating pursuant to the Interstate Commerce Clause, US Const, Art I, § 8, cl 3). In his dissent in Union Gas, which foreshadowed the Seminole Tribe decision, Justice Scalia asserted that Congress could not abrogate states' Eleventh Amendment immunity pursuant to its Article I powers. Union Gas, 491 US at 42 (Scalia dissenting).
36 US Const, Art I, § 8, cl 3.
37 Seminole Tribe, 517 US at 72-73.
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the bankruptcy court to issue judgments against states, including for recovery of monetary claims. Because it is an express abrogation of immunity by Congress, its application to states is rendered unconstitutional by *Seminole Tribe*.

The analysis of Sections 106(b) and (c) is similar. Section 106(b) provides that when a state files a proof of claim in a bankruptcy proceeding, it waives its immunity with respect to claims by the trustee against it arising from the same transaction or occurrence as the proof of claim. Section 106(c) provides for an offset against a claim by a state for any claim of the debtor or the trustee against that state. While not providing for a blanket abrogation of states' Eleventh Amendment immunity as Section 106(a) does, Sections 106(b) and (c) represent efforts by Congress to define a waiver of immunity. *Seminole Tribe* established that the parameters of waiver are constitutional; just as Congress has no power to abrogate a state's Eleventh Amendment immunity, Congress cannot determine the circumstances in which a state waives its immunity beyond constitutional parameters. As one bankruptcy court observed, "insofar as Congress undertook in [ ] §§ 106(b) and (c) to displace or to modify the meaning ascribed to the Eleventh Amendment by the courts, its endeavor must be deemed an attempted abrogation of the states' constitutional immunity."

The "same transaction or occurrence" test should be the constitutional test of waiver by a state of its Eleventh Amendment immunity. To the extent that Section 106(b) comports with this test, it is constitutional. Section 106(c), however, seeks to define waiver beyond that constitutional test, and thus is unconstitutional.

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38 For the text of 11 USC § 106(a), see note 31.
39 For the text of 11 USC § 106(b), see note 31.
40 For the text of 11 USC § 106(c), see note 31.
41 In re NVR LP, 206 Bankr 831, 839 (Bankr E D Va 1997).
42 See Part III.B.2.
43 See In re Charter Oak Associates, 203 Bankr 17, 21-22 (Bankr D Conn 1996) (holding Section 106(c) constitutional as well). One court has found Section 106(b) unconstitutional, even while adopting the same transaction or occurrence test. In re Creative Goldsmiths of Washington, D.C., Inc, 119 F3d 1140, 1147-48 (4th Cir 1997). The court reasoned that any attempt by Congress to abrogate immunity by defining the circumstances that constitute a waiver is unconstitutional. Id. Another court has expressed a similar concern, noting that "the power to define waiver can become the functional equivalent of the power to abrogate." AER-Aerotron, Inc v Texas Department of Transportation, 104 F3d 677, 681 (4th Cir 1997) (declining to rule on the constitutionality of Section 106).
B.  *Seminole Tribe*, the Fourteenth Amendment, and Section 106

The vast majority of courts that have considered the issue since *Seminole Tribe* have found that Section 106(a) is unconstitutional because it was enacted pursuant to Article I. The only courts that have held that Section 106 constitutionally abrogates states' sovereign immunity have concluded that the Bankruptcy Code was enacted pursuant to Section 5 of the Fourteenth Amendment—which is recognized by the *Seminole Tribe* Court as a valid source of congressional power to abrogate states' Eleventh Amendment immunity.

This reasoning, however, clearly contravenes the Supreme Court's interpretation of Congress's powers under the Fourteenth Amendment. First, the Court has held that it will not impute to Congress the intent to enact legislation pursuant to its Fourteenth Amendment power absent a clear congressional statement of such intent; the Bankruptcy Code contains no such statement. Moreover, Congress does not have the constitutional power to enact the Bankruptcy Code pursuant to its Fourteenth Amendment powers. The Supreme Court has recognized that the Fourteenth Amendment does not grant Congress a plenary power, but instead grants only a power to achieve the remedial ends advanced by the Fourteenth Amendment itself, namely the eradication of discrimination. The Bankruptcy Code does not serve any such remedial goal. The fact that Article I explicitly

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“See, for example, *In re Straight*, 209 Bankr 540, 555 (D Wyo 1997) (concluding that application of the Fourteenth Amendment to Section 106 renders it constitutional, but noting the need for clarification from higher courts); *In re Headrick*, 200 Bankr 963, 967 (Bankr S D Ga 1996) (“Article I gives Congress the power to legislate on the subject of bankruptcy, and the Fourteenth Amendment allows debtors to enforce the provisions of the Bankruptcy Code in federal court notwithstanding the States' Eleventh Amendment immunity.”).


“See *Pennhurst State School and Hospital v Halderman*, 451 US 1, 16 (1981), reaaff, 465 US 89 (1984) (stating that, absent a plain statement, “we should not . . . attribute to Congress an unstated intent to act under its authority to enforce the Fourteenth Amendment”).

“See *City of Boerne v Flores*, 117 S Ct 2157, 2167-68 (1997) (“Any suggestion that Congress has a substantive, non-remedial power under the Fourteenth Amendment is not supported by our case law.”). The Supreme Court has limited the remedial ends of the Fourteenth Amendment to “the mischief and wrong which the [A]mendment was intended to provide against.” *The Civil Rights Cases*, 109 US 3, 13 (1883), quoted in *City of Boerne*, 117 S Ct at 2170.
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confers on Congress the power to enact a bankruptcy law further undermines the contention that Congress enacted the Bankruptcy Code pursuant to Section 5 of the Fourteenth Amendment.

In short, the argument for upholding the constitutionality of the blanket abrogation of Section 106 fails to persuade. The Bankruptcy Code, of which Section 106 is a part, was undoubtedly enacted pursuant to Congress's powers under the Bankruptcy Clause of Article I. Even if Congress wanted to, it could not shore up the constitutionality of Section 106 by reenacting the Code pursuant to its powers under Section 5 of the Fourteenth Amendment. Given the constitutional invalidity of the blanket abrogation of Section 106, bankruptcy courts must employ other means of keeping states within the reach of the bankruptcy system. The next two Parts consider two doctrines that have that potential: waiver of immunity and Ex parte Young.

III. WAIVER OF ELEVENTH AMENDMENT IMMUNITY

The Supreme Court has long interpreted the Eleventh Amendment to allow states to consent to actions in federal court from which they would otherwise be immune. Such waiver mitigates to some extent Congress's inability to abrogate states' immunity. There are two types of waiver: explicit and constructive.

A. Explicit Waiver

A state may waive its Eleventh Amendment immunity by expressly agreeing to be sued in federal court. The Supreme Court has held that "[t]he test for determining whether a State has waived its immunity from federal-court jurisdiction is a

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49 US Const, Art I, § 8, cl 4.

50 For a more extended discussion of the arguments for and against the contention that Congress enacted the Bankruptcy Code pursuant to the Fourteenth Amendment, see In re Creative Goldsmiths, 119 F3d at 1145-47 (concluding that Congress did not enact the Bankruptcy Code pursuant to the Fourteenth Amendment); In re NVR, 206 Bankr at 839-43 (same).

51 See, for example, Atascadero State Hospital v Scanlon, 473 US 234, 238 (1985); Clark v Barnard, 108 US 436, 447 (1883).

52 As a prerequisite to finding that a state has waived its immunity, a court must determine whether the state official who took such actions had the authority to waive the Eleventh Amendment immunity of the state, a finding that depends on state law. See, for example, Ford Motor Co, 323 US at 467 (holding that state law did not authorize waiving immunity on a case by case basis); Maine Association of Interdependent Neighborhoods v Petit, 659 F Supp 1309, 1315 (D Me 1987) (holding that waiver is ineffective if the state officer is not authorized to waive immunity). See Mark Browning, Who Can Waive State Immunity?, 15 Am Bankr Inst J 10 (1997), for a discussion of how to determine the authority of state officials to waive.
stringent one.\textsuperscript{53} Courts will find an explicit waiver only where the state has stated its intent to waive "by the most express language or by such overwhelming implication from the text as [will] leave no room for any other reasonable construction."\textsuperscript{54} For example, a state may waive its Eleventh Amendment immunity with respect to certain claims by so providing in its Constitution, a statute,\textsuperscript{55} or a contract.\textsuperscript{56} However, a state does not waive its Eleventh Amendment immunity merely by receiving federal funds under a federal statute\textsuperscript{57} or agreeing to be bound by the requirements of the federal Medicaid Act.\textsuperscript{58} As Professor Erwin Chemerinsky has observed, "the Supreme Court's test is so stringent that it is quite unlikely that very many explicit state waivers of Eleventh Amendment immunity will be found.\textsuperscript{59}

B. Constructive Waiver

In addition to explicitly waiving its Eleventh Amendment immunity, a state may waive its immunity constructively. The Supreme Court has not yet comprehensively defined the requirements and boundaries of constructive waiver in the bankruptcy context, but some guidance is provided by \textit{Gardner v New Jersey}.\textsuperscript{60} In \textit{Gardner}, the Supreme Court held that when a state files a proof of claim against a debtor,\textsuperscript{61} the state waives any immunity it may have had with respect to adjudication of that particular claim—that is, any defensive counterclaim by the debtor.\textsuperscript{62} The Court reasoned that "[i]f the claimant is a State, the procedure of


\textsuperscript{55} However, a statute or constitutional provision authorizing the state to be sued in "any court of competent jurisdiction" does not constitute a waiver of Eleventh Amendment immunity. See \textit{Kennecott Copper Corp v State Tax Commission}, 327 US 573, 578-80 (1946). Nor does a provision evidencing the state's consent to be sued in its state courts indicate Eleventh Amendment waiver. See \textit{Florida Department of Health and Rehabilitation Services v Florida Nursing Home Association}, 450 US 147, 149-50 (1981).

\textsuperscript{56} See \textit{Petty v Tennessee-Missouri Bridge Commission}, 359 US 275, 281-82 (1959) (holding that provision in compact between two states allowing the bi-state commission to sue and be sued in its own name constitute a waiver by the commission).

\textsuperscript{57} See \textit{Atascadero}, 473 US at 246-47 (involving the Rehabilitation Act of 1973).

\textsuperscript{58} See \textit{Florida Department}, 450 US at 149-50.

\textsuperscript{59} \textit{Erwin Chemerinsky, Federal Jurisdiction} § 7.6 at 358 (Little, Brown 1989).

\textsuperscript{60} 329 US 565 (1947).

\textsuperscript{61} Generally, an unsecured creditor must file a proof of claim with the bankruptcy court in order for the claim to be considered. FRBrP 3002(a). Generally, secured creditors do not have to file proofs of claim, as their collateral evidences their claim. FRBrP 3002 advisory committee note.

\textsuperscript{62} \textit{Gardner}, 329 US at 573-74.
proof and allowance is not transmitted into a suit against the State because the court entertains objections to the claim. The State is seeking something from the debtor. No judgment is sought against the State.\textsuperscript{63}

The Court has not, however, identified other situations in which a waiver may be found. Lower courts have used two methods for finding constructive waiver: the defensive counterclaim test of \textit{Gardner} and the same transaction or occurrence test.\textsuperscript{64} The bankruptcy policy of achieving the twin goals supports adopting the same transaction or occurrence test for identifying constructive waivers, and the test does not unduly undermine federalism concerns.

1. The defensive counterclaim test.

Some courts have adopted the defensive counterclaim test recognized by the Supreme Court in \textit{Gardner} to define the constitutional requirements of waiver.\textsuperscript{65} Under this test, bankruptcy courts have very limited jurisdiction: they may adjudicate only those claims by the trustee that relate to the adjudication of the state's claim against the bankruptcy estate. One court justified this test as "comport[ing] more with the tendency of modern Eleventh Amendment jurisprudence to disfavor finding that a broad waiver has been effected.\textsuperscript{66}

2. The same transaction or occurrence test.

The majority of courts holding the blanket abrogation provisions of Section 106 unconstitutional under \textit{Seminole Tribe} have allowed federal court jurisdiction over all claims that arise out of the same transaction or occurrence as the claim filed by the state, declining to limit the scope of the waiver to defensive counterclaims.\textsuperscript{67} This same transaction or occurrence test derives from

\textsuperscript{63} \textit{Id.} The Court also asserted that "it is traditional bankruptcy law that he who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance must abide by the consequences of that procedure." \textit{Id} at 573.

\textsuperscript{64} See, for example, \textit{In re NVR}, 206 Bankr at 851 (adopting the defensive counterclaim test); \textit{In re Creative Goldsmiths}, 119 F3d at 1148 (adopting the same transaction or occurrence test).

\textsuperscript{65} See, for example, \textit{In re C.J. Rogers, Inc}, 212 Bankr 265, 274-75 (E D Mich 1997); \textit{In re NVR}, 206 Bankr at 851.

\textsuperscript{66} \textit{In re NVR}, 206 Bankr at 851.

\textsuperscript{67} See \textit{In re Creative Goldsmiths}, 119 F3d at 1148 (holding that the state has waived immunity with respect to any claim filed in response to a state's proof of claim that amounts to a compulsory counterclaim); \textit{In re Koehler}, 204 Bankr 210, 221 (Bankr D Minn 1997). Courts that have found Section 106(b) constitutional also use the same transaction or occurrence test, but they have relied on the statutory text and have not considered con-
Federal Rule of Civil Procedure 13(a), which defines the scope of compulsory counterclaims—those claims that a party must assert in the pending action.68

Courts outside of the bankruptcy context generally interpret the test "liberally."69 In determining whether the claim arose out of the same transaction or occurrence, courts use the "logical relation" standard.70 When this standard is applied in the bankruptcy context, jurisdiction exists over claims that have a logical relation to the subject matter of the proof of claim filed by the state.71 For example, a proof of claim filed by the state department of revenue for collection of taxes from the debtor is logically related to a claim by the trustee that the state violated the automatic stay to collect these taxes. The proof of claim is not logically related, however, to a claim by the trustee for reimbursement from the state department of health for Medicare services provided by the debtor. The latter claim involves a different state party and a different set of events than the proof of claim.

The distinction between the defensive counterclaim test and the same transaction or occurrence test, which may appear insignificant, proves dispositive in some cases. For example, in In re Lazar,72 California filed a proof of claim for unpaid taxes, a portion of which related to taxes payable to the Underground Storage Tank Cleanup Fund. The fund used taxes it collected to reimburse owners of underground storage tanks for costs of cleaning up any leaks. The bankruptcy trustee brought an action in bankruptcy court to litigate the denial of claims by the debtors for reimbursement from the fund, which were made prior to the bankruptcy filing. The court, applying the same transaction or occurrence test, found a logical relationship between the proof of claim for unpaid taxes for the fund and the trustee’s action against the fund, and accordingly held that California had waived its Eleventh Amendment immunity with respect to the trustee’s action.73 In contrast, if the court had applied the defensive counterclaim test, it would not have allowed the trustee’s action be-

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68 FRCP 13(a) provides: “A pleading shall state as a counterclaim any claim which at the time of serving the pleading the pleader has against any opposing party, if it arises out of the transaction or occurrence that is the subject matter of the opposing party’s claim . . . .”


70 Id at 65.

71 See, for example, In re Lazar, 200 Bankr at 378.

72 200 Bankr 358, 364 (Bankr C D Cal 1996).

73 Id at 364-66, 379.
cause adjudication of the claim for unpaid taxes did not require consideration of the trustee’s claim against the fund for payments owed to the debtors. The court could have determined what taxes were owed to the fund without deciding whether payments for pre-bankruptcy environmental cleanup were due to the bankruptcy estate. Indeed, this result illustrates the potential unfairness of the defensive counterclaim test: California could consent to jurisdiction to get its share of the bankruptcy estate, but could deny the court jurisdiction over it to determine if it owed money to the estate. As a result, California could receive a disproportionate share of the estate, harming other creditors.

3. Justification for adoption of the same transaction or occurrence test.

Courts should adopt the same transaction or occurrence test to identify constructive waiver. This test is superior to the defensive counterclaim test because it better serves important policy goals of the bankruptcy system while still respecting the federalism concerns underlying the Eleventh Amendment.

First, the same transaction or occurrence test is consistent with Supreme Court jurisprudence. The Gardner Court held that the defensive counterclaim rule was constitutional, but did not foreclose the possibility that a broader test may be constitutional. Indeed, the same transaction or occurrence test satisfies a primary concern animating the Seminole Tribe decision: when a state files a proof of claim, there is little need for concern regarding the “indignity of subjecting a State to the coercive process of judicial tribunals at the instance of private parties.” The test respects a state’s desire not to participate in federal court proceedings, while also limiting a state’s exposure to such proceedings to when it does decide to participate.

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71 329 US at 574.


73 Some courts have found that the filing of a proof of claim by one state agency constitutes a waiver of Eleventh Amendment immunity for all state agencies. See, for example, In re Hughes-Bechtol, Inc, 124 Bankr 1007, 1018 (Bankr S D Ohio 1991). See also NJ Dept Environ Protection v Gloucester Environ Mgmt Services, Inc, 923 F Supp 651, 664 (D NJ 1995) (involving nonbankruptcy action). While serving policy goals of bankruptcy by allowing the adjudication of all claims in the bankruptcy court, this holding fails to strike an appropriate balance between such policy goals and broader federalism concerns. A claim by one state agency will not necessarily put a wholly unrelated state agency on notice that its Eleventh Amendment immunity may have been waived. This raises Seminole Tribe’s concern about the “indignity” of subjecting a state to suit, and ignores the Supreme Court’s reluctance to find a waiver of immunity. Application of the same transaction or oc-
Second, the same transaction or occurrence test will facilitate the adjudication of all claims and obligations of the debtor in one forum, the bankruptcy court. Both efficiency concerns (resolving all disputes in one forum) and fairness concerns (ensuring that all creditors receive an equitable distribution) suggest the desirability of adjudicating as many claims as constitutionally permissible in the bankruptcy court.

The facts of In re C.J. Rogers, Inc illustrate both the federalism and policy justifications for the same transaction or occurrence test. The Michigan Employment Security Agency ("MESA") received, as an alleged preferential transfer, money from the debtor's bank account to pay outstanding taxes. When the debtor entered bankruptcy court, MESA filed proofs of claim for additional amounts owed. The trustee subsequently filed suit against MESA, challenging the validity of the lien pursuant to which MESA recovered the money from the debtor's bank account. Applying the defensive counterclaim test, the court held that it lacked jurisdiction over MESA to adjudicate the trustee's claim. This result seems unfair, for MESA consented to jurisdiction to recover additional monies owed to it, but was able to take advantage of its immunity to retain a potentially preferential transfer. The lack of jurisdiction thus allowed MESA to receive a disproportionate amount of the debtor's assets. The same transaction or occurrence test would have allowed the bankruptcy trustee to recover the preferential transfer and distribute it to the rest of the creditors—a more equitable result that would also have increased the assets of the bankruptcy estate.

4. Liberal application of same transaction or occurrence test.

Bankruptcy courts should interpret the same transaction or occurrence liberally in bankruptcy proceedings, as courts do in
the Federal Rule of Civil Procedure 13(a) context,\(^1\) "to facilitate the adjustment of all obligations of a debtor in one forum."\(^2\) As courts have recognized in the Federal Rule of Civil Procedure 13(a) context, there is no technical definition of what constitutes the same transaction or occurrence.\(^3\) Because of this lack of precision, the courts in applying the test should balance the federalism concerns underlying *Seminole Tribe* and the twin goals of the bankruptcy system: maximization and equitable distribution of the assets of the bankruptcy estate and a fresh start for the debtor.

With respect to federalism, if the state agency against whom the debtor's claim is asserted filed a proof of claim, there is less concern over the "indignity" of subjecting it to the jurisdiction of the bankruptcy court; the state has already consented to—has even requested—federal jurisdiction. However, if the debtor's claim involves an entirely separate state agency than the one filing the proof of claim, the court should be more careful in finding that jurisdiction exists, because that agency has not consented to jurisdiction. In this situation, the courts should consider the relationship between the two agencies. For example, if the state department of revenue files a proof of claim for unpaid taxes, and the trustee seeks to assert a claim against the state department of health services for payment for services rendered, no relationship between the agencies seems to exist, so federalism concerns militate against jurisdiction. On the other hand, the situation is different if the state department of revenue agrees to collect revenue and also makes payments on behalf of the state department of health services. In that case, a trustee should be allowed to bring a suit against the department of health services if it relates to a proof of claim filed by the department of revenue. The relationship between the agencies should put each on notice of claims filed by the others relating to their agreement—and so federalism concerns are respected.

On the policy side, courts should consider the importance of adjudicating the debtor's claim in the bankruptcy court. When application of the same transaction or occurrence test does not yield clear results, the courts should examine the availability of other avenues of relief for the debtor and the relative importance of the claim to the bankruptcy estate. For example, if adjudication of a trustee's claim against a state would only minimally

\(^1\) See Wright, Miller, and Kane, *Federal Practice* § 1410 at 50 (cited in note 69).
\(^2\) *In re Lazar*, 200 Bankr at 379.
\(^3\) See Wright, Miller, and Kane, *Federal Practice* § 1410 at 52 (cited in note 69).
augment the bankruptcy estate, or if the trustee could at low cost adjudicate his claim in another forum such as state court, bankruptcy courts should be more hesitant before asserting jurisdiction.

A liberal application of the same transaction or occurrence test would have resulted in a different outcome in *In re Creative Goldsmiths of Washington, D.C., Inc.* There, the bankruptcy trustee sued the Maryland comptroller, seeking to avoid as a preferential transfer the debtor's payment of income taxes to the state. Maryland filed a proof of claim for sales and withholding taxes, but not for the income taxes. The court held that the action to recover the preferentially paid income taxes did not arise out of the same transaction or occurrence as the payment of sales and withholding taxes, and so denied jurisdiction over the trustee's preference action. This result allowed the comptroller to retain the preferential transfer by avoiding the jurisdiction of the court, while seeking the jurisdiction of the same court to recover assets from the bankruptcy estate. The state became in effect a preferred creditor. A more liberal application of the same transaction or occurrence test, however, would lead to the opposite result. The court could have viewed the payment of income taxes to Maryland as logically related to Maryland's claim for sales and withholding taxes on the ground that both represent the obligation of the debtor to pay taxes relating to its business to the state. Moreover, both involve the comptroller of Maryland; because the comptroller agreed to the court's jurisdiction by filing a proof of claim, there is less intrusion on federalism concerns in deeming a waiver to have occurred. On the other hand, if Maryland's proof of claim related to a contract with the debtor for Medicaid services, there would be no logical relationship between that proof of claim and a refund of income taxes paid. Under the same transaction or occurrence test, the court would not have jurisdiction over such a claim.

In short, the doctrine of waiver of Eleventh Amendment immunity—especially under the same transaction or occurrence test—provides a foothold for the efforts of bankruptcy trustees and courts to assert authority over states in the bankruptcy process, while also respecting federalism concerns. The waiver doctrine is unavailable if the state does not file a proof of claim; moreover, even if the state does file a proof of claim, the same

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84 119 F3d 1140 (4th Cir 1997).
85 Id at 1143.
86 Id at 1149.
transaction or occurrence test will not always be satisfied. The next Part thus examines additional tools by which bankruptcy courts can bring states into a bankruptcy proceeding, including the *Ex parte Young* doctrine.

IV. HOW COURTS SHOULD ADDRESS POTENTIAL OBSTACLES PRESENTED BY SEMINOLE TRIBE

Debtors often seek to assert claims against a state in situations where the state has not filed a proof of claim or otherwise waived its Eleventh Amendment immunity. This Part discusses the options available to bankruptcy courts in four such scenarios: (1) state attempts to collect debts after discharge by the bankruptcy court; (2) violation by the state of the automatic stay; (3) the state's refusal to turn over preferential or fraudulent conveyances; and (4) claims for monetary recovery by the debtor against the state. These four scenarios represent instances where the *Seminole Tribe* holding may pose a serious threat to the bankruptcy process. However, because bankruptcy courts have a variety of tools with which to enjoin violations of the Bankruptcy Code, *Seminole Tribe* does not in fact pose a serious threat to the bankruptcy regime. The only conceivable area in which the debtor has no recourse against the state is when the state has received property of the debtor through preferential transfers. This does not pose a serious threat to the bankruptcy process because it is unlikely that states have the resources or information to accelerate aggressively their debt collection practices with respect to potential bankrupts.

A. Attempts by States to Collect Debts After Discharge

Even when a state has a claim against a debtor, it may choose not to file a proof of claim in order to retain its Eleventh Amendment immunity. In several such cases, states have attempted to collect payment from debtors after the bankruptcy court has discharged the debts.\(^7\) These attempts by state officials clearly violate federal law and thus can be enjoined by the bankruptcy court through the *Ex parte Young* doctrine.

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\(^7\) The Bankruptcy Code provides only for discharge of debts owed by individuals, not corporations. See note 5.
1. Enforceability of discharge orders.

Bankruptcy courts have the power to, among other things, determine the amount or legality of any tax, and discharge any debts, including debts owed to a state. The court’s discharge operates as an injunction against judicial proceedings and nonjudicial collection attempts relating to discharged debts. While resolution of an adversary proceeding against a state depends on the court’s jurisdiction over the state, the power of the bankruptcy court to discharge debts derives not from jurisdiction over the state or other creditors. Instead, the power derives from jurisdiction over debtors and their estates as established by the Bankruptcy Code. The state may choose not to appear in federal court, but that choice carries with it the consequence of foregoing any challenge to the federal court’s actions. Indeed, as the Fourth Circuit has observed, a confirmation order entered by a bankruptcy judge is not a “suit” against one of the United States for purposes of the Eleventh Amendment. In this sense, a discharge order is distinguishable from an adversary proceeding by the trustee against a state, in which the state is the named defendant. The latter action certainly constitutes a “suit in law or equity, commenced or prosecuted against one of the United States” under the Eleventh Amendment, over which federal courts lack jurisdiction absent waiver by the state. On the other hand, a discharge by the bankruptcy court operates as an injunction against any actions taken to recover discharged debts, and cannot be ignored by state actors.

2. Use of Ex parte Young to enforce discharge orders.

Bankruptcy courts have the power to enter bankruptcy plan confirmation orders under Section 105(a), provide for the discharge of debts, and issue any order necessary or appropriate to

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68 11 USC § 505(a)(1) (1994). See also Hoffman v Connecticut Department of Income Maintenance, 492 US 96, 102 (1989) (noting in dicta that the bankruptcy court’s determination of the amount or legality of any tax under 11 USC § 505(a)(1) should bind all government units).
69 The Bankruptcy Code provisions relating to discharge are 11 USC §§ 727, 1141, 1228(a)-(b), 1328(b) (1994).
70 11 USC § 524(a) (1994).
71 See Maryland v Antonelli Creditors’ Liquidating Trust, 123 F3d 777, 787 (4th Cir 1997) (finding that the bankruptcy court had authority to issue an order exempting certain transfers from state taxes).
72 Id.
73 Id at 786-87.
74 US Const, Amend XI.
75 See 11 USC § 524(a)(2).
carry out the provisions of the Bankruptcy Code. However, bankruptcy courts cannot practically enforce those orders without a mechanism to obtain jurisdiction over the state. The Ex parte Young doctrine provides such a tool. Because an attempt to collect a discharged debt violates the injunction established by the discharge under federal law, courts can employ the Ex parte Young doctrine to obtain the necessary jurisdiction over the state official. Moreover, once a court issues an order enjoining a state official from violating the discharge order under Ex parte Young, it can enforce that order with its normal contempt powers, because jurisdiction over the state official has already been established.

Despite the availability of the Ex parte Young doctrine to enjoin violations of the bankruptcy court's orders, at least one bankruptcy court has not found it proper to assert jurisdiction in such scenarios. In In re Kish, the debtor re-opened her bankruptcy case to determine the status of a debt that the Division of Motor Vehicles ("DMV"), a state agency, was seeking to collect after it had been discharged by the bankruptcy court. The debtor named both the DMV and its director in her action. The bankruptcy court found that it had no jurisdiction over the DMV to enforce the discharge order because the DMV, a state agency that was the real party in interest, would be harmed by such enforcement. The court did not explicitly discuss the Ex parte Young doctrine.

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96 11 USC § 105(a) (1994). Similarly, federal courts can invalidate any state laws that conflict with the provisions of the Bankruptcy Code. In Perez v Campbell, 402 US 637, 639-42, 652 (1971), for example, the Supreme Court struck down an Arizona statute providing that a bankruptcy discharge did not affect a driver's duty to repay damages from an auto accident. The Court enunciated "the controlling principle that any state legislation which frustrates the full effectiveness of federal law is rendered invalid by the Supremacy Clause." Id at 652.

97 See In re Jacksen, 105 Bankr 542, 544 (9th Cir Bankr App Panel 1989) (holding that 11 USC § 105(a) empowers the bankruptcy court to issue an injunction against attempts to collect a judgment relating to a discharged debt, but does not broaden the court's jurisdiction over parties, which must be established separately).

98 11 USC § 524(a)(2).

99 See text accompanying notes 28-30.

100 212 Bankr 808 (D NJ 1997).

101 Id at 814. The judge relied on Regents of the University of California v Doe, 117 S Ct 900, 904-05 (1997), for the proposition that "the relevant inquiry for Eleventh Amendment purposes is whether a state's potential legal rights are affected [by the action]." 212 Bankr at 814 n 5. Because the discharge of a debt would have an impact on the state's legal rights, the judge found he did not have jurisdiction to enforce such a discharge. Id at 814. The court's reliance on Doe is misplaced: Doe did not involve an Ex parte Young action, but rather addressed whether the indemnification of a state agency by someone other than the state precluded consideration of the agency as an arm of the state for Eleventh Amendment purposes. Doe, 117 S Ct at 904. Thus, Doe does not change Ex parte Young's central
The better view is that the *Ex parte Young* doctrine provides courts with jurisdiction to enforce discharge orders. To hold otherwise would, as Justice Brennan has noted, "exempt[t]... States from compliance with laws that bind every other legal actor in our Nation." Moreover, the Supreme Court has observed that "[o]ne of the primary purposes of the Bankruptcy Act" is to give debtors "a new opportunity in life and a clear field for future effort, unhampered by the pressure and discouragement of pre-existing debt." This purpose would be undermined if states were not bound to the bankruptcy court's discharge of debts.

While bankruptcy courts may not entertain adversary suits against states, they may enter orders that states must obey—for example, discharging debts or exempting certain transfers from state tax. Indeed, because states will be held to the discharge plan approved by the bankruptcy court, this principle may encourage states to file proofs of claim in the bankruptcy proceeding in order to protect their rights. Such a result would mitigate the negative effects of the *Seminole Tribe* decision on bankruptcy proceedings.

**B. Violations of the Automatic Stay**

The automatic stay provision of the Bankruptcy Code is an essential element of the bankruptcy process, preventing creditors from pursuing their claims against the debtor once a bankruptcy petition has been filed. In addition to barring creditors from seeking to collect debts and suspending judicial, administrative,

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premise that prospective injunctive relief may be awarded against state officials.

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11 USC § 362(a)(6).

**Atascadero**, 473 US at 248 (Brennan dissenting).

192 *Local Loan Co v Hunt*, 292 US 234, 244 (1934) (citations omitted).

104 The discussion in this Part is equally applicable to claims under 11 USC § 525 (1994), which prohibits discrimination against a person or entity merely because it is or has been in bankruptcy or a debtor under the Bankruptcy Code. Just as a violation of the automatic stay constitutes a violation of federal law, so does discriminating against a debtor.

105 11 USC § 362. The court has the authority to grant a party relief from the stay in certain circumstances. 11 USC § 362(d), (f).

106 Congress explained its importance as follows:

The automatic stay is one of the fundamental debtor protections provided by the bankruptcy laws. It gives the debtor a breathing spell from his creditors. It stops all collection efforts, all harassment, and all foreclosure actions. It permits the debtor to attempt a repayment or reorganization plan, or simply to be relieved of the financial pressures that drove him into bankruptcy.


107 11 USC § 362(a)(6).
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and other proceedings against the debtor,\textsuperscript{108} the automatic stay prevents creditors from offsetting money they owe to the debtor against money the debtor owes to them without leave of the court.\textsuperscript{109} The filing of a voluntary or involuntary petition under any chapter of the Bankruptcy Code automatically triggers the stay. The stay remains in place until the property against which a claim is being asserted is no longer property of the estate,\textsuperscript{110} the case is closed, the case is dismissed, or a discharge is granted or denied, whichever comes first.\textsuperscript{111} Section 362(a) provides that the automatic stay applies to all entities, which Congress has defined to include states.\textsuperscript{112} Section 362(h) provides, upon violation of the stay, for the recovery of "actual damages, including costs and attorneys' fees, and, in appropriate circumstances, punitive damages."\textsuperscript{113}

As one commentator has noted, "[t]he operation of the automatic stay and ultimately the policies of fair distribution and a debtor's fresh start are obviated if a state entity may routinely violate the automatic stay and in effect enjoy a preferential status in comparison to other creditors by not filing a proof of claim."\textsuperscript{114} If bankruptcy courts could not obtain jurisdiction over states violating the automatic stay, inequality in the treatment of creditors would result in cases in which states collect from the debtor outside of the bankruptcy process.

1. Use of \textit{Ex parte Young} to enjoin violations of the automatic stay.

Like a bankruptcy court's order discharging debts, the automatic stay is an injunction. Debtors and bankruptcy trustees can bring \textit{Ex parte Young} actions against the state official violating the stay to obtain the necessary jurisdiction over the state official to enjoin the violation. Because under \textit{Ex parte Young} plaintiffs are entitled to only prospective injunctive relief, they cannot recover damages.\textsuperscript{115} They may, however, recover attorneys' fees.\textsuperscript{116}

\begin{itemize}
\item \textsuperscript{108} 11 USC § 362(a)(1).
\item \textsuperscript{109} 11 USC § 362(a)(7).
\item \textsuperscript{110} 11 USC § 362(c)(1).
\item \textsuperscript{111} 11 USC § 362(c)(2).
\item \textsuperscript{112} 11 USC § 101(15) defines "entity" to include any "governmental unit." 11 USC § 101(27) defines "governmental unit" to include "a State."
\item \textsuperscript{113} 11 USC § 362(h).
\item \textsuperscript{114} Ron S. Chun, \textit{Avoiding a Jurassic Dinosaur Run Amok: Circumventing Eleventh Amendment Sovereign Immunity to Remedy Violations of the Automatic Stay}, 98 Comm L J 179, 180 (1993).
\item \textsuperscript{115} See Part I.B. See also \textit{In re Louis; Harris}, 213 Bankr 796, 798 (Bankr D Conn 1997) (recognizing that only prospective injunctive relief is available under \textit{Ex parte Young}).
\end{itemize}
Bankruptcy courts may enforce their orders; if a state official violates the injunction issued by the court in the *Ex parte Young* action, a court may award damages against him for contempt regarding the court-ordered injunction (as distinguished from damages for the initial violation of the automatic stay, which are not allowed).\(^{117}\)

While some bankruptcy courts have enjoined state officials from violating the automatic stay,\(^{118}\) another court has asserted that it is powerless to enjoin the violation.\(^{119}\) This court did not address the applicability of *Ex parte Young* to state violations of the automatic stay; instead it simply asserted that jurisdiction does not exist in light of *Seminole Tribe*.\(^{120}\) As discussed above, *Ex parte Young* remains a viable means of obtaining jurisdiction over a state official to enjoin a violation of federal law.

2. Incentives for states to violate the automatic stay.

While an *Ex parte Young* action can be maintained to enjoin state officials from violating the automatic stay, the *Ex parte Young* doctrine's preclusion of a damage award creates a perverse incentive for states to violate the automatic stay. Under the current *Ex parte Young* doctrine, even if the trustee brings an action against a state official, the worst penalty a federal court can levy is an injunction and attorneys' fees; the state official is immune from paying damages. In the meantime, if the state (acting through the state official) can collect the debt during the automatic stay, it does not have to turn over the property to the bankruptcy trustee.\(^{121}\)

However, it is unlikely that states will become rogue creditors who use their Eleventh Amendment immunity to extract aggressively every last penny of their claims from the debtor. Even if states violate the automatic stay, debtors and trustees can stop these violations early through the *Ex parte Young* doctrine, thereby reducing the benefit to the state of violating the automatic stay in the first place. Moreover, active employment of the

\(^{118}\) See id at 799.

\(^{117}\) See the discussion of enforcement of *Ex parte Young* orders in Part I.B.

\(^{118}\) See *In re Guiding Light Corp*, 213 Bankr 489, 492 (Bankr E D La 1997) (allowing an *Ex parte Young* action seeking to enjoin the Louisiana Department of Health and Human Services to proceed); *In re Martinez*, 196 Bankr at 229-30 (disallowing monetary damages against the Department of the Treasury of the Commonwealth of Puerto Rico).

\(^{119}\) See *In re Lush Lawns, Inc*, 203 Bankr 418, 420-21 (Bankr N D Ohio 1996) (finding enjoinment to be a contempt proceeding, not an *Ex parte Young* action, and so declining to find jurisdiction).

\(^{120}\) Id at 421.

\(^{121}\) See Part IV.C.
Ex parte Young doctrine may discourage states from invoking Eleventh Amendment immunity in the first place, because the consequence could be litigation against state officials. Where the state has indemnified the state official, it will have to pay the costs of the ensuing litigation, providing a further disincentive to violating the automatic stay.

C. Turnover of Property Obtained by the State

An issue related to enjoining violations of the automatic stay involves the bankruptcy court's ability to require that a state return to the estate property held in violation of the bankruptcy laws. Two specific instances deserve attention: property received by the state in a preferential transfer and property received by the state in a fraudulent conveyance.

The Bankruptcy Code provides that conveyances made within ninety days of the filing of a bankruptcy petition, termed "preferential transfers," must generally be returned to the bankruptcy trustee. Similarly, transfers made by the debtor with an intent to defraud or made for less than fair value ("fraudulent conveyances") must also be turned over to the trustee. These provisions are designed to ensure that all creditors receive their fair share of the bankruptcy estate. Allowing the state to retain such transfers would reduce the assets available to other creditors, thus compromising the goals of equitable treatment of all creditors and maximization of the assets of the bankruptcy estate. Allowing retention may also create incentives for states to accelerate their collection processes. Unfortunately, while bankruptcy policy concerns support forcing turnover of the property,

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122 See In re Lazar, 200 Bankr at 383 ("The principal effect of the Seminole decision, in the bankruptcy context, may be to convert litigation against a state . . . into litigation against the applicable state officers.").

123 The analysis in this Part also applies to transfers made in violation of the automatic stay. Such transfers are unlikely to occur, however, because once the debtor enters bankruptcy, the trustee controls the assets of the bankruptcy estate. The trustee, aware of his rights under the Bankruptcy Code, will not consent to such transfers and can bring an Ex parte Young action to enjoin any state collection efforts.


125 11 USC §§ 548, 550. While the more common case will involve preferential transfers, fraudulent conveyances to states may also arise. For example, in United States v Nordic Village, Inc, 503 US 30, 31 (1992), a case involving federal sovereign immunity, an officer of a bankrupt corporation withdrew money from its account to pay his own federal tax liability. The Court refused to permit the bankruptcy court jurisdiction over the Internal Revenue Service to recover the fraudulent transfer, on the grounds that the Bankruptcy Code did not "establish unambiguously" that Congress intended to abrogate sovereign immunity with respect to monetary claims. Id at 34.
Ex parte Young's requirement that relief be only prospective precludes bankruptcy courts from using Ex parte Young to obtain jurisdiction over the state to force the turnover of the property. An exception to this rule exists where the state does not hold clear title to the property—for example, property seized pursuant to a lien, but not yet sold.

1. Use of Ex parte Young to achieve turnover.

In order to avoid the inequitable results described above, courts could characterize return of the property as prospective relief for purposes of the Ex parte Young doctrine on the ground that only through such return could the compliance with federal law be restored. Under this view, because the state in holding the property affects the distribution of assets into the future, the relevant state official is in continuing violation of the Bankruptcy Code. Remedyng this violation would require turnover of the property.

While such a conception would best serve the goals of the bankruptcy process, it runs afoul of the Supreme Court's conception of "prospective relief" in Ex parte Young actions. In Ford Motor Co v Department of Treasury of Indiana, the Court established that "when the action is in essence one for the recovery of money from the state, the state is the real, substantial party in interest and is entitled to invoke its sovereign immunity from suit even though individual officers are nominal defendants." Similarly, in Edelman v Jordan, the Supreme Court held that payment of benefits withheld from citizens in violation of federal law did not need to be paid retroactively to the citizens. The Court reasoned that, because the funds to satisfy the award must come from the state treasury, such payment resembled more closely the monetary relief against the state prohibited by Ford than the prospective relief in Ex parte Young. Similarly, because the return of property obtained by a state in violation of the Bankruptcy Code must come from the state treasury, the Ex parte Young doctrine cannot be used to force turnover.

One might argue that the bankruptcy situation is distinguishable from Edelman on the ground that the property involved once belonged to the debtor and was kept in violation of federal law, while the denied benefits in Edelman were never the prop-

129 For a similar argument, see In re Colon, 114 Bankr at 897.
129 Id at 665-66 & n 11.
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Property of the citizens. Such a distinction is not tenable, however, as turnover in both situations requires payment from the state treasury, which the *Ex parte Young* doctrine forbids.

One particular bankruptcy situation is distinguishable from *Edelman*: turnover of property seized by the state to which the state does not have title. In *United States v Whiting Pools, Inc*, the Supreme Court allowed the bankruptcy trustee to recover tangible personal property seized by the Internal Revenue Service ("IRS"). In authorizing the turnover, the Court emphasized that the IRS did not have title to the property, but rather held a lien on the property.

Similarly, in *In re Mt. Moriah Elevator, Inc*, the bankruptcy court allowed the trustee to recover property of the estate that the state was holding in an escrow account. The court stressed that the money was not being paid from the state treasury.

Therefore, if the state does not have title to the seized property, the judge can order its turnover.

Some lower courts, relying primarily on policy reasons, have asserted jurisdiction over states to require them to turn over property held by the state under the bankruptcy laws. One court, ordering the return of property obtained in violation of the automatic stay, justified its order by noting that:

"The return of [funds recovered by the State in violation of the automatic stay] to the estate is essential if the fundamental bankruptcy principles embodied in the automatic stay (i.e. debtor relief and creditor equality) are to have meaning. . . . The return of such funds is not merely compensatory to the debtor; it also restores compliance with federal law and vindicates the bankruptcy stay."
Yet, while use of the *Ex parte Young* doctrine to mandate turnover of property would best serve the policies of bankruptcy, such considerations cannot outweigh the constitutional limitations established by the Supreme Court. The Court has repeatedly made clear its requirement that relief in *Ex parte Young* actions be prospective only. The return of property obtained in violation of the Bankruptcy Code cannot be termed “prospective relief” apart from the *Whiting Pools* scenario, and therefore cannot be distinguished from the Supreme Court’s refusal in *Edelman* to award retroactive benefits withheld in violation of federal law. While the result may be that states receive a disproportionate share of the bankruptcy assets relative to other unsecured creditors—a result that undermines one of the bankruptcy regime’s twin goals—it is dictated by the jurisdictional requirements of the Eleventh Amendment as interpreted by the Supreme Court.

2. Incentives for states to obtain preferential transfers.

Given the limited usefulness of the *Ex parte Young* doctrine in this context, states may take advantage of the situation by trying to obtain preferential transfers from the debtor. Creditors must generally turn over to the bankruptcy estate all transfers received from the debtor within ninety days of the filing of the bankruptcy petition. The incentives for states to collect such preferential transfers are unclear in light of bankruptcy courts’ inability to force turnover. On the one hand, states may have an incentive to accelerate their collection practices. As the Seventh Circuit explained in *In re McVey Trucking, Inc.*

If the federal courts were not able to order a state to turn over assets to a bankruptcy estate, then any state owed money by a debtor having financial problems would have a strong incentive to collect whatever funds it believed to be due as rapidly as possible—even if this pushed the debtor into insolvency—rather than risking the possibility of recovering only a portion of their debt in any subsequent bankruptcy proceeding. In effect, we would be holding that the Constitution makes a state a preferred creditor in every bankruptcy. The very existence of this power would doubtless encourage other creditors to accelerate their collections. The end result would be an increase in bankruptcies and a

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118 See text accompanying notes 24-25.
119 11 USC §§ 347(b)(4)(A), 550(a).
120 812 F2d 311 (7th Cir 1987).
distortion of the system of preferences that Congress has carefully crafted.\textsuperscript{139}

On the other hand, it is unclear whether state agencies will have either the information necessary to identify individuals and corporations that pose a bankruptcy risk, or the tools to seek to collect aggressively as much money as possible prior to their filing of a bankruptcy petition. Perhaps states will undertake accelerated collection with respect to individuals or corporations that have large liabilities; however, these groups are likely to be more sophisticated and aware of their option to refuse to pay. If, however, states in practice accelerate their collection practices post-\textit{Seminole Tribe}, other creditors' incentives could be altered in two ways. First, if creditors perceive that preferential transfers to states diminish assets available to them in bankruptcy proceedings, they can charge higher interest rates or alter other credit terms ex ante to compensate for this risk. Ex post, if a creditor thinks that the debtor is about to make a payment to the state, it can attempt to force the debtor into bankruptcy before the payment is made,\textsuperscript{140} thus triggering the automatic stay, which precludes collection by the state.\textsuperscript{141} A creditor would need detailed information about the debtor's financial situation and plans to pay the state in order to take such steps.\textsuperscript{142} Ultimately, resolution of this issue is an empirical question, but this indeterminacy should alleviate concerns that states will aggressively accelerate collections as a result of \textit{Seminole Tribe}.

D. Claims by the Debtor Against the State

In the course of a bankruptcy proceeding, a debtor will often have a claim against the state. For example, in a number of cases debtors have sought refunds of overpayments to state agencies made in the ordinary course of business.\textsuperscript{143} If a state has not filed a proof of claim or otherwise waived its Eleventh Amendment

\textsuperscript{139} Id at 328.
\textsuperscript{140} The creditor could either exert pressure on the debtor to file for bankruptcy, or could force the debtor into bankruptcy pursuant to an involuntary filing. See 11 USC § 303 (1994).
\textsuperscript{141} See Part IV.B.
\textsuperscript{142} Moreover, claims by states for taxes receive priority over other claims in bankruptcy. See 11 USC § 507(a)(8) (1994). If the payment to the state involved such taxes, the creditor would not have an incentive to accelerate filing of a bankruptcy petition, because the state claim would have priority over the other creditors' claims.
\textsuperscript{143} See, for example, \textit{In re NVR}, 206 Bankr at 835 (involving refund of taxes paid); \textit{In re Charter Oak}, 203 Bankr at 19-20 (involving repayment of rent, property insurance, and property taxes relating to services rendered to the state by the debtor).
immunity, bankruptcy courts will not have jurisdiction to adjudicate such claims.

Unfortunately, from the perspective of the bankruptcy regime, there is little that the courts can do to mitigate this problem in light of Seminole Tribe. As discussed above, *Ex parte Young* actions require a violation of federal law; most of these types of claims will involve state law. Moreover, even if a violation of federal law exists, the *Ex parte Young* doctrine provides only for prospective injunctive relief, and does not allow for the return of money from the state treasury. A liberal application of the same transaction or occurrence test may be useful in obtaining jurisdiction over some of these claims, but requires first that some state agency has filed a proof of claim.

Of course, if a bankruptcy court cannot obtain jurisdiction over a state, suit with respect to these types of claims can still be brought in state court. 28 USC § 1334(b) provides the federal courts “original but not exclusive jurisdiction of all civil proceedings arising under title 11,”"144 “or arising in or related to cases under title 11.”145 However, this nonexclusivity does not fully resolve the issue. Trustees may lack the resources to bring suit in state court.146 Furthermore, adjudication of claims in state court undermines one of the primary attributes of the Bankruptcy Code: establishment of an efficient debt collection mechanism.147 To the extent the debtor is unable to obtain speedy (or any) resolution of a claim against a state in state court, creditors will have fewer assets to divide. Despite both of these problems with pursuing claims in state court, the fact remains that ultimately the trustee has an avenue for recovery in state courts to collect on these claims from the state, though perhaps with a loss of efficiency. In contrast, the trustee has no ability to force turnover of property obtained as a preferential transfer or fraudulent conveyance.

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144 Title 11 of the US Code contains the bankruptcy provisions.
145 28 USC § 1334(b) (1994).
146 See, for example, *In re Zywiczynski*, 210 Bankr at 925 (noting that the trustee had no resources to bring suit in state court, or even pay the filing fee).
147 See Douglas G. Baird and Thomas H. Jackson, *Corporate Reorganizations and the Treatment of Diverse Ownership Interests: A Comment on Adequate Protection of Secured Creditors in Bankruptcy*, 51 U Chi L Rev 97, 100-01 (1984) (asserting that the primary goal of bankruptcy is as an efficient debt collection mechanism). One scholar, however, has noted that “[t]he fact that a debtor or trustee may have to seek relief in state court is only extraordinary when viewed in the narrow bankruptcy context; in the broader context, it is perfectly consistent with the relationship between the states and the federal government.” Patricia L. Barsalou, *Defining the Limits of Federal Court Jurisdiction over States in Bankruptcy Court*, 28 St Mary's L J 575, 623 (1997). Nonetheless, the requirement that debtors bring their claims in state court impairs the efficiency of the bankruptcy process.
CONCLUSION

The Supreme Court's decision in *Seminole Tribe* has complicated the bankruptcy process by allowing states to invoke their Eleventh Amendment immunity from suit in bankruptcy courts. In some instances, this invocation of immunity threatens to undermine both the efficiency and fairness of the bankruptcy process by in effect making states preferred creditors.

Courts may employ various tools to obtain jurisdiction over states in bankruptcy courts and mitigate the negative effects of *Seminole Tribe*. In certain cases, states waive their Eleventh Amendment immunity by filing a proof of claim in the bankruptcy proceeding. Courts should liberally apply the same transaction or occurrence test to determine the scope of the waiver. Courts can also employ the *Ex parte Young* doctrine to enjoin state officials who are violating provisions of the Bankruptcy Code, such as the automatic stay or the discharge of debts.

The only area where the implications of *Seminole Tribe* leave the debtor and the trustee without any remedy against a state involves the lack of jurisdiction of bankruptcy courts over states to force turnover of property obtained in violation of the Bankruptcy Code. As a result of this inability, other creditors will have fewer assets to share. Nonetheless, this issue does not pose a serious threat to the bankruptcy process. In the preferential transfer context, states will not likely have the resources or information to accelerate aggressively debt collection from potential bankrupts. In terms of the automatic stay, the bankruptcy court can employ the *Ex parte Young* doctrine to enjoin violations before transfers occur. These considerations indicate that in this context, the state is not likely to have a significant advantage over other creditors.