THE GOLDEN SHARES DILEMMA: AN ANALYSIS OF FEDERAL COMMON LAW, FIDUCIARY DUTIES, AND THE ENFORCEABILITY OF BANKRUPTCY BLOCKING PROVISIONS IN CORPORATE CONTROL DOCUMENTS

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The COVID-19 pandemic brought unprecedented challenges to American businesses. For those businesses facing the most pressure, the American bankruptcy system promised relief and a means of emerging from the crisis. This system is driven by a historic policy of liberal access for debtors, with attempts by creditors to block bankruptcy filings under loan terms routinely nullified.

Yet the promise of bankruptcy for some debtors may prove to be illusory, thanks to a device known as the "golden share." Instead of inserting bankruptcy blocking provisions in loan documents, creditors obtained equity and established their rights to block bankruptcy filings in corporate control documents. While the only appellate court to speak directly on the issue has suggested golden shares are valid, a post-COVID-19 case from the bankruptcy court in Delaware expressed its disapproval of this device. An emerging split of authority threatens to create only more uncertainty for corporate debtors already facing significant pressures.

This Note tracks the dilemma of golden shares. It first reviews the history of golden shares, as well as the most important cases dealing with this device. It explores the theory behind the golden shares dilemma, including the role of fiduciary duties in the analysis. The Note then proceeds into a discussion of federal common law. The Note concludes with a proposal that implementing federal common law fiduciary duties through a burden-shifting framework provides the optimal means of resolving the golden shares dilemma.

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TABLE OF CONTENTS

I. INTRODUCTION 1973
II. BACKGROUND 1974
A. *Public Policy Concerns* 1975
B. *The Authority Opening* 1976
C. *History of Golden Shares* 1978
D. *Judicial Reception of Golden Shares* 1979
1. Intervention Energy 1980
2. Franchise Services 1980
3. Pace Industries 1981
E. *Current Status of Golden Shares* 1982
III. ANALYSIS 1982
A. *Fiduciary Duties and Golden Shares* 1983
B. *A History of Federal Common Law* 1986
C. *Federal Common Law Arising by Congressional Authorization* 1987
1. *Example #1: The Labor Management Relations Act (LMRA)* 1988
2. *Example #2: Employee Retirement Income Security Act (ERISA)* 1989
D. *Federal Common Law in Bankruptcy* 1990
1. *Preemption* 1991
a. Example #1: *Ipso Facto* Clauses 1993
b. Example #2: Corporate Authority to File Bankruptcy 1993
c. Example #3: Shareholder Breach of Fiduciary Duty Claims 1994
2. *Uniform Nature of Bankruptcy* 1995
3. *Legislative History* 1996
IV. RECOMMENDATION 1997
A. Starr Int'l Co. v. Fed. Reserve Bank of New York 1998
B. Texas Lottery Comm'n v. Tran 1998
C. *Federal Common Law's Role in Resolving the Golden Shares Dilemma* 1999
D. *Implementing Federal Common Law Fiduciary Duty through a Burden-Shifting Framework* 2000
V. CONCLUSION 2001

I. INTRODUCTION

Creditors have long sought creative ways to limit debtors' ability to find refuge in the bankruptcy system.[1] By giving their holders the right to prevent a voluntary bankruptcy petition, golden shares provide one mechanism by which creditors can theoretically block a bankruptcy filing.[2] Standing in the way of golden shares' effective implementation is the longstanding public policy of liberal access to bankruptcy relief, as reflected in the courts' frequent invalidation of attempted contractual waivers of bankruptcy.[3] This apparent judicial hostility has contributed to the common view that any attempt at blocking or restricting bankruptcy access will be void as contrary to public policy.[4]

A deeper dive into the judicial treatment of golden shares, however, reveals a theoretical complexity and ambiguity that case law has done little to illuminate or resolve. The difficulty in understanding the enforceability of golden shares is compounded by the widely varying factual circumstances at play in each golden share case.[5] With such great variation, it is hard to glean how much of the courts' opinions are guided by the facts and how much by an interpretation of the law's acceptance of golden shares. The increase in corporate Chapter 11 filings brought on by the COVID-19 pandemic has heightened the necessity for a degree of uniformity in adjudicating golden shares disputes.[6]

While the majority of courts have considered golden shares to be void as contrary to public policy, the Fifth Circuit indicated these shares could be valid.[7] With an emergent split in authority and the predicted long-term rise in business bankruptcies in the wake of the COVID-19 pandemic, achieving a level of uniformity in approaching these issues is vital for all constituencies in the bankruptcy process.[8]

Part II of this Note discusses the background of golden shares. It reviews the historical development of the device and then proceeds to consider the public policy concerns that are implicated by golden shares. Part II concludes with a discussion of several cases involving golden shares. Part III analyzes the

1. Timothy J. McKeon, *Delaware Bankruptcy Court Rules that Shareholder Cannot Enforce "Golden Share" Blocking Right to Dismiss Bankruptcy Filed Without its Consent*, MINTZ (May 27, 2020), https://www.mintz.com/insights-center/viewpoints/2831/2020-05-27-delaware-bankruptcy-court-rules-shareholder-cannot?_cldee=cHJvY2Vzc2luZ0Btb25kYXEuY29t&recipientid=contact-295d9778829aea11943ba0d3c1f8c3d1-32dc5eafbe374bc9a2c7d5f4f8762f8d&esid=797428c4-4da#utm_source=Mondaq&utm_medium=syndication&utm_campaign=LinkedIn-integration [https://perma.cc/4PMX-8Y67].

2. *See In re* Franchise Servs. of N. Am., Inc., 891 F.3d 198, 205 (5th Cir. 2018).

3. *See, e.g.*, *In re* Intervention Energy Holdings, LLC, 553 B.R. 258, 265 (Bankr. D. Del. 2016).

4. *See* Marshall E. Tracht, *Contractual Bankruptcy Waivers: Reconciling Theory, Practice, and Law*, 82 CORNELL L. REV. 301, 305–09 (1997).

5. *See infra* Section II.D.

6. *Chapter 11 U.S. Commercial Bankruptcy Filings up 78% in September*, EPIQ (Oct. 5, 2020), https://www.epiqglobal.com/en-us/about/news/restructuring-bankruptcy/chapter-11-us-bankruptcy-filings-up-78-september [https://perma.cc/B8FX-XGFL].

7. *See Franchise Services*, 891 F.3d at 209.

8. *Compare Intervention Energy*, 553 B.R. at 263, *and* Transcript of Telephonic Hearing at 17, *In re* Pace Industries, LLC, No. 20-10927, 2020 WL 5015839 (Bankr. D. Del. May 5, 2020), *with Franchise Services*, 891 F.3d at 209.

theoretical underpinnings of the debate over golden shares. First, it explores the issue of fiduciary duty and how they might arise where a golden shareholder seeks to exercise its blocking right. It then moves into a discussion of the history of federal common law as a preview to a proposed path towards resolution of the issue.

Part IV offers federal common law fiduciary duty as the ideal means to adjudicate these disputes. This solution provides the court with a structure that is compatible with the widely varying factual circumstances seen in golden shares cases.[9] In addition, the burden-shifting framework sketched out in Part IV serves to filter improper bankruptcy blocking actions by golden shareholders from those exercises of legitimate business decision-making authority by a bona fide shareholder. Superimposing this procedural framework will help to obviate an overly broad expansion of fiduciary duties owed by minority shareholders that may otherwise be precipitated by an absolute federal common law fiduciary duty. Part V will conclude by emphasizing the importance of resolving this dispute and restating the arguments in favor of establishing a federal common law fiduciary duty.

II. BACKGROUND

A golden share arises from "the issuance to a creditor of a trivial number of shares that gives the creditor the right to prevent a voluntary bankruptcy petition, potentially among other rights."[10] It has been reiterated by the courts that bankruptcy cannot be contractually waived or avoided.[11] Questions still remain over the ability of creditors who are *also shareholders* to influence a bankruptcy decision by exercising veto rights under a golden share.[12]

Concern over undermining the longstanding public policy favoring access to bankruptcy relief stems from the realities of golden shares' historical development. As the rate of corporate bankruptcy filing increased in the late 1980s and 1990s, creditors began to seek craftier ways to restrict debtors' ability to file.[13] The resounding judicial rejection of pure contractual bankruptcy waivers led creditors to instead explore machinations in corporate law.[14] Bankruptcy-remote entities ("BREs"), formed for the purpose of "insulat[ing] the debt owed to the creditor from other parts of the business that may enter a bankruptcy case,"

9. John J. Rapisardi, Evan M. Jones & Daniel S. Shamah, *Courts Differ on Enforcement of "Bankruptcy Remote" Provisions*, O'MELVENY & MEYERS (June 11, 2020), https://www.omm.com/resources/alerts-and-publications/alerts/courts-differ-on-enforcement-of-bankruptcy-remote-provisions/ [https://perma.cc/BL9G-DQKR].

10. *Franchise Services*, 891 F.3d at 205.

11. *See Intervention Energy*, 553 B.R. at 263.

12. *The Fifth Circuit Considers Enforceability of Bankruptcy Blocking "Golden Share" Provisions in Franchise Services*, WEIL RESTRUCTURING (Jun. 15, 2018), https://restructuring.weil.com/corporate-governance/the-fifth-circuit-considers-of-golden-share-provisions-in-franchise-services/ [https://perma.cc/TN6C-8E9A].

13. Tracht, *supra* note 4, at 304.

14. Theresa J. Pulley Radwan, *Who's Got A Golden Ticket?—Limiting Creditor Use of Golden Shares to Prevent A Bankruptcy Filing*, 83 ALB. L. REV. 569, 576–77 (2020).

provided a potential remedy for creditors.[15] A BRE is frequently tied to a larger parent business and structured so as to require unanimous approval from its own board of directors to file for bankruptcy.[16] Furthermore, one of the BRE's directors is independent from the parent business, often chosen by the parent's largest creditor.[17]

The problem such entities run into, however, is the lack of fiduciary duty owed by the blocking director to the business itself.[18] While there is some uncertainty over the extent of the fiduciary duty that a creditor owes a debtor corporation, some Delaware courts have shown a general hesitancy to hold no fiduciary duty where there is clear control in the ability to block a filing.[19] By granting the blocking power to an equity owner instead of a director, golden shares offer creditors an attractive means to avoid the fiduciary duty pitfall of BREs.[20]

This Part will explore the public policy concerns that led to early judicial opposition to bankruptcy waivers and restrictions. It will then analyze how creditors have utilized corporate authority arguments in response to this. The Part concludes with a discussion of the rise of golden shares and the judicial response to the device.

A. Public Policy Concerns

Bankruptcy is at its very core a collective process, designed to dispose of the claims of all creditors in a singular proceeding that ideally maximizes both the value of the bankruptcy estate and the satisfaction of creditors' claims.[21] More than two centuries ago, the founders recognized the necessity of a uniform bankruptcy system to accomplish these goals, specifically providing for this in Article I, § 8 of the United States Constitution.[22] Courts were keenly aware that allowing parties to contract their way out of this uniform bankruptcy system would directly undermine the policies it was meant to enforce. Namely, the policy of "assur[ing] access to the right of a person, including a business entity, to seek federal bankruptcy relief as authorized by the Constitution and enacted by Congress" would be vitiated.[23]

Relying upon these policies, the District Court for the Southern District of New York in 1933 rejected an agreement to waive the bankruptcy discharge for an individual debtor.[24] The court held that such an attempt to bypass bankruptcy would enfeeble the system and frustrate its important purpose of facilitating the

15. *Id.* at 577.
16. *Id.*
17. *Id.*
18. *Id.* at 578.
19. *See id.*
20. *See id.* at 583–84.
21. *See* Daniel J. Bussel, *Corporate Governance*, *Bankruptcy Waivers, and Consolidation in Bankruptcy*, 36 EMORY BANKR. DEV. J. 99, 121 (2020).
22. U.S. CONST. art. I, § 8, cl. 4.
23. *In re* Intervention Energy Holdings, LLC, 553 B.R. 258, 265 (Bankr. D. Del. 2016).
24. *In re* Weitzen, 3 F. Supp. 698, 698 (S.D.N.Y. 1933).

settlement of a debtor's estate.[25] Numerous courts have since reaffirmed the principle that the collective mechanisms of bankruptcy may not be waived by private contractual agreement.[26] In the individual debtor context, another fundamental consideration animating these courts has been protecting the bankruptcy goal of affording debtors the ability to obtain a "fresh start."[27] The "fresh start" concept, while more relevant perhaps as applied to individual debtors, carries weight in the corporate debtor context as well.[28]

B. The Authority Opening

With such an array of cases over the past century reaffirming the importance of shielding bankruptcy benefits from contractual waivers, it may appear on first glance that the door leading to successful limitation of debtor bankruptcy is all but closed to creditors. Although courts have consistently voided contractual provisions that purport to waive access to the bankruptcy system's most fundamental benefits, judicial consensus has not been reached on the effect of similar limitations pertaining to the *authority* of a corporate entity to file bankruptcy.[29] The Supreme Court held in 1945 that state law determines corporate authority to file for bankruptcy.[30] Furthermore, the Supreme Court established in 1979 that property rights in bankruptcy are defined by state law unless a compelling federal interest demands otherwise.[31] The reasoning behind the Court's decision in *Butner* can logically be extended to cover contract rights as well.[32]

25. *Id.* ("It would be repugnant to the purpose of the Bankruptcy Act to permit the circumvention of its object by the simple device of a clause in the agreement, out of which the provable debt springs, stipulating that a discharge in bankruptcy will not be pleaded by the debtor. The Bankruptcy Act would in the natural course of business be nullified in the vast majority of debts arising out of contracts, if this were permissible.") (quoting Fed. Nat. Bank v. Koppel, 148 N.E. 379, 380 (Mass. 1925)).

26. *See, e.g.*, *In re* Pease, 195 B.R. 431, 432 (Bankr. D. Neb. 1996) ("It has long been settled that contractual provisions prohibiting the filing of a bankruptcy case are not enforceable."); *In re* Huang, 275 F.3d 1173, 1177 (9th Cir. 2002) ("It is against public policy for a debtor to waive the prepetition protection of the Bankruptcy Code."); *In re* Shady Grove Tech Ctr. Assocs. L.P., 216 B.R. 386, 389 (Bankr. D. Md. 1998) ("The courts have uniformly held that a waiver of the right to file a bankruptcy case is unenforceable.").

27. *In re* Bogdanovich, 292 F.3d 104, 107 (2d Cir. 2002) ("Congress made it a central purpose of the bankruptcy code to give debtors a fresh start in life and a clear field for future effort unburdened by the existence of old debts."). For an example of the "fresh start" concept serving as the driving force behind an analysis of prepetition waiver of bankruptcy benefits, see *In re* Kline, 520 B.R. 168, 177 (Bankr. E.D. Pa. 2014) (characterizing, and ultimately rejecting, a prepetition waiver of discharge as "fall[ing] in the face of the primacy and essential nature of the 'fresh start'").

28. *See* Tracht, *supra* note 4, at 307–08 (noting the various courts that have applied the "fresh start" concept to business debtors, yet criticizing the appropriateness of this application).

29. *Compare In re* Franchise Servs. of N. Am., Inc., 891 F.3d 198, 209 (5th Cir. 2018) ("No statute or binding caselaw licenses this court to . . . reallocate corporate authority to file for bankruptcy just because the shareholder also happens to be an unsecured creditor."), *with In re* Intervention Energy Holdings, LLC, 553 B.R. 258, 265 (Bankr. D. Del. 2016) ("A provision in a limited liability company governance document obtained by contract, the sole purpose and effect of which is to place into the hands of a single, minority equity holder the ultimate authority to eviscerate the right of that entity to seek federal bankruptcy relief . . . is tantamount to an absolute waiver of that right, and . . . is void as contrary to federal public policy.").

30. Price v. Gurney, 324 U.S. 100, 106 (1945).

31. Butner v. United States, 440 U.S. 48, 55 (1979).

32. *See* Steven L. Schwarcz, *Rethinking Freedom of Contract: A Bankruptcy Paradigm*, 77 TEX. L. REV. 515, 577 (1999).

Both the Third and Seventh Circuits have relied on state law in interpreting executory contracts,[33] and scholars have argued property rights and contract rights are increasingly blurred in bankruptcy.[34] The following two cases shed more light on how the corporate authority issue informs judicial analyses of golden shares.

In *Global Ship Systems*, a limited liability company ("LLC") whose main asset was a shipyard entered into an operating agreement with its major secured lender.[35] Under the terms of the operating agreement, this lender's consent was required for any voluntary bankruptcy petition.[36] Some of the money that flowed from the lender to the company was allocated to equity, resulting in the lender attaining an equity position as well.[37] When the LLC defaulted on its loan, the major secured lender moved to initiate foreclosure proceedings on the shipyard.[38] In order to avoid this consent requirement, the LLC's CEO encouraged several other creditors to file an involuntary bankruptcy petition against the debtor.[39] The major secured lender responded by asking the court to dismiss the petition due to bad faith.[40]

While the court recognized the extensive case law restricting pre-petition bankruptcy waivers imposed by creditors, it distinguished these decisions as pertaining exclusively to creditors.[41] Because the secured creditor here had equity in the company, it "[wore] two hats in this case" and "[had] the unquestioned right to prevent, by withholding consent, a voluntary bankruptcy case."[42] Once the court established the consent provision didn't undermine any federal public policy of bankruptcy, it deferred to Georgia state law that provided for flexible contractual structuring of LLCs, which led to the bankruptcy petition's ultimate dismissal.[43]

In *DB Capital*, the debtor was an LLC with the sole purpose of developing and selling a luxury condominium project in Aspen, Colorado.[44] The debtor defaulted on its loans with the primary mortgage lender involved in the project, and it filed for Chapter 11 protection after a receivership action was brought against it by the lender and another member of the LLC in state court.[45] The debtor

33. *In re* Columbia Gas Sys. Inc., 50 F.3d 233, 241 (3d Cir. 1995); *In re* Streets & Beard Farm P'ship, 882 F.2d 233, 235 (7th Cir. 1989).

34. Margaret Howard, *Equipment Lessors and Secured Parties in Bankrputcy: An Argument for Coherence*, 48 WASH. & LEE L. REV. 253, 298 (1991); Schwarcz, *supra* note 32, at 576–77, 577 n.338.

35. *In re* Glob. Ship Sys., LLC, 391 B.R. 193, 196, 199 (Bankr. S.D. Ga. 2007).

36. *Id.* at 199.

37. *Id.* at 203.

38. *Id.* at 197.

39. *Id.* at 199.

40. *Id.* at 201.

41. *Id.* at 203.

42. *Id.*

43. *Id.* at 204 ("Georgia law is clear in that it permits, to the maximum extent possible, parties to exercise freedom of contract in the structuring of LLC[s]. Members of an LLC are statutorily empowered to make *all decisions* in managing the LLC subject to the operating agreement.").

44. *In re* DB Capital Holdings, LLC, Nos. CO–10–046, 10–23242, 2010 WL 4925811, at *1 (10th Cir. BAP (Colo.) Dec. 6, 2010).

45. *Id.* at *1–2.

corporate entity was governed by an operating agreement formed in early 2006, which was amended later a few months later to provide that the company "will not institute proceedings to be adjudicated bankrupt or insolvent . . . or file a petition seeking, or consent to, reorganization or relief under any applicable federal or state law relating to bankruptcy."[46] The other LLC member sought the dismissal of the bankruptcy petition on the grounds that the project manager, who also owned an entity that was a general partner in the LLC, did not have the authority to file for bankruptcy under the amended operating agreement.[47] The debtor argued that since the amendment was ultimately executed at the demand of the secured creditor, it should be invalidated due to the public policy disfavoring pre-petition waivers of bankruptcy.[48]

A Bankruptcy Appellate Panel for the Tenth Circuit ("B.A.P.") found no evidence that the amendment was coerced by the secured creditor and declined to invalidate the amendment.[49] The B.A.P. held that, regardless of the court's disposition of the amendment's enforceability, state law determines authority to file for bankruptcy.[50] As the project manager did not have authority to file for bankruptcy on behalf of the business under Colorado law, the court was required to dismiss the petition.[51]

Despite the commonly held view that restrictions on the ability to file bankruptcy are void as contrary to public policy, *Global Ship Systems and DB Capital* signify the lack of consensus on bankruptcy blocking provisions in corporate documents. By grounding their analyses in the issues of who has the authority to file bankruptcy and what contract rights are guaranteed under state law, these courts similarly concluded that corporate control documents may impose valid limitations upon the right of a corporate debtor to access the bankruptcy system.[52] Similar tensions between federal public policy and state law remained at the forefront in subsequent cases considering a unique type of blocking provision–the golden share.[53]

C. History of Golden Shares

Golden shares originated in the United Kingdom during the wave of privatization in the 1980s.[54] Rather than being devised by sophisticated corporate creditors, it was the British government that utilized the device to influence previously state-held firms of significant importance to the state.[55] The control rights these shares conferred were broad, including the ability to veto corporate

46. *Id.* at *7.
47. *Id.* at *1–2.
48. *Id.* at *3.
49. *Id.*
50. *Id.*
51. *Id.*
52. *See id.* at *5; *In re* Glob. Ship Sys., LLC, 391 B.R. 193, 203–05 (Bankr. S.D. Ga. 2007).
53. *See* discussion *infra* Section II.D.
54. Andrei A. Baev, *Is There A Niche for the State in Corporate Governance? Securitization of State-Owned Enterprises and New Forms of State Ownership*, 18 HOUS. J. INT'L L. 1, 20 (1995).
55. *Id.*

decisions and restrict acquisition activity.[56] Transferability of golden shares was restricted to governmental actors due to the great power conferred on owners by the device.[57] A number of other countries made use of golden shares to maintain some control over major privatizing companies, including Turkey in its airlines, Israel in its state telecommunications company, and Portugal in its oil company.[58] The constant of these golden share systems was the disproportionate control its holder had in relation to its equity in the corporation.[59]

Eventually, the European Commission restricted golden shares through a series of decisions issued across several nations in the early 2000s.[60] The European Commission was concerned with the effect this extensive state influence would have upon freedom of movement and freedom of establishment between European Community members.[61] Despite this judicial hostility in Europe, the device was adopted by private lenders in America seeking to have control over a corporate borrower's decision to file bankruptcy.[62] Where lenders saw an attractive tool to steer borrowers clear of bankruptcy's uncertainty while avoiding the incurrence of fiduciary duties on their part, courts and scholars perceived an impermissible undermining of the vital public policy favoring liberal access to bankruptcy relief for debtors.[63]

D. Judicial Reception of Golden Shares

With the history of bankruptcy blocking provisions recounted and some background on how corporate authority can provide an avenue of relief for creditors sketched out, this Section will discuss three key cases dealing with golden shares. The divergent outcomes of these cases highlight how the competing policy goals of bankruptcy continue to produce tension in determining golden shares' enforceability.

56. *See* Christine O'Grady Putek, *Limited but Not Lost: A Comment on the ECJ's Golden Share Decisions*, 72 FORDHAM L. REV. 2219, 2222–23 (2004).

57. *See* Baev, *supra* note 54, at 26.

58. *See id.* at 21–22.

59. *See id.* at 26.

60. *See* Putek, *supra* note 56, at 2254–71.

61. *See id.* at 2220.

62. *See* Eric L. Johnson & Mark G. Stingley, *Intervention Energy Holdings Good Public Policy, or Unnecessary Intrusion into State Law?*, 35 AM. BANKR. INST. J. 20, 20 (2016).

63. *See, e.g.*, *In re* Intervention Energy Holdings, LLC, 553 B.R. 258, 265 (Bankr. D. Del. 2016) (describing a golden share arrangement as being "tantamount to an absolute waiver of that right, and, even if arguably permitted by state law, . . . void as contrary to federal public policy"); Bussel, *supra* note 21, at 121 ("[A]ny set of contractual arrangements with the substantive effect of requiring the consent of a creditor . . . to a voluntary corporate bankruptcy filing, whether in the creditor's debt contract or baked into the corporate charter, should run afoul of the public policy prohibiting advance waiver of access to bankruptcy.").

1. Intervention Energy

In *Intervention Energy,* a 2016 case from the Bankruptcy Court for the District of Delaware, the debtor was an oil and natural gas exploration and production company that had issued 22,000,001 shares.[64] The debtor's holding company held 22,000,000 of these shares while EIG, a secured creditor, held only one share.[65] The debtor and EIG entered into a note purchase agreement that was amended to include a provision "requir[ing] approval of each holder of common units of the Parent prior to any voluntary filing for bankruptcy protection for the Parent of the Company."[66]

The court, emphasizing that the golden shareholder's "primary relationship with the debtor is that of creditor—not equity holder," held that such a provision was void as contrary to public policy.[67] It noted that the public policy of assuring access to bankruptcy relief applies just as much to a business entity as to an individual.[68] Factors of particular importance to the court's analysis included the creditor's purpose in crafting the golden share's blocking right; the relationship between the party seeking bankruptcy relief and the party seeking to block it being substantively that of creditor and debtor in this instance; and the blocking party's owing no duty to anyone but itself.[69] The court indicated that even if the golden share's blocking provision was enforceable under state law, federal public policy superseded this and acted to void the provision.[70]

2. Franchise Services

In the 2018 Fifth Circuit case *Franchise Services*, the debtor was a car rental company that retained the services of a bank to finance an acquisition.[71] In exchange for the requisite capital, the bank received through its subsidiary 100% of the debtor's preferred stock that would have accounted for a 49.76% equity interest if converted.[72] It also reincorporated, providing that holders of preferred stock had to consent to a bankruptcy filing.[73] When the debtor later went bankrupt, the bank sought to dismiss the petition on the grounds that consent had not been obtained.[74] The debtor countered that the bank was also an unsecured creditor due to an unpaid bill it owed the bank, and thus policy and precedent weighed against permitting a creditor to block a bankruptcy filing.[75]

64. *Intervention Energy*, 553 B.R. at 260.
65. *Id.*
66. *Id.* at 261.
67. *Id.* at 265.
68. *Id.*
69. *See id.*
70. *Id.*
71. *In re* Franchise Servs. of N. Am., Inc., 891 F.3d 198, 203 (5th Cir. 2018).
72. *Id.*
73. *Id.*
74. *Id.* at 204.
75. *Id.*

The court held that "federal bankruptcy law does not prevent a bona fide equity holder from exercising its voting rights to prevent the corporation from filing a voluntary bankruptcy petition just because it also holds a debt owed by the corporation and owes no fiduciary duty to the corporation or its fellow shareholders."[76] It expressed skepticism over the argument that the bank would invest $15 million to protect itself from a potential unpaid $3 million bill.[77] Dismissing concerns that any and all veto provisions in corporate documents constitute an impermissible restriction, the court pointed out that "[n]o statute or binding caselaw licenses this court to ignore corporate foundational documents, deprive a bona fide shareholder of its voting rights, and reallocate corporate authority to file for bankruptcy just because the shareholder also happens to be an unsecured creditor."[78]

The golden shareholder's exercise of its blocking right did not give rise to any fiduciary duties under federal law.[79] The court noted that state law determines who has authority to file for bankruptcy on behalf of a corporation.[80] While it did not explicitly rule on the issue due to the debtor's having waived the argument on appeal, the court emphasized the great flexibility of Delaware's corporate statute and assumed that the provision would be valid under Delaware law.[81] On the question of fiduciary duty under state law, the court looked to Delaware case law on shareholder fiduciary duty.[82] A minority shareholder such as the bank could only have fiduciary duties under Delaware law if it was deemed a controlling shareholder.[83] Even though the bank had a 49.76% stake and sought to dismiss the debtor's bankruptcy petition, the court held that it did not have sufficient influence over the board to establish its status as a controlling shareholder.[84]

3. Pace Industries

In *Pace Industries*, a 2020 case from the Bankruptcy Court for the District of Delaware, the debtor corporation proposed a $300 million prepackaged plan of reorganization.[85] A preferred shareholder asked the bankruptcy court to dismiss the filing, arguing its blocking provision enabled it to veto any bankruptcy petition.[86] The court declined to dismiss the petition.[87] Judge Walrath noted that,

76. *Id.* at 209.
77. *Id.* at 208.
78. *Id.* at 209.
79. *Id.*
80. *Id.*
81. *Id.* at 210–11.
82. *Id.* at 211.
83. *Id.*
84. *Id.* at 213.
85. Eric Daucher & Christy Rivera, *Rights to Block Bankruptcy Filings in Doubt*, NORTON ROSE FULBRIGHT (June 16, 2020), https://www.projectfinance.law/publications/rights-to-block-bankruptcy-filings-in-doubt [https://perma.cc/YXR9-MV79].
86. Transcript of Telephonic Hearing at 17, *In re* Pace Industries, LLC, No. 20-10927, 2020 WL 5015839 (Bankr. D. Del. May 5, 2020).
87. *Id.* at 38.

while no prior case had directly held a blocking right void as contrary to federal policy favoring liberal access to the bankruptcy system, "based on the facts of this case, I am prepared to be the first court to do so . . ."[88] According to the court, any restriction on the right to file bankruptcy is void.[89] The court expressly declined to follow the reasoning of the Fifth Circuit in *Franchise Services*, suggesting both minority shareholders and creditors are equally barred from blocking a bankruptcy filing.[90] The court stressed the federal public policy of maintaining access to the bankruptcy system for debtors in need of such relief.[91] In holding that "federal public policy does require that the Court consider what is in the best interest of all," the court also affirmed the collective principle upon which the bankruptcy system is based.[92]

E. Current Status of Golden Shares

While there is some uncertainty over the extent of the fiduciary duty that a creditor owes a debtor corporation, some Delaware courts have shown a general hesitancy to hold no fiduciary duty where there is clear control in the ability to block a filing.[93] By granting the blocking power to an equity owner instead of a director, golden shares offer creditors an attractive means to avoid the fiduciary duty pitfall of BREs.[94] As *Franchise Services* suggests, the courts may be more willing to defer to state corporate law and enforce golden shares where the ability to block a bankruptcy filing is inherently intertwined with the corporate ownership structure itself.[95] The utility of golden shares to both debtors and creditors is limited, however, until a modicum of uniformity is established in the judicial approach to golden shares.

III. ANALYSIS

The golden shares dilemma is rooted in two fundamental principles of bankruptcy law that frequently conflict with one another. First, the right to file bankruptcy cannot be waived or contractually prevented.[96] Second, bankruptcy law does not alter or modify state law rights or remedies, except where a statutory provision or compelling federal policy justifies their supersession.[97] This applies to corporate charters and the determination of who is authorized to file a bankruptcy petition on behalf of a business debtor.[98] Therefore, the principles

88. *Id.*
89. *Id.* at 39.
90. *Id.* at 40.
91. *Id.* at 38–39.
92. *Id.* at 42.
93. *See, e.g.*, *id.*
94. *See* Radwan, *supra* note 14, at 583–84.
95. *In re* Franchise Servs. of N. Am., Inc., 891 F.3d 198, 208–10 (5th Cir. 2018).
96. Bussel, *supra* note 21, at 116.
97. Butner v. United States, 440 U.S. 48, 55 (1979).
98. Price v. Gurney, 324 U.S. 100, 106 (1945).

governing contractual waivers apply to golden shares as well.[99] State contract and business law thus inform the rights of creditors and debtors under the federal bankruptcy system.[100]

An illustration of this interplay can be found in *Franchise Services*, the Fifth Circuit golden share case examined above.[101] The court construed a Delaware corporate statute that was defined by its laissez-faire approach to contractual relations between business entities.[102] While it did not reach a final interpretation of whether Delaware law permitted golden shares, the Fifth Circuit in *Franchise Services* appeared willing to defer to the flexibility of Delaware law on the issue of the validity of golden shares.[103] In holding that "federal bankruptcy law does not prevent a bona fide equity holder from exercising its voting rights to prevent the corporation from filing a voluntary bankruptcy petition just because it also holds a debt owed by the corporation and owes no fiduciary duty to the corporation or its fellow shareholders," the court signaled that the putative judicial aversion to anything resembling a bankruptcy waiver might be overstated.[104]

This Part will first discuss the importance of fiduciary duty to adjudicating disputes involving golden shares. It will then lay the groundwork for a recommended remedy to the golden shares dilemma through a discussion of the history of federal common law.

A. Fiduciary Duties and Golden Shares

The golden shareholder's exercise of its blocking right could potentially constitute a breach a fiduciary duty.[105] While there is no question over the longstanding principle that a majority shareholder owes a fiduciary duty to minority shareholders,[106] more uncertainty surrounds the question of what fiduciary duties are owed by minority shareholders.[107] Generally, a minority shareholder will owe fiduciary duties to other shareholders if it "exercises control over the business affairs of the corporation."[108] To establish a fiduciary duty, it is

99. *See* Bussel, *supra* note 21, at 121 ("The bankruptcy policy supporting the longstanding prohibition of pre-petition bankruptcy waivers directly applies to attempts to contractually vary corporate governance rules to prohibit voluntary bankruptcy filings without creditor consent. Indeed, any set of contractual arrangements with the substantive effect of requiring the consent of a creditor or its designated representative to a voluntary corporate bankruptcy filing, whether in the creditor's debt contract or baked into the corporate charter, should run afoul of the public policy prohibiting advance waiver of access to bankruptcy.").

100. *Franchise Services*, 891 F.3d at 208–10.

101. *See* discussion *supra* Subsection II.D.2.

102. *Franchise Services,* 891 F.3d at 210.

103. *Id.*

104. *Id.* at 209.

105. Transcript of Telephonic Hearing at 39–40, *In re* Pace Indust., LLC, No. 20-10927, 2020 WL 5015839 (Bankr. D. Del. May 5, 2020) ("I do believe that, under Delaware state law . . . a blocking right, such as exercised in the circumstances of this case, would create a fiduciary duty on the part of the shareholder . . . .").

106. *See* Allied Chem. & Dye Corp. v. Steel & Tube Co. of Am., 120 A. 486, 491 (Del. Ch. 1923)

107. For a comparison of cases that have come out differently on the status of minority shareholders who exercise bankruptcy blocking rights, see *supra* Section II.D.

108. Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d 1334, 1344 (Del. 1987).

sufficient that there be "actual control over a particular decision."[109] In *Basho*, the court identified one potential source of this control as "the exercise of contractual rights to channel the corporation into a particular outcome by blocking or restricting other paths."[110] The blocking right in this case enabled the minority shareholder to restrict the corporation's access to capital and other financing options.[111] This significant control over the corporation's financing decisions was a primary factor in the court holding that the minority shareholder owed a fiduciary duty to the corporation and its other shareholders.[112]

Control is inferred "when blocking rights empower a minority investor to 'channel the corporation into a particular outcome.'"[113] A "formal equity stake" is not required, for "even without a formal equity stake, contractual control can be exerted to the point where fiduciary obligations follow."[114] Some courts have even suggested that a necessary component of any acceptable bankruptcy remote structure is the director's owing fiduciary duties.[115] In *Pace Industries*, the court hinted a fiduciary duty might arise where creditors seek to exercise their blocking right as golden shareholders.[116] Where a non-controlling creditor exercises its blocking right as a golden shareholder, the particular facts of each case will be highly determinative in the court's fiduciary duty analysis.[117]

As illustrated by cases such as *Global Ship Systems*, *DB Capital*, and *Franchise Services*, however, there has emerged an alternative judicial approach towards bankruptcy blocking provisions that is markedly more accepting of these restrictions.[118] At the root of this shifting paradigm is the increasingly prominent role that contracts play in bankruptcy.[119] As corporate control documents are essentially contractual arrangements,[120] they may be subjected to the same analysis in bankruptcy.[121] The classification of corporate control documents as contracts

109. Basho Techs. Holdco B, LLC v. Georgetown Basho Invs., LLC, No. 11802-VCL, 2018 WL 3326693, at *26 (Del. Ch. July 6, 2018), *aff'd sub nom.* Davenport v. Basho Techs. Holdco B, LLC, 221 A.3d 100 (Del. 2019); *see also In re* Primedia Inc. Derivative Litig., 910 A.2d 248, 257 (Del. Ch. 2006) ("[C]ontrol over the particular transaction at issue [is] enough.").

110. *Basho*, No. 11802-VCL, 2018 WL 3326693, at *26.

111. *See id.* at *35.

112. *See id.*

113. Skye Mineral Invs., LLC v. DXS Capital (U.S.) Ltd., No. 2018-0059-JRS, 2020 WL 881544, at *27 (Del. Ch. Feb. 24, 2020).

114. Ann M. Lipton, *After* Corwin*: Down the Controlling Shareholder Rabbit Hole*, 72 VAND. L. REV. 1977, 2004–05 (2019).

115. *See e.g.*, *In re* Lake Michigan Beach Pottawattamie Resort LLC, 547 B.R. 899, 913 (Bankr. N.D. Ill. 2016).

116. Transcript of Telephonic Hearing at 40–41, *In re* Pace Indust., LLC, No. 20-10927, 2020 WL 5015839 (Bankr. D. Del. May 5, 2020).

117. *See* R. Stephen McNeill & Eric D. Torres, *Loyalty to the Bar: An Analysis of Corporate Charter Bankruptcy Blocking Provisions*, 29 No. 2 J. BANKR. L. & PRAC. NL Art. 3 (2020).

118. *See id.*; *see also supra* Section II.B.

119. *See* David A. Skeel, Jr. & George Triantis, *Bankruptcy's Uneasy Shift to A Contract Paradigm*, 166 U. PA. L. REV. 1777, 1779 (2018).

120. *See* Salzberg v. Sciabacucchi, 227 A.3d 102, 116 (Del. 2020) ("[C]orporate charters are contracts among a corporation's stockholders . . . ."); Bussel, *supra* note 21, at 121.

121. *See In re* Lake Michigan Beach Pottawattamie Resort LLC, 547 B.R. 899, 912 (Bankr. N.D. Ill. 2016) ("[T]he long-standing policy against contracting away bankruptcy benefits is not necessarily controlling when what defeats the rights in question is a corporate control document instead of a contract . . . . Nonetheless,

brings them under the ambit of *Butner* and *Price*, which reorients the analysis around the mandates of state law.[122]

In addition to being more permissive towards corporate contracting, state law provides the means to avoid the fiduciary duty issue as well.[123] In Delaware, for example, breach of fiduciary duty is understood conceptually as an equitable tort.[124] Namely, it is a relationship "derived from a special relationship between one person and another."[125] Equity and law merged in 1938 with the promulgation of the Federal Rules of Civil Procedure, yet this hardly vitiated the force of equitable fiduciary duties.[126] The Supreme Court of Delaware has established that "the Delaware General Corporation Law is a broad enabling act which leaves latitude for substantial private ordering, provided the statutory parameters and judicially imposed principles of fiduciary duty are honored."[127] Similarly, the state's LLC Act was meant to be "read in concert with equitable fiduciary duties."[128] "The common law fiduciary duties that were developed to address those who manage business entities were . . . an equitable gap-filler."[129]

As "Delaware's corporate statute is widely regarded as the most flexible in the nation because it leaves the parties to the corporate contract (managers and stockholders) with great leeway to structure their relations, subject to relatively loose statutory constraints and to the policing of director misconduct through equitable review," the analytical shift towards state law provides more freedom to the court to defer to the parties' contractual arrangements on breach of fiduciary duty claims in cases involving bankruptcy blocking provisions.[130] Considering golden shares in particular, it is important to recall the two circumstances when Delaware courts will find a fiduciary duty exists on the part of shareholders. First, majority shareholders owe a fiduciary duty to fellow shareholders and the corporation.[131] Second, minority shareholders owe a fiduciary duty to fellow shareholders and the corporation when they exercise a "controlling interest" over the affairs of the business.[132] Control over a particular transaction is sufficient to establish a party's status as a controller and, as the *Basho* court noted, one

common wisdom dictates that the corporate control documents should not include an absolute prohibition against bankruptcy filing.").

122. Butner v. United States, 440 U.S. 48, 55 (1979); Price v. Gurney, 324 U.S. 100, 106 (1945). For a discussion of why *Butner* implicates contract rights in addition to property rights, see Schwarcz, *supra* note 32, at 576, 577, 577 n.338.

123. *See* Radwan, *supra* note 14, at 601; Skeel, Jr. & Triantis, *supra* note 119, at 1785.

124. *See* Basho Techs. Holdco B, LLC v. Georgetown Basho Inv'rs, LLC, No. 11802-VCL, 2018 WL 3326693, at *22 (Del. Ch. July 6, 2018), *aff'd sub nom.* Davenport v. Basho Techs. Holdco B, LLC, 221 A.3d 100 (Del. 2019).

125. *See* J. Travis Laster & Michelle D. Morris, *Breaches of Fiduciary Duty and the Delaware Uniform Contribution Act*, 11 DEL. L. REV. 71, 89 (2010).

126. *See id.* at 89, 89 n.102, 91–93.

127. Williams v. Geier, 671 A.2d 1368, 1381 (Del. 1996); *see also* Auriga Cap. Corp. v. Gatz Prop., LCC, 40 A.3d 839, 849 (Del. Ch. 2012), *aff'd sub nom.*, Gatz Props., LLC v. Auriga Cap. Corp., 59 A.3d 1206 (Del. 2012).

128. *Auriga Capital*, 40 A.3d at 849.

129. *Id.* at 853.

130. Salzberg v. Sciabacucchi, 227 A.3d 102, 116 (Del. 2020).

131. *See* Ivanhoe Partners v. Newmont Mining Corp., 535 A.2d 1334, 1344 (Del. 1987).

132. *See id.* at 1343–44.

sufficient indication of control is "the exercise of contractual rights to channel the corporation into a particular outcome by blocking or restricting other paths."[133]

It was against this backdrop of Delaware's highly lenient corporate statute and case law on fiduciary duty that the Fifth Circuit held no fiduciary duty existed in *Franchise Services*, even though the golden shareholder owned shares amounting to 49.76% and blocked the debtor from filing for bankruptcy.[134] The court relied on Delaware case law requiring a "steep" threshold for minority control and establishing that "a shareholder is generally free to act in its self-interest, unencumbered by any fiduciary obligation."[135] When the golden shares analysis is untethered from considerations of federal public policy and anchored instead in state law on business, contracts, and fiduciary duty, courts have ample ground to adopt an accommodating stance towards these devices.

B. A History of Federal Common Law

Establishing a federal common law fiduciary duty owed by creditors possessing blocking rights to corporate debtors provides an avenue of resolving the golden share dilemma. Beginning with its landmark *Erie* decision, the Supreme Court has made clear that federal common law is appropriate only in specific circumstances.[136] To adhere to the Supreme Court's dictates and provide helpful clarity to all parties, this fiduciary duty under federal common law must be carefully defined and justified.

Swift v. Tyson represents the first attempt by the Supreme Court to determine the parameters of federal common law when faced with a state common law rule or statute conflict.[137] The Court held that state common law only provides evidence of what the law is, and it does not in itself constitute binding legal authority on federal courts sitting in diversity.[138] In disputes involving negotiable instruments, the court is fully competent to adjudicate the matter based on general principles of commercial jurisprudence.[139] Justice Story's opinion reflected the desire for uniformity and the federalization of commercial law that undergirded the court's decision.[140] *Swift* did not result in greater uniformity within the judicial system, however, and instead produced uncertainty about which law

133. Basho Techs. Holdco B, LLC v. Georgetown Basho Inv's., LLC, No. 11802-VCL, 2018 WL 3326693, at *26 (Del. Ch. July 6, 2018), *aff'd sub nom.* Davenport v. Basho Techs. Holdco B, LLC, 221 A.3d 100 (Del. 2019).

134. *In re* Franchise Servs. of N. Am., Inc., 891 F.3d 198, 209–11 (5th Cir. 2018).

135. *Id.* at 211.

136. *See* Erie R.R. Co. v. Tompkins, 304 U.S. 64, 71–80 (1938); *see also* Tex. Indus., Inc. v. Radcliff Materials, Inc., 451 U.S. 630, 640 (1981) (discussing the limited circumstances in which federal common law is appropriate).

137. Swift v. Tyson, 41 U.S. 1 (1842), *overruled by* Erie R.R. Co. v. Tompkins, 304 U.S. 64 (1938); *see* 19 CHARLES ALAN WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE & PROCEDURE § 4502 (3d ed. 2020).

138. *Swift*, 41 U.S. at 18.

139. *Id.* at 19.

140. Koen Lenaerts & Kathleen Gutman, *"Federal Common Law" in the European Union: A Comparative Perspective from the United States*, 54 AM. J. COMPAR. L. 1, 24 (2006).

applied, an unfair advantage for plaintiffs in the choice of law, and ripe conditions for citizenship maneuvering by corporations.[141]

Overturning *Swift* almost a century later, the Supreme Court's *Erie* decision augured a dramatic shift in the jurisdiction of federal courts.[142] But while regularly viewed as the death knell of federal common law, *Erie's* ultimate effect may not have been so profound.[143] First, *Erie* dealt with a diversity action and the conflict between federal and state common law in this particular circumstance.[144] Second, at issue was the formulation of federal general common law, leaving the door open to specific areas of applicability.[145] While the conceptual justifications for the court's decision are multiple, a concern for maintaining the vitality of federalism was undoubtedly a primary driving force.[146] Federal courts infringe upon the states' autonomy "whenever they unilaterally apply a rule of their own choosing in lieu of substantive state law."[147] When the federal court can point to some constitutional or federal statutory provision for support, this infringement problem is assuaged.[148]

In order for federal common lawmaking to be constitutionally valid as applied to golden shares in bankruptcy, the issue must be suitable for categorization within one of the general realms that the Supreme Court has indicated are acceptable locations for the creation of federal common law.[149] Federal common lawmaking has been deemed permissible when "a federal rule of decision is necessary to protect uniquely federal interests," or when "Congress has given the courts the power to develop substantive law."[150] Congressional authorization provides ample room for the exercise of federal common lawmaking power in bankruptcy to impose a fiduciary duty on golden shareholders.

C. Federal Common Law Arising by Congressional Authorization

The courts have authority to craft federal common law when there exists "some congressional authorization to formulate substantive rules of decision."[151] After reaffirming this foundational principle, the *Texas Industries* court adduced the Labor Management Relations Act ("LMRA") and the Sherman Act as

141. *See* Martha A. Field, *Sources of Law: The Scope of Federal Common Law*, 99 HARV. L. REV. 881, 900 (1986).

142. *See* Erie R.R. Co. v. Tompkins, 304 U.S. 64, 91–92 (1938); *see also* Peter Manus, Kivalina *at the Supreme Court: A Lost Opportunity for Federal Common Law*, 8 PITT. J. ENV'T PUB. HEALTH L. 223, 239–40 (2014).

143. *See* Manus, *supra* note 142, at 239–41.

144. *See id.* at 240–41.

145. *See id.*

146. Bradford R. Clark, *Federal Common Law: A Structural Reinterpretation*, 144 U. PA. L. REV. 1245, 1259 (1996); Thomas W. Merrill, *The Common Law Powers of Federal Courts*, 52 U. CHI. L. REV. 1, 18 (1985).

147. *See* Clark, *supra* note 146.

148. *Id.*

149. *See* Tex. Indus., Inc. v. Radcliff Materials, Inc., 451 U.S. 630, 640 (1981).

150. *Id.* (citation omitted).

151. *Id.* at 641.

instances where the Court has read a statute to vest in the federal judiciary the authority to fashion federal common law.[152]

1. Example #1: The Labor Management Relations Act (LMRA)

> The operative language in the LMRA comes from Section 301(a):
> Suits for violation of contracts between an employer and a labor organization representing employees in an industry affecting commerce as defined in this chapter, or between any such labor organizations, may be brought in any district court of the United States having jurisdiction of the parties, without respect to the amount in controversy or without regard to the citizenship of the parties.[153]

The *Texas Industries* Court viewed this as not only a jurisdictional grant, but also an authorization of the federal courts' development of "a common law of labor-management relations within that jurisdiction."[154] In commenting on the Sherman Act, the court noted that its "sweeping language forb[ade] '[e]very contract, combination . . . , or conspiracy, in restraint of trade' and 'monopoliz[ing], or attempt[ing] to monopolize, . . . any part of the trade or commerce . . . .'"[155]

Federal common law's applicability to the LMRA was first established in *Lincoln Mills*, where the Court interpreted Section 301(a) as a grant of broad authority to federal courts to fashion substantive federal law for the enforcement of collective bargaining agreements.[156] The Court highlighted the legislative history of the statute in construing its meaning.[157] Leading proponents of the bill had stressed the importance of maintaining stable industrial relations through promoting collective bargaining agreements without strikes and establishing a procedure by which such agreements could be enforced by either party.[158] Once the Court determined that federal law was the applicable substantive law, it indicated that the content of this federal law is "fashion[ed] from the policy of our national labor laws."[159] Courts may find authority for their decisions on Section 301(a) disputes from the express language of the statute; "in the penumbra of express statutory mandates;" or "by looking at the policy of the legislation and fashioning a remedy that will effectuate that policy."[160] Ultimately, "[t]he range of judicial inventiveness will be determined by the nature of the problem."[161]

152. *Id.* at 642–43.
153. 29 U.S.C. § 185(a).
154. *Texas Indus.*, 451 U.S. at 642–43.
155. *Id.* at 643 (quoting 15 U.S.C. §§ 1, 2).
156. Textile Workers Union of Am. v. Lincoln Mills of Ala., 353 U.S. 448, 450–51 (1957).
157. *Id.* at 453–54.
158. *Id.* at 454.
159. *Id.* at 456.
160. *Id.* at 457.
161. *Id.*

2. Example #2: Employee Retirement Income Security Act (ERISA)

Similar in structure to the LMRA, the Employee Retirement Income Security Act ("ERISA") led the courts to establish another area for the application of federal common law.[162] The Court first indicated that federal common law was called for under ERISA in *Construction Laborers*.[163] In making this determination, the Court relied upon the federal policy as expressed by Senator Javits.[164] The cosponsoring senator stated his intention that "a body of Federal substantive law will be developed by the courts to deal with issues involving rights and obligations under private welfare and pension plans."[165]

Just two years later, the issue again arose as the focus of Justice Brennan's concurrence in *Mass. Mutual*.[166] In arguing for liberal exercise of federal common law powers under ERISA, Justice Brennan placed great emphasis upon the statute's legislative history.[167] Justice Brennan pointed to both the Javits statement that was cited by the *Construction Laborers* court and the comments of Senator Williams, the other cosponsor of the bill.[168] Senator Williams had said that disputes about beneficiaries' rights under ERISA "will be regarded as arising under the laws of the United States, in similar fashion to those brought under Section 301 of the Labor Management Relations Act."[169] Since *Lincoln Mills* held that the LMRA required federal common law be derived from the policy animating the statute, the logical conclusion followed that ERISA was also designed with the intention of giving the courts freedom to fashion "appropriate rights and remedies."[170]

The Court further solidified the applicability of federal common law to ERISA in its *Pilot Life* decision.[171] The case involved an employee who sought benefits under a group insurance policy after he was injured in an accident.[172] The district court rejected the employee's state law claims for failure to pay benefits on the group policy, holding that they were preempted by ERISA, in a decision subsequently reversed by the Fifth Circuit.[173] In reversing the Fifth Circuit, the Supreme Court relied on both the structure of the statute and its legislative history.[174] The intended structural similarities between ERISA and the LMRA, which had previously been construed by the court as directing the

162. *See* Jeffrey A. Brauch, *The Federal Common Law of ERISA*, 21 HARV. J. L. & PUB. POL'Y 541, 543 (1998).

163. Franchise Tax Bd. of Cal. v. Constr. Laborers Vacation Tr. for S. Cal., 463 U.S. 1, 24 n.26 (1983); *see* Brauch, *supra* note 162, at 549.

164. *Construction Laborers*, 463 U.S. at 24 n.26.

165. *Id.* (quoting 120 CONG. REC. 29,942 (1974)).

166. Massachusetts Mut. Life Ins. Co. v. Russell, 473 U.S. 134, 156 (1985) (Brennan, J., concurring).

167. *Id.* at 156–57.

168. *Id.* at 156.

169. *Id.* (quoting 120 CONG. REC. 29,933 (1974)).

170. *Id.* at 157.

171. Pilot Life Ins. Co. v. Dedeaux, 481 U.S. 41, 56 (1987); *see* Brauch, *supra* note 162, at 552–53.

172. *Pilot Life*, 481 U.S. at 43.

173. *Id.* at 44.

174. *Id.* at 52.

judiciary to fashion a federal rule of decision,[175] led the Court to conclude that Congress sought the development of federal common law under ERISA as well.[176]

Following Justice Brennan, the Court cited the statements of Senators Javits and Williams to underscore Congress's desire for both a "uniformity of decision" and federalized system of adjudication to develop under ERISA.[177] Notably, the Court slightly altered the meaning of the Javits statement to provide further support for its stance in favor of a federal common law under ERISA.[178] Whereas Senator Javits said that "a body of Federal substantive law will be developed by the courts to deal with issues involving rights and obligations under private welfare and pension plans," the Court claimed congressional expectations were that "a federal common law of rights and obligations under ERISA-regulated plans would develop."[179] By altering this expression to suggest Congress intended the development of a federal common law dealing broadly with rights and obligations under the ERISA *statute* itself rather than the formulation of federal common law under ERISA-regulated *plans*, the Court erected a platform for the further expansion of federal common law under ERISA.[180]

With its decision two years later in *Bruch*, the Court conclusively confirmed its expansive interpretation of federal common law under ERISA.[181] The Court noted that ERISA "abounds with the language and terminology of trust law," and it pointed to Senator Javits's statement as evidence of the legislative intent for a federal common law to develop.[182] ERISA's legislative history, the structure of the statute's language, and the similarities between its remedies provisions and the LMRA's form the basis of the Court's precedent favoring an expansive interpretation of federal common lawmaking authority under ERISA.[183]

D. Federal Common Law in Bankruptcy

The following Section will analyze the historical and constitutional justifications of a significant role for federal common law in bankruptcy. First, it will explain why the doctrine of conflict preemption lends support to the exercise of federal common lawmaking power in bankruptcy. This Section will then proceed to address the uniquely federal nature of the modern bankruptcy system. Finally, support for federal common lawmaking in bankruptcy will be adduced from the legislative history and structure of the Bankruptcy Code.

175. *See* Textile Workers Union of Am. v. Lincoln Mills of Ala., 353 U.S. 448, 456 (1957).
176. *Pilot Life*, 481 U.S. at 56–57.
177. *Id.* at 56 (quoting H.R. REP. No. 93–533, at 12 (1973)).
178. *See id.*; Brauch, *supra* note 162, at 553.
179. *Pilot Life*, 481 U.S. at 56.
180. *See* Brauch, *supra* note 162, at 553.
181. Firestone Tire & Rubber Co. v. Bruch, 489 U.S. 101, 110 (1989); *see* Brauch, *supra* note 162, at 553.
182. *Bruch*, 489 U.S. at 110.
183. *See* Brauch, *supra* note 162, at 554.

1. Preemption

By providing that federal law "shall be the supreme law of the land,"[184] the Constitution established that "Congress has the power to preempt state law."[185] The preemptive authority can be exercised when there is an express statutory provision indicating the intent to supersede state law (express preemption); when a federal regulatory scheme is so pervasive as to leave no room for supplemental state legislation (field preemption); and when a federal law and state law are in conflict with one another (conflict preemption).[186] Conflict preemption "includes cases where compliance with both federal and state regulations is a physical impossibility, and those instances where the challenged state law stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."[187] In weighing whether a state law constitutes a sufficient impediment to a federal legislative program, courts must "examin[e] the federal statute as a whole and identify[] its purpose and intended effects."[188]

The doctrine of conflict preemption is closely related to federal common law.[189] When federal common law controls in a proceeding, the court can incorporate state law or a uniform federal common law rule.[190] If state law is incorporated, the court has essentially made a de facto determination that preemption does not apply.[191] While there is no preemption if a federal common law rule is adopted, it still leads to the same result as preemption: federal law applies, and state law does not.[192]

There is a "'strong presumption against inferring Congressional preemption' [that] also applies 'in the bankruptcy context.'"[193] "The presumption may be overcome, however, where 'a Congressional purpose to preempt . . . is clear and manifest.'"[194] In evaluating whether Congress intended for preemption to occur, courts must "look to the text, structure, and purpose of the statute and the surrounding statutory framework."[195]

Congress's intent in establishing a national and uniform system of bankruptcy is plain, and "[t]he national purpose to establish uniformity necessarily excludes state regulation."[196] Therefore, "[s]tates may not pass or enforce laws to interfere with or complement the [federal bankruptcy laws] or to provide

184. U.S. CONST. art. VI, cl. 2.

185. Arizona v. United States, 567 U.S. 387, 399 (2012).

186. *Id.*

187. *Id.* (citations omitted).

188. Crosby v. Nat'l Foreign Trade Council, 530 U.S. 363, 373 (2000).

189. *See* Robert W. Miller, *A Comprehensive Framework for Conflict Preemption in Federal Insolvency Proceedings*, 123 W. VA. L. REV. 423, 446–47 (2020).

190. *Id.*

191. *Id.* at 447.

192. *Id.*

193. *In re* Fed.-Mogul Glob. Inc., 684 F.3d 355, 365 (3d Cir. 2012) (quoting Integrated Sols., Inc. v. Serv. Support Specialties, Inc., 124 F.3d 487, 493 (3d Cir. 1997)).

194. *Id.* (quoting Farina v. Nokia Inc., 625 F.3d 97, 117 (3d Cir. 2010).

195. Rosenberg v. DVI Receivables XVII, LLC, 835 F.3d 414, 419 (3d Cir. 2016).

196. Int'l Shoe Co. v. Pinkus, 278 U.S. 261, 265 (1929).

additional or auxiliary regulations."[197] Where a state statute "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress" in establishing a centralized bankruptcy system, it must lose out to the conflicting federal provision in the Bankruptcy Code.[198]

Federal bankruptcy law presents a particularly accommodating sphere for the operation of conflict preemption, which in turn creates a potent justification for the imposition of federal common law fiduciary duties on golden shareholders.[199] Congress specified that bankruptcy matters should be adjudicated in a federal forum by conferring exclusive jurisdiction on the district courts under 28 U.S.C. § 1334(a).[200] The unique nature of this exclusively federal jurisdiction renders preemption claims in bankruptcy more formidable than those made in cases premised on claims over which the federal and state courts have concurrent jurisdiction.[201]

Exclusive bankruptcy jurisdiction "would mean little if standards of conduct in bankruptcy proceedings varied from state to state, and from state to federal court."[202] Recall that Congress derived its authority to establish bankruptcy law from the United States Constitution, which gave Congress the power "[t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States."[203] Acting pursuant to its powers under the Constitution, Congress has created a comprehensive statutory framework built upon the concept of bankruptcy as a federal forum power.[204] Under this federal forum power, federal courts have the authority to bind all the debtor's creditors to a single plan of restructuring.[205] To illustrate how federal bankruptcy law can preempt conflicting state law and adjust the rights of debtors and creditors, an analysis of the courts' preemption analysis in the context of *ipso facto* clauses under § 365(e) of the Bankruptcy Code and state law breach of fiduciary duty claims will be necessary.[206]

197. *Id.*

198. Perez v. Campbell, 402 U.S. 637, 649 (1971) (quoting Hines v. Davidowitz, 312 U.S. 52, 67 (1941)).

199. *See* MSR Expl., Ltd. v. Meridian Oil, Inc., 74 F.3d 910, 913–16 (9th Cir. 1996).

200. 28 U.S.C. § 1334(a); *see id.* at 913. Bankruptcy judges have authority to hear bankruptcy matters under 28 U.S.C. § 157(a), which allows district courts to "provide that any or all cases under title 11 and any or all proceedings arising under title 11 or arising in or related to a case under title 11 shall be referred to the bankruptcy judges for the district." There are local rules in every judicial district that provide for the automatic reference of bankruptcy matters to the bankruptcy court. CHARLES J. TABB & RALPH BRUBAKER, BANKRUPTCY LAW: PRINCIPLES, POLICIES, AND PRACTICE 759 (3d. ed. 2010).

201. *See MSR*, 74 F.3d at 913–14.

202. Koffman v. Osteoimplant Tech., Inc., 182 B.R. 115, 126 (D. Md. 1995).

203. U.S. CONST. art. I, § 8, cl. 4.

204. Ralph Brubaker, *Explaining* Katz*'s New Bankruptcy Exception to State Sovereign Immunity: The Bankruptcy Power as a Federal Forum Power*, 15 AM. BANKR. INST. L. REV. 95, 127 (2007).

205. *Id.*

206. 11 U.S.C. § 365(e).

a. Example #1: *Ipso Facto* Clauses

In *Summit*, the First Circuit considered the preemptive effect of § 365(e) of the Bankruptcy Code,[207] which provides that modifications or termination clauses conditioned on the debtor's bankruptcy filing are prohibited.[208] After two general partners in a partnership had filed for bankruptcy, another general partner ("plaintiff partner") sought to oust them from their management roles.[209] In moving the court for a declaratory determination of the parties' rights, the plaintiff partner relied on a Massachusetts state law that provided for the automatic termination of general partnership rights upon the filing of a bankruptcy petition.[210] Attempting to evade the reach of § 365(e)'s prohibition on *ipso facto* bankruptcy clauses, the plaintiff partner argued that the provision only applied to private contractual *ipso facto* clauses.[211] Thus, statutory *ipso facto* provisions and the states' interests in their enforcement should still be effective in bankruptcy.[212]

The court rejected this interpretation and held that the state law provision was preempted by § 365(e).[213] The court related how the legislature wanted to combat *ipso facto* clauses because of their inhibiting effect on debtors' attempts at rehabilitation through bankruptcy.[214] By providing that *ipso facto* clauses are banned "[n]otwithstanding a . . . provision . . . in applicable law," § 365(e) clearly expressed this legislative intent.[215] With nothing to indicate that statutory *ipso facto* clauses posed less of a threat to debtor rehabilitation efforts than contractual *ipso facto* clauses, the court concluded that § 365(e) preempted the Massachusetts state law terminating general partnership interests upon a bankruptcy filing.[216]

b. Example #2: Corporate Authority to File Bankruptcy

In *Bral*, the co-manager ("plaintiff co-manager") of an LLC sued the other co-manager ("defendant co-manager") after he filed for bankruptcy on behalf of the company right before a nonjudicial foreclosure sale of the company's office building was scheduled to occur.[217] The plaintiff co-manager's credit bid of $3 million was the highest bid at the sale, but the foreclosure trustee vacated the sale after learning of the bankruptcy petition.[218] Eventually, the bankruptcy court dismissed the LLC's bankruptcy case for improper authorization of the filing, but the plaintiff co-manager had to increase his bid to $4.1 million at the second sale

207. Summit Inv. & Dev. Corp. v. Leroux, 69 F.3d 608, 611 (1st Cir. 1995).
208. 11 U.S.C. § 365(e).
209. *Leroux,* 69 F.3d at 609.
210. *Id.*
211. *Id.* at 611.
212. *Id.*
213. *Id.*
214. *Id.*
215. *Id.*; 11 U.S.C. § 365(e)(1).
216. *Leroux,* 69 F.3d at 611.
217. Steward Fin., LLC v. Bral (*In re* Bral), 622 B.R. 737, 740–41 (B.A.P. 9th Cir. 2020).
218. *Id.* at 740.

to win.[219] The plaintiff co-manager sued the defendant co-manager, who also happened to be in Chapter 11 as an individual debtor, for the $1.1 million difference in the sales prices.[220] The co-managers' contractual relationship, as spelled out in the operating agreement, provided the basis for the allegation of liability arising out of the improper filing.[221] As a result of the alleged breach of these contractual obligations, the plaintiff co-manager pursued state law claims of abuse of process and tortious interference with contractual relations against the defendant co-manager.[222] In holding such claims to be preempted by federal bankruptcy law, the court stressed the importance of a broad and systematic bankruptcy power.[223] Any preemption analysis must recognize in bankruptcy a "comprehensive federal scheme and a dominant federal interest in maintaining complete control over the bankruptcy process."[224]

Further analogizing the case at bar to prior cases in the Ninth Circuit, the court distinguished between prepetition and postpetition breach of fiduciary duty claims under state law.[225] If the breach of fiduciary duty occurred entirely before the bankruptcy petition was filed, state corporate governance law controlled the adjudication of the parties' rights and injuries arising from the corporate relationship.[226] Where the breach of fiduciary duty is interwoven with the bankruptcy petition itself, however, the parties' contractual rights under state corporate governance law must cede to the federal courts' "exclusive[] control [over] the regulation of the bankruptcy process."[227] In this way, federal bankruptcy law preempts contractual rights arising under state law by dint of the parties' corporate relationship.[228]

c. Example #3: Shareholder Breach of Fiduciary Duty Claims

The same principle was applied in the context of a derivative shareholder suit in *Casden*, with the Bankruptcy Court for the Northern District of Ohio reaching the same result.[229] After a company issued allegedly false and misleading public statements about its financial situation and subsequently filed for Chapter 11 bankruptcy protection, a shareholder filed a derivative class claim against the company's directors and officers for, inter alia, breach of fiduciary duty.[230] The class was comprised entirely of the company's shareholders, and the company's directors and officers owed a fiduciary duty to these shareholders

219. *Id.* at 740–41.
220. *Id.* at 741.
221. *Id.* at 740–41.
222. *Id.* at 741.
223. *See id.* at 745.
224. *Id.* at 745.
225. *Id.* at 747.
226. *See id.*
227. *Id.* at 745.
228. *See id.* at 740–47.
229. Casden v. Burns, 504 F. Supp. 2d 272, 279–82 (N.D. Ohio 2007), *aff'd on other grounds*, 306 F. App'x 966 (6th Cir. 2009).
230. *Id.* at 275.

under state law.[231] The court held that this claim was preempted by federal bankruptcy law and presented three justifications in support.[232]

First, the claim had not accrued because no cognizable injury to the shareholder had yet occurred.[233] Since "accrual of the claim depends on what happens in the Bankruptcy Court, the potential future claim would interfere sufficiently with the bankruptcy process to trigger preemption."[234] Second, further interference with the bankruptcy process would be invited by allowing such a state law fiduciary duty claim to stand without being preempted.[235] Similar suits would arise in other cases, and "[p]ermitting assertion of a host of state law causes of action to redress wrongs under the Bankruptcy Code would . . . stand[ ] as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress."[236] Lastly, "a nexus exists between plaintiff's claim and sanctions available for improper filing of a bankruptcy proceeding."[237] Bankruptcy law retains exclusive control over remedies for abuse of the bankruptcy system, regardless of what liability might arise from a fiduciary relationship under state corporate law.[238]

Taken together, these cases suggest the willingness of courts to adjust the rights of corporate parties through preemption based on considerations of bankruptcy policy. Undergirding this judicial comfort with preemption in bankruptcy is the uniform nature of bankruptcy law.

2. Uniform Nature of Bankruptcy

The uniform nature of bankruptcy law derives from the history of bankruptcy and the Constitution.[239] Under the United States Constitution, Congress has the authority "[t]o establish . . . uniform Laws on the subject of Bankruptcies throughout the United States."[240] The express grant of the power to make "uniform" laws indicates the historical roots of bankruptcy's uniform nature.[241] The remedies promised by bankruptcy can be facilitated only through "giving a power to the general government to introduce and perpetuate a uniform system."[242] Thus, there is a "unique, historical, and even constitutional need for uniformity in the administration of the bankruptcy laws . . . ."[243]

231. *Id.*
232. *Id.* at 281–82.
233. *Id.* at 281.
234. *Id.*
235. *See id.* at 282.
236. *Id.* (quoting Pertuso v. Ford Motor Credit Co., 233 F.3d 417, 426 (6th Cir. 2000)).
237. *Id.*
238. *Id.*
239. *See* Adam J. Levitin, *Toward a Federal Common Law of Bankruptcy: Judicial Lawmaking in a Statutory Regime*, 80 AM. BANKR. L.J. 1, 72 (2006).
240. U.S. CONST. art. I, § 8, cl. 4.
241. *See* Levitin, *supra* note 239, at 72.
242. MSR Expl., Ltd. v. Meridian Oil, Inc., 74 F.3d 910, 915 (9th Cir. 1996) (quoting 2 JOSEPH STORY, COMMENTARIES ON THE CONSTITUTION OF THE UNITED STATES § 1107 (2d ed. 1851)).
243. *Id.*

In *Katz*, the Court illuminated the weight of this uniformity interest.[244] The respondent, the trustee supervising the liquidation of the debtor's estate, brought suit against Virginia higher education institutions (petitioners) to recover preferential transfers made to them by the debtor.[245] Defending against the preference action, the petitioners argued they were shielded from the suit as state agencies entitled to sovereign immunity.[246] The Court rejected the petitioners' argument, relying on the Constitutional authorization of Congressional establishment of "uniform" bankruptcy laws.[247] Moreover, "[t]he power granted to Congress by that Clause is a unitary concept rather than an amalgam of discrete segments."[248] Through its passage of §§ 547 and 550(a), Congress sought to give federal courts the power to avoid preferential transfers.[249] Acting under its Constitutional grant of authority, Congress permissibly intruded upon the authority of the states and subordinated their sovereign immunity to the "uniformity interest"[250] characteristic of the federal bankruptcy system.[251] Other Circuit Courts of Appeals have relied on this interest in uniformity to justify creating federal common law, highlighting the vitality of the uniformity interest in bankruptcy.[252]

3. Legislative History

The legislative history of the Bankruptcy Code evinces Congress's intent to preserve the equitable powers of the bankruptcy court.[253] The House Report on the Bankruptcy Act of 1978 emphasized that "[t]he bankruptcy court will remain a court of equity . . . . The court's power is broader than the general doctrine of equitable subordination, and encompasses subordination on any equitable grounds."[254] As Professor Levitin explains, "the term 'equity' in the context of bankruptcy jurisdiction and powers is a term of art that means 'federal common law.' Thus, a 'court of equity' is better understood as a 'court with federal common lawmaking power.'"[255]

This dynamic can be seen in the legislative histories of §§ 105(a) and 510(c) of the Bankruptcy Code.[256] Under §105(a), "[t]he court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions

244. Cent. Va. Cmty. Coll. v. Katz, 546 U.S. 356, 376–77 (2006).
245. *Id.* at 360.
246. *Id.*
247. *See id.* at 370.
248. *Id.*
249. *Id.* at 371–72.
250. Levitin, *supra* note 239, at 72.
251. *Katz*, 546 U.S. at 377 ("[T]he power to enact bankruptcy legislation was understood to carry with it the power to subordinate state sovereignty, albeit within a limited sphere.").
252. *See, e.g.*, Lindsay v. Beneficial Reinsurance Co. (*In re* Lindsay), 59 F.3d 942, 948 (9th Cir. 1995) ("The value of national uniformity of approach need not be subordinated, therefore, to differences in state choice of law rules.").
253. Levitin, *supra* note 239, at 74.
254. H.R. REP. 95-595, at 359 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6315.
255. *See* Levitin, *supra* note 239, at 75.
256. 11 U.S.C. § 105(a); *id.* § 510(c).

of this title."[257] The broad grant of authority represented by this language represents § 105(a)'s role as "a device that incorporates bankruptcy courts' historical equity powers into the Code."[258] Furthermore, the House Committee Report indicated that the Bankruptcy Code incorporated bankruptcy courts' historical equity powers.[259]

Section 510(c) represents another expression of Congress's desire for the courts to have federal common lawmaking power.[260] It provides that the court may:

> (1) under principles of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim or all or part of an allowed interest to all or part of another allowed interest; or
>
> (2) order that any lien securing such a subordinated claim be transferred to the estate.[261]

One of the legislative leaders behind the provision conveyed the intention "that the term 'principles of equitable subordination' follow existing case law and leave to the courts development of this principle."[262] Thus, the power of equitable subordination is essentially a power to make federal common law in bankruptcy.[263]

IV. RECOMMENDATION

As the aforementioned cases illustrate, federal common lawmaking in bankruptcy is by no means a rarity. Federal courts do not have the freedom to craft federal common law for every issue arising in bankruptcy, however.[264] Rather, the courts have been given authority to develop federal common law for specific issues in bankruptcy.[265] Before the federal common lawmaking power in bankruptcy can be utilized to impose a fiduciary duty on golden shareholders, the appropriateness of establishing fiduciary duties through federal common law must first be shown. The following cases demonstrate that federal courts are willing to impose fiduciary duties under federal common law, provided some legislative authorization or uniquely federal interest exists.

257. *Id.* § 105(a).

258. *See* Levitin, *supra* note 239, at 57.

259. *Id.* at 57 (citing H.R. REP. NO. 95-595, at 316–17 (1977), *reprinted in* 1978 U.S.C.C.A.N. 5963, 6315).

260. *See id.* at 76.

261. 11 U.S.C. § 510(c).

262. Levitin, *supra* note 239, at 76.

263. *See id. But see* J. Maxwell Tucker, *Substantive Consolidation: The Cacophony Continues*, 18 AM. BANKR. INST. L. REV. 89, 144 (2010) (disagreeing with Professor Levitin and arguing that Congress has constrained federal common lawmaking through several amendments since the passage of the Bankruptcy Reform Act of 1978).

264. *See* John T. Cross, *Viewing Federal Jurisdiction Through the Looking Glass of Bankruptcy*, 23 SETON HALL L. REV. 530, 549–50 (1993); *In re* Consol. Freightways Corp., 443 F.3d 1160, 1163 (9th Cir. 2006) ("Thus, one cannot say that the underlying principles of federal bankruptcy law auger for the recognition of a federal common law rule.").

265. *See* Cross, *supra* note 264, at 548–52.

A. Starr Int'l Co. v. Fed. Reserve Bank of New York

In *Starr International*, the principal shareholder of AIG sued the Federal Reserve Bank of New York ("FRBNY") in the Southern District of New York for breach of fiduciary duty and aiding and abetting breach of fiduciary duty after it rescued the insurance company during the financial crisis of 2008.[266] The claim challenged FRBNY's rescue arrangement, which was conditioned on AIG's handing over an 80% interest in its common stock to the federal government through a trust instrument.[267] The shareholder argued that Delaware fiduciary duty law controls, and therefore the bank is liable for its actions involving the rescue.[268] The district court dismissed the shareholder's complaint and the Second Circuit affirmed.[269]

In its decision, the court emphasized that the "uniquely federal interest" implicated by the government's rescue of AIG required federal common law's preemption of state fiduciary duty law.[270] The court reasoned that Delaware fiduciary duty law could not be applied to FRBNY's actions, for FRBNY was not meant to be "operated for the profit of shareholders," but rather was "created and [is] operated in furtherance of the national fiscal policy."[271] If subjected to Delaware fiduciary duty law, FRBNY would be required to act in the best interests of AIG's shareholders.[272] Such a "private duty would present a significant and direct conflict with FRBNY's obligation to act in the public interest as a fiscal agent of the United States and to take action in unusual and exigent circumstances when its failure to act would adversely affect the economy."[273]

B. Texas Lottery Comm'n v. Tran

Section 523(a)(4) of the Bankruptcy Code provides that "[a] discharge . . . does not discharge an individual debtor from any debt . . . for fraud or defalcation while acting in a fiduciary capacity, embezzlement, or larceny[.]"[274] In *Tran*, the Fifth Circuit applied federal common law to determine that a Texas lottery sales agent is a fiduciary within the meaning of § 523(a)(4).[275] The Texas Lottery Commission had brought an adversary action in the bankruptcy case, arguing that the debt owed on the proceeds of lottery tickets the debtor had not delivered to the Commission as a lottery sales agent was incurred through "fraud or defalcation while acting in a fiduciary capacity."[276]

266. Starr Int'l Co. v. Fed. Rsrv. Bank of N.Y., 742 F.3d 37, 38–39 (2d Cir. 2014).
267. *Id.* at 39.
268. *Id.* at 40.
269. *Id.* at 38.
270. *Id.* at 40.
271. *Id.*
272. *Id.* at 41–42.
273. *Id.* at 42 (internal quotation marks omitted).
274. 11 U.S.C. § 523(a).
275. Tex. Lottery Comm'n v. Tran, 151 F.3d 339, 342 (5th Cir. 1998).
276. *Id.* at 341.

The court began its analysis by recalling the fundamental "fresh start" policy of the bankruptcy system, which is accomplished through granting debtors a discharge from their debts.[277] Exceptions to the discharge, such as that provided for in § 523(a)(4), must be construed narrowly so as to effectuate this policy.[278] The concept of "fiduciary" in § 523(a)(4) is thus limited under federal common law to situations involving expressly created trusts or fiduciary relationships.[279] For a trusts or fiduciary relationship created by state statute to meet the federal common law standard, it must "(1) include a definable res and (2) impose 'trust-like' duties."[280]

The state statute at issue provided that lottery sales agents must hold the money they receive "in trust for the benefit of the state before delivery" to the Texas Lottery Commission, while the Commission's rules provided that the sales agent "shall have a fiduciary duty to preserve and account for lottery proceeds."[281] Although the state law proclaimed a fiduciary relationship, the court held that federal common law's narrow interpretation of "fiduciary" under § 523(a)(4) controlled and the debtor was not a fiduciary in her capacity as lottery sales agent.[282]

C. Federal Common Law's Role in Resolving the Golden Shares Dilemma

Starr and *Tran* show that where a uniquely federal interest is at odds with state law, federal common law must be applied.[283] The golden shares dilemma presents just such a situation. Maintaining broad access to the federal bankruptcy system for debtors is a fundamentally important federal interest.[284] If excessive deference is given to state law and creditors are able to block bankruptcy filings through their status as shareholders, this federal interest shall inevitably be jeopardized.[285] Imposing a federal common law fiduciary duty provides a path forward out of this dilemma. As the case law demonstrates, it is by no means an extinct power of the federal judiciary. Rather, a considerable body of federal common law has arisen in the years since the Supreme Court's *Erie* decision.[286]

This body of federal common law includes the ability to establish fiduciary duties at federal common law where the state standard is in conflict.[287] Golden shareholders are by no means restricted from contesting a bankruptcy filing.[288] A showing must simply be made that such actions are for the best interests of the

277. *Id.* at 342.
278. *See id.*
279. *Id.*
280. *Id.* at 342–43.
281. *Id.* at 343.
282. *Id.* at 342–43.
283. *See id.* at 342; Starr Int'l Co. v. Fed. Resrv. Bank of N.Y., 742 F.3d 37, 40 (2d Cir. 2014).
284. *See In re* Intervention Energy Holdings, LLC, 553 B.R. 258, 263 (Bankr. D. Del. 2016).
285. *Id.* at 264.
286. *See* Manus, *supra* note 142, at 239–40.
287. Tex. Indus., Inc. v. Radcliff Materials, Inc., 451 U.S. 630, 641 (1981).
288. *See In re* Franchise Servs. of N. Am., Inc., 891 F.3d 198, 205, 209 (5th Cir. 2018).

company that is seeking to file bankruptcy.[289] It is particularly appropriate to create a federal common law fiduciary duty in the golden shares context, as this would reaffirm the equitable power of the bankruptcy court.[290] The factual variations in golden shares cases is significant, and calls for broad discretion on the part of the fact-finder.[291]

D. Implementing Federal Common Law Fiduciary Duty through a Burden-Shifting Framework

If the establishment of a fiduciary duty under federal common law is to provide an equitable solution to the golden shares dilemma, shareholders with bona fide objections to a bankruptcy filing must be accorded a level of protection. There exist obvious differences between a primary lender with a blocking right by dint of owning one share a corporation and a 40% shareholder directly involved in the corporation's business decisions that just so happens to have also loaned to the business occasionally. Applying a burden-shifting framework in conjunction with imposing a federal common law fiduciary duty would help to distinguish between these situations and ensure all parties receive proper treatment.

In the context of claim valuation disputes under § 506(a) of the Bankruptcy Code, courts already utilize a burden-shifting framework to allocate the burden of proof between the debtor and creditor.[292] The Third Circuit was faced with divergent judicial approaches to this issue in *Heritage*, with some courts placing the burden of proof on the debtor, some placing the burden of proof on the creditor, and some opting for a burden-shifting analysis.[293] The court determined that employing a burden-shifting framework was the most suitable for adjudication of claims disputes.[294] By operation of 11 U.S.C. § 502(a) and Bankruptcy Rule 3001(f), a secured creditor's properly filed claim has prima facie validity.[295] Thus, the initial burden must be on the debtor seeking to challenge either the amount of the claim or the claim itself.[296] Once sufficient evidence has been adduced by the debtor, the burden shifts to the creditor, who has "the ultimate burden of persuasion . . . to demonstrate by a preponderance of the evidence both the extent of its lien and the value of the collateral securing its claim."[297]

289. *See* George Howard & Lawrence Elbaum, *Shareholder Rights in Bankruptcy*, N.Y. L.J. (June 4, 2021, 2:00 PM), https://www.law.com/newyorklawjournal/2021/06/04/shareholder-rights-in-bankruptcy/?slreturn=20220125200735 [https://perma.cc/ZR4B-4698].

290. *See* Levitin, *supra* note 239, at 74.

291. *See* discussion *supra* Part II.

292. *E.g.*, *In re* Heritage Highgate, Inc., 679 F.3d 132, 139–40 (3d Cir. 2012); *In re* Harford Sands, Inc., 372 F.3d 637, 640–41 (4th Cir. 2004); *In re* Porretto, 761 F. App'x 437, 442 (5th Cir. 2019).

293. *Heritage*, 679 F.3d at 139–40.

294. *Id.* at 140.

295. *Id.*

296. *Id.*

297. *Id.* (quoting *In re* Robertson, 135 B.R. 350, 352 (Bankr. E.D. Ark. 1992); *see also In re* Harford Sands, Inc., 372 F.3d 637, 640 (4th Cir. 2004) ("If the debtor carries its burden, the creditor has the ultimate burden of proving the amount and validity of the claim by a preponderance of the evidence.").

It requires no stretch in logic to apply this framework to the imposition of a federal common law fiduciary duty on golden shareholders seeking to block the debtor's bankruptcy. Under § 301(a) of the Bankruptcy Code, a voluntary bankruptcy case is commenced upon the filing of the petition by the debtor.[298] Like the creditor's properly filed claim in the context of § 506(a) claims disputes, the debtor's petition for bankruptcy protection has prima facie validity.[299] Once the bankruptcy case has been initiated, the golden shareholder would have the burden of proving that it has the contractual right to block the bankruptcy filing. If the creditor can show that it does have a valid right to block the bankruptcy filing under state contract and corporate law, the burden would then shift back to the debtor.

This burden of persuasion would require a showing by the debtor that the blocking party does not have a bona fide business reason to exercise its veto right, and it is acting discreetly as a lender in contravention of accepted bankruptcy principles. Factors for the court's consideration may include: (1) the extent of the golden shareholder's equity ownership; (2) the correlation between profit for the golden shareholder and profit for the company; (3) the parties' voting rights outside of bankruptcy; (4) the reasonableness of the business justifications for blocking the bankruptcy filing; and (5) the length of time separating the attainment of the equity interest and the distribution of money to the company.[300] After weighing all the particularized facts in a given case, the bankruptcy court can rely on its discretion as a court of equity to make a determination about whether a federal common law fiduciary duty should arise as a result of the creditor's actions as a golden shareholder.

V. CONCLUSION

The creation of a federal common law fiduciary duty owed by golden shareholders that block corporate debtors from filing bankruptcy provides the most promising solution to the golden shares dilemma. The longstanding federal policy of liberal access to the bankruptcy system must be safeguarded.[301] At the same time, a shareholder being a creditor should not neutralize their rightful role in corporate decision-making.[302]

298. 11 U.S.C. § 301(a).

299. *See Heritage*, 679 F.3d at 139–40.

300. *See* Radwan, *supra* note 14, at 599–600.

301. *See In re* Intervention Energy Holdings, LLC, 553 B.R. 258, 263 (Bankr. D. Del. 2016). Professor Markell notes that, in addition to the *Intervention Energy* court's explanation of the federal policy being guarded by prohibiting contractual bankruptcy waivers, there are other theoretical grounds on which the policy may well be defended. These include "protection of the fresh start" and "ensur[ing] that the federal bankruptcy scheme is always available as a matter of preemption over state law." Bruce A. Markell, *Fool's Gold?: Opting Out of Bankruptcy by Manipulating State Entity Law*, 36 No. 8 BANKR. L. LETTER 1 (2016).

302. *See In re* Franchise Servs. of N. Am., Inc., 891 F.3d 198, 208 (5th Cir. 2018) ("There is no prohibition in federal bankruptcy law against granting a preferred shareholder the right to prevent a voluntary bankruptcy filing just because the shareholder also happens to be an unsecured creditor by virtue of an unpaid consulting bill.").

The implementation of a federal common law fiduciary duty alongside a burden-shifting framework enables the bankruptcy court to exercise its equitable powers in determining whether a decision to oppose a bankruptcy filing is in the best interest of the business or the creditor that poses as a shareholder. The facts in *Intervention Energy* and *Franchise Services* represent the extreme variation in potential corporate and lending relationships that may arise in a restructuring.[303] Neither a blanket prohibition nor a total acceptance of golden shares would further the goals of the bankruptcy system. Thus, justice and equity in the bankruptcy system would be best served by striking the kind of balance a federal common law fiduciary duty could offer.

303. *See* discussion *supra* Part II.