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BANKRUPTCY - CALIFORNIA

In re Venoco LLC

United States Court of Appeals, Third Circuit - May 24, 2021 - F.3d - 2021 WL 2067331

Liquidating trustee appointed under confirmed Chapter 11 plan of debtors, entities that had operated leased offshore oil and gas drilling rig and owned onshore refining facility, filed adversary complaint seeking to recover, on inverse condemnation theory, compensation from the State of California and its Lands Commission for the alleged taking of debtors' refinery.

State defendants moved to dismiss based on, inter alia, sovereign immunity. The United States Bankruptcy Court for the District of Delaware denied motions, and defendants were granted leave for partial interlocutory appeal. The District Court affirmed. Defendants appealed.

The Court of Appeals held that:

- Liquidating trustee's claims were brought to effectuate the bankruptcy court's in rem jurisdiction and were thus claims as to which the state had waived its immunity from suit by ratifying the Bankruptcy Clause of the United States Constitution;
- State defendants forfeited the argument they had immunity from liability when they failed to raise it in the Bankruptcy Court; and
- Even if they had not forfeited argument, state defendants were not actually immune from liability under California law.

Although states can generally assert sovereign immunity to shield themselves from lawsuits, bankruptcy proceedings are one of the exceptions; by ratifying the Bankruptcy Clause of the United States Constitution, states waived their sovereign immunity defense in proceedings that further a bankruptcy court's exercise of its jurisdiction over property of the debtor and its estate, also known as "in rem jurisdiction."

Adversary proceeding in which liquidating trustee appointed under debtors' confirmed Chapter 11 plan sought to recover, on inverse condemnation theory, compensation from State of California and its Lands Commission for alleged taking of debtors' oil refinery was brought to effectuate the bankruptcy court's in rem jurisdiction and was thus claim as to which state had waived its Eleventh Amendment immunity from suit by ratifying Bankruptcy Clause of United States Constitution; though form of action resembled claim for money damages, its function was to decide property rights and so it furthered court's exercise of jurisdiction over property of debtors and their estates, under the circumstances court's in rem jurisdiction extended to estate property transferred to trust for purpose of liquidation and distribution to debtors' creditors, and over which court retained substantial control under the plan, and proceeding also furthered equitable distribution of estate's assets.

In adversary proceeding in which liquidating trustee appointed under debtors' confirmed Chapter 11 plan sought to recover, on inverse condemnation theory, compensation from State of California and its Lands Commission for alleged taking of debtors' oil refinery, both State and Commission could be sued in California courts for their alleged violation of the Takings Clause under the United States or

California Constitutions, and so they were not actually immune from liability under California law.

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