Uniformity Requirement; Equitable Mootness; Scope of the Automatic Stay; Tax Refund Allocation; Finality of Orders Denying Stay Relief; Appointments Clause; Effect of Rejection; Good Faith Violations of the Discharge Injunction; Standards of Appellate Review; Pass-Through Transfers; the Fraud Discharge Exception; and Structured Dismissals: *Siegel v. Fitzgerald*; *City of Chicago v. Fulton; Rodriguez v. FDIC; Ritzen Group, Inc. v. Jackson Masonry, LLC; Financial Oversight and Management Board for Puerto Rico v. Aurelius Investment, LLC; Mission Product Holdings, Inc. v. Tempnology, LLC*; *Taggert v. Lorenzen*; *U.S. Bank Nat'l Assoc. v. Village at Lakeridge*; *Merit Management Group LP v. FTI Consulting, Inc.*; *Lamar, Archer & Cofrin, LLP. v. Appling*; and *Czyzewski v. Jevic Holding Corp.*

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During the current 2021-2022 term, the Supreme Court has granted certiorari in *Siegel v. Fitzgerald*, no. 21-441 (2022), a case involving the scope of the Uniformity Requirement of the Bankruptcy Clause. Once again, it was asked to review the doctrine of Equitable Mootness, which (once again) it declined to take up. During the 2020-2021 term, the Supreme Court decided *City of Chicago v. Fulton*, 141 S. Ct. 585 (2021), addressing a profound circuit split over whether the automatic stay applies to so-called "passive" creditor conduct. During the 2019-2020 term, the Supreme Court decided *Rodriguez v. FDIC*, 140 S. Ct. 713 (2020), addressing whether, in determining how to allocate a tax refund among affiliated corporations, federal courts properly look to state law or federal common law; *Ritzen Group, Inc. v. Jackson Masonry, LLC*, 140 S. Ct. 582 (2020), addressing whether a bankruptcy court's order denying relief from stay is final for appellate purposes; and *Financial Oversight and Management Board for Puerto Rico v. Aurelius Investment, LLC*, 139 S. Ct. 2735 (2020), addressing whether the appointment of the members of the oversight board overseeing the restructuring of Puerto Rico's finances violated the

Appointments Clause of the federal Constitution. During the 2018-2019 term, the Supreme Court decided *Mission Product Holdings, Inc. v. Tempnology, LLC*, 139 S. Ct. 1652 (2019), addressing the effect of rejection in bankruptcy; and *Taggart v. Lorenzen*, 139 S. Ct. 1795 (2019), addressing good faith violations of the bankruptcy discharge. During the 2017-2018 term, the Supreme Court decided *U.S. Bank Nat'l Assoc. v. Village at Lakeridge*, 138 S. Ct. 960 (2018), addressing appellate standards of review; *Merit Management Group LP v. FTI Consulting, Inc.*, 138 S. Ct. 883 (2018), addressing the avoidability of pass-through transfers; and *Lamar, Archer & Cofrin, LLP. v. Appling*, 138 S. Ct. 1752 (2018), addressing the fraud discharge exception. During the 2016-2017 term, the Supreme Court decided *Czyzewski v. Jevic Holding Corp.*, 137 S. Ct. 973 (2017), addressing structured dismissals in Chapter 11 cases. This paper examines these issues and decisions.

A. Siegel and the Uniformity Requirement of the Bankruptcy Clause

The Bankruptcy Clause authorizes Congress to enact "uniform laws" on the subject of bankruptcies. U.S. Const. art. I, § 8, cl. 4. A question that has divided the circuit courts is whether the Chapter 11 fees charged in districts supervised by the United States Trustee program, as compared to the different fees charged in districts supervised by the Bankruptcy Administrator Program, violate the Uniformity Requirement. Two circuits have held that it does, and three have held that it does not. *See United States Trustee Region 21 v. Bast Amron LLP (In re Mosaic Mgmt. Grp., Inc.)*, 22 F.4th 1291 (11th Cir. 2022)(no); *In re Clinton Nurseries, Inc.*, 998 F.3d 56 (2d Cir. 2021) (yes); *Seigel v. Fitzgerald* (*In re Circuit City Stores, Inc.)*, 996 F.3d 156 (4th Cir. 2021) (no); *Mater of Buffets, L.L.C.*, 979 F.3d 366 (5th Cir. 2020) (no); *In re John Q. Hammons Fall 2006, LLC,* no. 20-3203 (10th Cir. October 5, 2021) (yes).

The federal judiciary is divided into ninety-four judicial districts, most of which have a bankruptcy court (the Eastern and Western Districts of Arkansas share a bankruptcy court; the judicial districts for the Virgin Islands, Northern Mariana Islands, and Guam do not have bankruptcy courts). The Department of Justice, through the U.S. Trustee Program, supervises bankruptcy proceedings in eighty-eight of these districts. The Judicial Conference, through its Bankruptcy Administrator Program, supervises six districts located in Alabama and North Carolina.

The two systems are funded in different ways. The Bankruptcy Administrator Program is funded from the general judicial budget supervised by the Judicial Conference. The U.S. Trustee Program is funded from the budget supervised by the Department of Justice funded from fees that debtors pay. As is relevant to the controversy, Chapter 11 debtors pay quarterly disbursement fees based on the size of the quarterly disbursements they make to creditors. At first, Congress imposed these fees only in the districts supervised by the United States Trustee Program. In 1994, however, the Ninth Circuit ruled that imposing a different and more costly system on debtors everywhere but in Alabama and North Carolina violated the Uniformity Requirement. *See St. Angelo v. Victoria Farms, Inc.*, 38 F.3d 1525 (9th Cir. 1994). In response, Congress allowed the Judicial Conference to charge fees in districts supervised by the Bankruptcy Administrator Program equivalent to those charged in all the other districts.

For many years, the fees charged in the different districts were the same. In 2017, however, Congress mandated increased quarterly Chapter 11 disbursement fees for large debtors in districts supervised by the U.S. Trustee Program. These changes were designed to cover shortfalls in funding for the program. This raised the fees from a maximum of $30,000 to the lesser of either $250,000 or one percent of the quarterly disbursements. Beginning on and after January 1, 2018,

the fees increased accordingly for all large Chapter 11 debtors in districts supervised by the U.S. Trustee Program, even if these debtors' cases were already pending. Large Chapter 11 debtors in districts supervised by the Bankruptcy Administrator Program were charged less. First, the Judicial Conference did not increase the quarterly fees for these debtors until October of 2018, and, second, the increase did not apply to pending cases. Thus, in districts supervised by the Bankruptcy Administrator Program, large Chapter 11 debtors with cases pending before October of 2018 incurred no increased fees regardless of how long their cases remained pending.

As noted, two courts of appeals have concluded that this disparate system violates the Uniformity Requirement; three have concluded that it does not. The Court granted certiorari in the Fourth Circuit case (*Seigel v. Fitzgerald,* no. 21-441) on January 10, 2022.

B. Equitable Mootness

Orders confirming Chapter 11 plans are characteristically final orders subject to immediate appellate review. In the absence of a stay pending appeal, however, debtors are generally free to substantially consummate their plans, including by transferring assets, borrowing funds, and making distributions to creditors. In some cases, appellate relief seeking to alter the treatment of a particular claim, the disposition of assets, the order confirming the plan, or other orders of the bankruptcy court, may be infeasible or inequitable owing to its effects on third parties. If so, the appellate court may deny relief under the court-created doctrine of "equitable mootness." *See, e.g., In re Envirodyne Indus., Inc.*, 29 F.3d 301, 304 (7th Cir. 1994) (Posner, J.) (equitable mootness "is perhaps best described as merely an application of the age-old principle that in formulating equitable relief a court must consider the effects of the relief on innocent third parties."); *see also Search Market Direct, Inc. v. Jubber (In re Paige)*, 584

F.3d 1327, 1335 (10th Cir. 2009) ("[T]he doctrine of equitable mootness is rooted, at least in part, in the court's discretionary power to fashion a remedy in cases seeking equitable relief."); *In re AOV Indus., Inc.*, 792 F.2d 1140, 1147–48 (D.C. Cir. 1986) ("[T]here exists … a melange of doctrines relating to the court's discretion in matters of remedy and judicial administration. Even when the moving party is not entitled to dismissal on [A]rticle III grounds, common sense or equitable considerations may justify a decision not to decide a case on the merits.").

The doctrine traces its origins to *Trone v. Roberts Farms, Inc. (In re Roberts Farms, Inc.),* 652 F.2d 793 (9th Cir. 1981). In that case, the bankruptcy court confirmed a plan of arrangement under Chapter XI of the Bankruptcy Act of 1898 over the objection of a creditor, Trone. After Trone appealed to the district court, the appellees moved to dismiss the appeal as moot. After the district court granted the motion, Trone appealed to the Court of Appeals for the Ninth Circuit. By that time, the plan had been substantially consummated. In dismissing the appeal as moot, the Ninth Circuit reasoned as follows:

> Here the many intricate and involved transactions … were contemplated by the plan of arrangement (even to and including liquidation and reorganization of the debtor corporation) and stand solely upon the order confirming the plan of arrangement for court approval and confirmation of the transactions. Were we to deny the motion to dismiss for mootness and on consideration of the merits reverse the order of the District Court, what would be the result? Are we not quite patently faced with a situation where the plan of arrangement has been so far implemented that it is impossible to fashion effective relief for all concerned? Certainly, reversal of the order confirming the plan of arrangement, which would knock the props out from under the authorization for every transaction that has taken place, would do nothing other than create an unmanageable, uncontrollable situation for the Bankruptcy Court.

652 F.2d at 797.

In 1996, the Third Circuit applied the doctrine in its *en banc* decision in *In re Continental Airlines*, 91 F.3d 553 (3d Cir. 1996) (*en banc*). In approving the doctrine, the court recognized that its application typically rests on the consideration of several factors:

> Factors that have been considered by courts in determining whether it would be equitable or prudential to reach the merits of a bankruptcy appeal include (1) whether the reorganization plan has been substantially consummated, (2) whether a stay has been obtained, (3) whether the relief requested would affect the rights of parties not before the court, (4) whether the relief requested would affect the success of the plan, and (5) the public policy of affording finality to bankruptcy judgments.

Id., at 560. Dissenting from this decision, then-Judge Alito reasoned that the doctrine had been applied too broadly—well-beyond (in his view) any legitimate justification. *See id.*, at 570 (Alito, J., dissenting). Echoing then-Judge Alito's view, the doctrine has been criticized more recently as an abrogation of the federal courts' "virtually unflagging obligation" to hear appeals within their jurisdiction. *In re One2One Commc'ns, LLC*, 805 F.3d 428, 433 (3d Cir. 2015); *In re Charter Commc'ns, Inc.*, 691 F.3d 476, 481 (2d Cir. 2012). Under this line of reasoning, dismissing an appeal on equitable mootness grounds "should be the rare exception." *In re Tribune Media Co.*, 799 F.3d 272, 288 (3d Cir. 2015); *In re Pac. Lumber Co.*, 584 F.3d 229, 240 (5th Cir. 2009) (the doctrine of equitable mootness should be applied "with a scalpel rather than an axe").

Although every court of appeals has applied the doctrine in one form or another, there are differences in the particular tests they apply. *Compare R2 Investments, LDC v. Charter Communications, Inc.,* 691 F.3d 476, 481 (2d Cir. 2012) (reciting Second Circuit's five-part test),[1]

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[1] The court explained: "In this circuit, an appeal is presumed equitably moot where the debtor's plan of reorganization has been substantially consummated. . . . . The presumption of equitable mootness can be overcome, however, if … five … factors are met:

> (1) 'the court can still order some effective relief';
>
> (2) 'such relief will not affect the re-emergence of the debtor as a revitalized corporate entity';
>
> (3) 'such relief will not unravel intricate transactions so as to knock the props out from under the authorization for every transaction that has taken place and create an unmanageable, uncontrollable situation for the Bankruptcy Court';
>
> (4) 'the parties who would be adversely affected by the modification have notice of the appeal and an opportunity to participate in the proceedings'; and

with Samson Energy Resources Company v. Semcrude, L.P. (In re Semcrude, L.P.), 728 F.3d 314, 321 (3d Cir. 2013) ("it is useful to think of equitable mootness as proceeding in two analytical steps: (1) whether a confirmed plan has been substantially consummated; and (2) if so, whether granting the relief requested in the appeal will (a) fatally scramble the plan and/or (b) significantly harm third parties who have justifiably relied on plan confirmation."). In addition, some courts have limited the doctrine to orders confirming Chapter 11 plans. *See, e.g., In re LCI Holding Company, Inc.*, 802 F.3d 547, 554 (3d Cir. 2015); *In re Sneed Shipbuilding, Inc.*, 916 F.3d 405, 409 (5th Cir. 2019). Others, including those in the Second, Fourth, Ninth, Tenth, and Eleventh Circuits, have applied it more broadly. *See, e.g., In re Windstream Holdings, Inc.*, 838 Fed. App'x. 634 (2d Cir. 2021) (dismissing as equitably moot an appeal of a "critical vendor" order directing the payment of the prepetition claims of vendors deemed essential to the success of a Chapter 11 debtor's reorganization before the claims of other unsecured creditors following confirmation of the debtor's Chapter 11 plan); *Myers v. Offit Kurman, P.A.*, 773 F. App'x 161, 162 (4th Cir. 2019) (dismissing as equitably moot an appeal from a bankruptcy court order granting a Chapter 7 trustee's motion for approval of a settlement agreement where the agreement had been fully consummated and the funds had been distributed accordingly); *Stokes v. Gardner*, 483 F. App'x 345, 346 (9th Cir. 2012) (dismissing appeal of an order approving a settlement agreement in a Chapter 7 case as equitably moot); *Ordonez v. ABM Aviation, Inc.*, 787 F. App'x 533 (10th Cir. 2019) (dismissing as equitably moot debtor's appeal from a

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> (5) 'the appellant pursued with diligence all available remedies to obtain a stay of execution of the objectionable order if the failure to do so creates a situation rendering it inequitable to reverse the orders appealed from.'

Id., at 481(quoting *Frito-Lay, Inc. v. LTV Steel Co. (In re Chateaugay Corp.)*, 10 F.3d 944, 952 53 (2d Cir. 1993)).

bankruptcy court order relating to a Chapter 7 trustee's settlement of the debtor's employment discrimination claims where the debtor did not diligently seek a stay, the settlement agreement had been fully consummated, the funds had been distributed, the estate had been fully administered, and the debtor's challenges were not compelling); *In re JMC Memphis, LLC*, 655 F. App'x 802 (11th Cir. 2016) (dismissing as equitably moot an appeal from an unstayed order approving a settlement between the Chapter 7 trustee and the debtor's insurer).

In *In re Nuverra Environmental Solutions, Inc.*, 834 Fed. App'x 729 (3d Cir. 2021), a divided panel of the Third Circuit dismissed as equitably moot an appeal of a "gifting" Chapter 11 plan—one in which a senior class "gifts" a portion of its recovery to a junior class as a means of achieving a consensual confirmation, but the effect is unequal treatment among unsecured creditors or one that permits a subordinate class to be paid ahead of a class entitled to a higher priority. A creditor filed a petition for a writ of certiorari on July 6, 2021 seeking review of the doctrine, which the Court denied. *See Hargreaves v. Nuverra Environmental Solutions Inc.*, No. 21-17 (U.S.). In addition, the Court on October 4, 2021 denied a petition seeking review of the Second Circuit's equitable mootness decision in *Windstream*. Given the frequency with which petitions seeking review of the doctrine have been filed in recent years, it is likely the Court will eventually take up the issue.

C. Fulton and the Scope of the Automatic Stay

Section 362 of the Bankruptcy Code generally prevents a creditor from seizing the debtor's or estate property after the filing of the debtor's bankruptcy case. But what if the creditor has already seized the property before the filing? Does the automatic stay prevent the creditor from continuing to hold onto the seized property? Like many other courts of appeals, the Seventh

Circuit held that it does. *See, e.g.*, *Weber v. SEFCU (In re Weber)*, 719 F.3d 72 (2d Cir. 2013); *Thompson v. Gen'l Motors Acceptance Corp., LLC*, 566 F.3d 699 (7th Cir. 2009); *Knaus v. Concordia Lumber Co. (In re Knaus)*, 889 F.2d 773 (8th Cir. 1989); *State of California Emp. Dev. Dep't v. Taxel (In re Del Mission Limited)*, 98 F.3d 1147 (9th Cir. 1996); *In re Rozier*, 376 F.3d 1323 (11th Cir. 2004). Other circuits, however, have gone the other way. *See, e.g., In re Cowen*, 849 F.3d 943, 950 (10th Cir. 2017).

A leading case adopting and illustrating the majority approach was the Second Circuit's decision in *Weber*. In *Weber*, the debtor financed his truck with a loan from a creditor. 719 F.3d at 74. Under the terms of the loan agreement, the debtor granted a lien on the truck to the creditor to secure repayment of the loan, which lien permitted the creditor to "repossess Weber's vehicle upon default." *Id.* After the debtor defaulted, the creditor repossessed the vehicle. Four days later, the debtor filed a chapter 13 bankruptcy petition. *Id.* Notably, repossession of the vehicle did not divest the debtor of his ownership interest in the truck; it simply permitted the creditor to possess the vehicle pending foreclosure. Thus, when the debtor filed for bankruptcy, the truck became property of the debtor's bankruptcy estate notwithstanding the creditor's possession. Following the Supreme Court's analysis in *United States v. Whiting Pools*, Inc., 462 U.S. 198 (1983), the Second Circuit held that, upon the bankruptcy filing, the creditor had a duty to turn over the vehicle to the estate. *See id.* at 79. It further held that the creditor's passive failure to do so constituted a violation of the automatic stay as an act to "'exercise control' over the property of the estate." *Id.* at 79 (quoting 11 U.S.C. § 362).

The Second Circuit focused its analysis on the fact that, by retaining possession of the truck, the creditor was impermissibly exercising control over estate property. *Id.* at 79-80. But the court also found support for its holding in the 1984 amendments to the Bankruptcy Code, which

"broadened the already sweeping provisions of the automatic stay even further to prohibit expressly not only 'acts to obtain possession' of property of the estate, but also 'any act . . . to exercise control over the property of the estate.'" *Id.* at 80 (citing Pub. L. No. 98-353, 98 Stat. 333, 371). The court viewed this expansion as a further effort to ensure that the debtor's property is handed over for orderly bankruptcy administration. *Id.* Citing precedent from the Seventh Circuit, the court stated that, "[a]lthough Congress did not provide an explanation of that amendment, the mere fact that Congress expanded the provision to prohibit conduct above and beyond obtaining possession of an asset suggests that it intended to include conduct by creditors who seized an asset pre-petition." *Id.* (quoting *Thompson*, 566 F.3d at 702). Any other outcome, the Second Circuit determined, would "place on the debtor or trustee the burden of undertaking a series of adversary proceedings to pull together the bankruptcy estate"—an outcome inconsistent with the Supreme Court's decision in *Whiting Pools* and the turnover provisions of section 542. *Id.*

The Second Circuit's reference to *Whiting Pools* was relevant because, in *Whiting Pools*, the Court explained that, for bankruptcy purposes, it is immaterial whether a creditor obtains property of the estate before or after bankruptcy is filed. *See Whiting Pools*, Inc., 462 U.S. at 203-05, 209 (1983) ("We conclude that the reorganization estate includes property of the debtor that has been seized by a creditor prior to the filing of a petition for reorganization."). That is so, the Court reasoned, because "[b]oth the congressional goal of encouraging reorganizations and Congress' choice of methods to protect secured creditors suggest that Congress intended a broad range of property to be included in the estate." *Id*. at 204. The Court then emphasized: "The Bankruptcy Code provides secured creditors various rights . . . and these rights *replace* the protection afforded by possession." *Id*. at 207 (emphasis added). Critically, the kind of conduct

this Court identified as *within* the reach of, and modified by, the Code—mere possession of property of the estate—is precisely the kind of "passive" conduct the court below concluded falls *outside* the scope of the automatic stay.

A leading case adopting the minority approach was *In re Cowen*, 849 F.3d 943, 950 (10th Cir. 2017). In *Cowen*, the Tenth Circuit held that, after the debtor filed his bankruptcy petition, a creditor's passive act of retaining property seized before the bankruptcy filing did not violate the stay. In reaching its conclusion, the court acknowledged that the majority rule, adopted by most of the Courts of Appeals to have addressed the issue, is that a creditor's passive conduct may indeed violate the stay. *Id*. at 948-49. Rejecting the majority approach, the court stated that "we adopt the minority rule: only affirmative acts to gain possession of, or to exercise control over, property of the estate violate [the stay]." *Id*. at 950.

Prior to Fulton's filing of her Chapter 13 bankruptcy case, the City of Chicago impounded her vehicle after discovering that she had been driving on a suspended license. After Fulton filed her bankruptcy case, she demanded the return of her car. Asserting that Fulton owed the City $11,831.20 in connection with 54 separate and outstanding violations, the City refused. The bankruptcy court, however, determined that the City's refusal to return the car violated the automatic stay, citing *Thompson v. General Motors Corp.*, 566 F.3d 699 (7th Cir. 2009), and ordered the return of her vehicle. In three other cases involving similarly situated debtors, the City likewise was directed to return impounded vehicles. The City appealed these decisions directly to the Seventh Circuit, which affirmed in all four instances.

Adhering to prior circuit precedent, the court of appeals ruled that the City's retention of the debtor's property following the debtor's bankruptcy case constituted an "act to . . . exercise control" over the property within the meaning of section 362(a)(3). According to the Seventh

Circuit, the debtor need not bring an action demanding turnover of the vehicle to prevail; section 362 itself prohibits the continued retention of the property. Recognizing that its decision was contrary to a decision of the Tenth Circuit on the same issue, the Seventh Circuit nonetheless observed that its holding was in line with decisions of the Second, Eighth, and Ninth Circuits (the Eleventh Circuit had likewise adopted the majority view). After the Seventh Circuit issued its decision in the case, the Third Circuit joined the Tenth Circuit in concluding that the automatic stay does not prevent a creditor from continuing to hold onto property seized prior to the debtor's bankruptcy filing (the D.C. Circuit also follows this approach). The Supreme Court granted certiorari on December 18, 2019.

In its briefs filed in the Supreme Court, the City and its amici contended that the Seventh Circuit misconstrued section 362(a)(3), observing that the statute does not simply prevent the exercise of control over the debtor's property, but more pointedly "any act" to exercise control over the property. The City contended that the "passive" activity of holding onto property is not an "act" within the meaning of the statute. In addition, the City argued, section 362(a)(3) must be read in context with other provisions of the Code, particularly section 542 governing turnover and section 363 requiring the provision of adequate protection to protect the creditor's interest. According to the City, the Seventh Circuit's approach would render section 542 largely meaningless—a debtor need not seek turnover, but merely have the creditor held in contempt for violating the stay. It would also erode the adequate protection requirement, the City contended, by allowing the debtor to obtain the property without necessarily ensuring the protection of the creditor's interest, forcing the creditor to seek relief from stay.

In contrast, Fulton and her amici contended that the activity of holding onto seized property is as much an "act" as seizing the property itself. Likewise, they contended, the City's argument

misconstrues the relationship between sections 362 and 542 by suggesting that turnover is an exclusive remedy if property is not in the debtor's possession. Turnover is certainly available to require parties to transfer property to the estate, but nothing in section 542 indicates that it is exclusive. And once property is returned to the estate, a creditor may seek relief from stay, including on grounds of lack of adequate protection. The creditor, however, is not entitled to short-circuit that process by retaining the property. Oral argument was conducted on October 13, 2020, and a decision was issued on January 14, 2021.

Reversing the Seventh Circuit, the Supreme Court concluded that the "mere" activity of holding onto seized property did not constitute "an act" within the meaning of section 362(a)(3), and thus did not violate the automatic stay. The Court based its reasoning on several considerations.

First, the Court observed that the term "act" typically connotes some kind of assertive conduct. That is certainly true. But in ordinary English, holding onto something is also plainly an "act." Perhaps more important, creditors that retain seized vehicles after the debtor files for bankruptcy rarely just hold onto the vehicle. In the ordinary course, they also characteristically refuse to give the vehicle back, prevent the debtor from gaining access to it, employ someone to watch over it, and either implicitly or explicitly continue to hold onto the vehicle as a means to leverage the payment of a debt. In conducting its analysis, the Court refused to consider any of these additional activities. In a footnote, the Court observed that, in one of the cases, the Bankruptcy Court had determined that by retaining the debtor's car *and* demanding payment, "the City also had violated §§362(a)(4) and (a)(6)." The Court stated, however, that the Court of Appeals did not address these considerations and, thus, "[n]either do we." The Court concluded:

"We hold only that mere retention of estate property after the filing of a bankruptcy petition does not violate §362(a)(3) of the Bankruptcy Code."

Relatedly, the Court also avoided considering the meaning of the phrase "any act" by reference to how the phrase is used in other parts of section 362. The phrase "any act" appears repeatedly throughout the various subsections of section 362, including section 362(a)(4), which enjoins "any act to create, perfect, or enforce any lien against property of the estate." Among other things, section 362(a)(4) codifies the ancient principle that liens cannot attach to property *in custodia legis*—in the custody of the court. This includes property of the bankruptcy estate, which is constituted in the custody of the federal bankruptcy court. This principle applies regardless of whether the creditor attempts to create the lien "actively" or whether the lien is created "passively" simply by operation of non-bankruptcy law—the lien simply cannot attach.

In figuring out whether the City's activity of continuing to hold onto the car constituted "an act" to exercise control over property of the estate, one might have thought that the Court would have looked to how the phrase "any act" is used across section 362 to fathom Congress's intent. Specifically, one might have thought that the Court would have taken a close look at how the phrase is used in the very next subsection—section 362(a)(4). Instead, the Court purposefully avoided parsing the meaning of the same phrase in other parts of the same section.

Second, the Court invoked the canon of construction that disfavors surplusage. The Court's concern here was about the overlapping scope of sections 362 and 542, and in particular its concern that if section 362 were interpreted to require the City to return the seized property then that would leave little work for section 542 to perform. But as the Court acknowledged, there would still be at least *some* work for section 542, such as by specifying to whom the property was to be returned. So the canon would not seem technically to apply. What the Court did not address clearly was the

same concern in reverse: If the City's conduct does not violate section 362(a)(3), what work does the phrase "exercise control over property of the estate" actually perform? The Court's cryptic remark was that this language was added simply to deal with "intangible" property.

The Court's focus on the overlapping nature of sections 362 and 542 is also somewhat odd for a different reason. Overlapping remedies are an everyday occurrence in law, especially commercial law. Think of the various ways creditors may seek to collect on unpaid debts. Under UCC Article 9, secured creditors may pick and choose between a variety of redundant and overlapping remedies, and no one would think twice about curtailing them because the exercise of one renders redundant the exercise of another. *See* UCC § 9-625. Rather, they are simply understood to be cumulative options at the creditors' disposal.

Third, the Court was concerned that, if section 362 were interpreted to require the return of the vehicles, a conflict would arise between sections 362 and 542 owing to the exception in section 542 excusing turnover if the property is of inconsequential value. But it is hard to see this as a real problem. After all, section 362 is not fully self-executing. Typically, if the debtor or trustee wishes the return of seized property, the debtor or trustee will send a letter to the creditor. If the creditor refuses, then the parties may go to court and the court may enforce the statutory provisions by directing the creditor to cease violating the automatic stay. Obviously, if the property is of inconsequential value, that letter will not be sent and the controversy will never be joined.

Fourth, the Court was reluctant to discuss the practical consequences of its decision. In a concurring opinion, however, Justice Sotomayor did just that. Although she agreed that the City's retention of the debtors' cars did not violate "the letter of the Code," she concluded that it nonetheless "hardly comports with its spirit." She then went on to elaborate how cumbersome,

time consuming, and expensive it can be for debtors or trustees to pursue turnover actions under section 542. As she observed, turnover actions can easily take over one hundred days to prosecute and "[o]ne hundred days is a long time to wait for a creditor to return your car, especially when you need that car to get to work so you can earn an income and make your bankruptcy plan payments." This, she noted, is inconsistent with the Code's fundamental policy of providing the debtor with a "fresh start," which all acknowledge section 362 aims to promote. Given Justice Sotomayor's elaboration of the Code's purpose in this context, it seems improbable that Congress intended the consequences that the Court's decision yields, namely forcing debtors to pursue time-consuming and expensive turnover proceedings when the outcome will generally be the same—the creditor must give the car back.

Finally, the Court based its analysis in part on the observation that section 362 is essentially an injunction, and injunctions are often designed to maintain the *status quo*, not alter it. In ordinary terms, it is true that injunctions are often used to maintain the *status quo*. But that is not their only use—as the Court was undoubtedly aware. Injunctions may also be fully remedial, and section 362 is plainly a remedial provision.

D. Rodriguez and the Proper Allocation of Tax Refunds

The IRS allows affiliated groups of corporations to file consolidated tax returns. Under applicable IRS regulations, when a refund is owing, the IRS generally pays the refund to the group's designated agent and the IRS's payment to the agent discharges its payment obligation. But how then is the refund to be allocated among members of the group? Affiliated corporate groups frequently enter into tax allocation agreements specifying which members of the group are responsible for paying what part of the group's tax liability, and likewise how to allocate any

refund. But what if there is no such agreement in place or the members of the group dispute its provisions? Absent IRS regulation, should the courts resort to state law to resolve these disputes or follow some principle of federal common law?

Addressing this question, some courts followed what came to be known as the "*Bob Richards*" rule, so-named after the decision of the Ninth Circuit that adopted it: *In re Bob Richards Chrysler-Plymouth Corp.*, 473 F.3d 262 (1973). Under this federal common-law approach, absent a tax allocation agreement, the refund properly belongs to the group member responsible for the losses that led to it. Further expanding the rule, some courts applied it even when the parties had a tax allocation agreement in place.

Rodriguez involved two affiliated entities: United Western Bank ("United Western") and its parent, United Western Bancorp, Inc. ("UWP"). Notably, the parties had a tax allocation agreement. After suffering substantial losses, United Western was placed into receivership with the FDIC as receiver. Shortly thereafter, UWP was forced into bankruptcy, with Simon Rodriguez appointed as trustee. After the IRS issued a refund, Rodriguez and the FDIC both claimed the money. Unable to resolve their differences, they litigated the matter in the bankruptcy court, district court, and Tenth Circuit. Applying the more expanded version of the *Bob Richards* rule, the Tenth Circuit ruled in favor of the FDIC.

Not all courts, however, followed the *Bob Richards* rule. In order to address this methodological disagreement, the Supreme Court granted certiorari on June 28, 2019. Concluding that there was no need for a federal common-law rule in this instance, the Court vacated the decision of the Tenth Circuit. Remarking that the role of judicial lawmaking in the federal courts is modest at best, the Supreme Court observed that the creation of federal common-law rules must be *necessary* to protect uniquely federal interests. With respect to the collection of taxes, the Court

observed that the federal government may well have a vital interest in how it receives the revenue and from whom. But with respect to the allocation of a tax refund among affiliated corporations, no unique federal interest is present and the matter should be resolved through the application of relevant principles of state law.

E. Ritzen and the Finality of Orders Denying Relief from Stay

Under 28 U.S.C. § 158(a), an appeal as of right lies from "final judgments, orders, and decrees" entered by bankruptcy judges "in cases and proceedings." A bankruptcy judge's order is considered "final" when it resolves a "discrete dispute" within the larger bankruptcy case. As the Supreme Court ruled in *Bullard v. Blue Hills Bank*, 575 U.S. 496 (2015), whether an order resolves a discrete dispute turns on the context in which the dispute is decided. For example, although an order confirming a plan finally resolves a discrete dispute, an order denying confirmation of a plan does not—at least not where the case continues because, absent dismissal, another plan could be filed and thus the plan confirmation process has not yet concluded. What about an order denying relief from stay? Does that involve the resolution of a sufficiently discrete dispute? In *Ritzen Group, Inc. v. Jackson Masonry, LLC*, the Supreme Court answered in the affirmative.

Prior to Ritzen's bankruptcy filing, it was embroiled in a breach-of-contract dispute with Jackson over the sale of some real estate that Jackson owned. After a year of litigation, and just days before trial was to begin, Jackson filed its Chapter 11 case. Ritzen filed a motion for relief from stay to allow it to continue the state-court litigation. After a hearing, the bankruptcy court denied the motion. Thereafter, Ritzen filed a proof of claim, Jackson objected, and the bankruptcy court ruled in Jackson's favor on Ritzen's breach-of-contract theory and disallowed Ritzen's claim.

Thereafter, Ritzen appealed both the bankruptcy court's adverse ruling on its claim as well as the bankruptcy court's denial of its motion for relief from stay.

On appeal, the district court held that Ritzen's appeal from the bankruptcy court's ruling denying relief from stay was untimely—Ritzen should have filed its notice of appeal within 14 days after the bankruptcy court entered its stay-relief order. With respect to the bankruptcy court's resolution of the breach-of-contract claim, the district court ruled against Ritzen on the merits. On further appeal, the Sixth Circuit affirmed. As to timeliness, the court reasoned that the automatic stay proceeding qualified as sufficiently "discrete" for purposes of finality. The court also affirmed the district court on the merits of the breach-of-contract claim. On May 20, 2019, the Supreme Court granted certiorari to review the timeliness question. Affirming the Sixth Circuit, the court reasoned that a bankruptcy court's order dispositively ruling on a motion for relief from stay is immediately final and appealable.

The Court began by observing how the finality analysis differs in bankruptcy. In ordinary civil litigation, a final order is usually one that ends the litigation as a whole, leaving nothing more for the trial court to do except execute the judgment. In bankruptcy, however, things are different. As the Court observed in *Bullard*, bankruptcy cases typically encompass a multitude of discrete proceedings, many of which would exist as stand-alone lawsuits. The question becomes whether the order in question resolves a dispute that is sufficiently discrete. Figuring that out, the Court observed, requires the proper delineation of the relevant bankruptcy "proceeding" for purposes of finality.

The Court considered two conflicting propositions: (1) Jackson's argument that stay-relief litigation involves is its own discrete proceeding, and (2) Ritzen's claim that the stay-relief litigation in question was simply the first step in determining Ritzen's claim—the relevant

proceeding involved the adjudication of Ritzen's breach-of-contract dispute, which was not over until the bankruptcy court ruled on the merits of the claim. As Ritzen observed, the stay-relief question at issue simply involved where its claim would be litigated: in state court or in the bankruptcy court. Ordinarily, orders that deny the transfer of litigation from one court to the next are not final until the end of the litigation. Rejecting Ritzen's argument, the Court concluded that the relief-from-stay process is itself sufficiently discrete that orders denying a motion for relief from stay are properly final.

F. Financial Management and Oversight Board and the Appointments Clause

In 2016, Congress enacted the Puerto Rico Oversight, Management, and Economic Stability Act ("PROMESA"). Among other things, PROMESA created a Financial Oversight and Management Board entrusted with supervising the restructuring of Puerto Rico's financial affairs, including representing Puerto Rico in bankruptcy proceedings and overseeing aspects of Puerto Rico's fiscal and budgetary policies. PROMESA provides that the President appoints the seven members of the Board without the advice and consent of the Senate (*i.e.*, Senate confirmation). The question was whether that authorization violated the Appointments Clause of the federal Constitution, which states that the President, with the advice and consent of the Senate, shall appoint "Ambassadors, others public Ministers and Consuls, Judges of the supreme Court, and all other *Officers of the United States* . . . ." Art. II, § 2, cl. 2 (emphasis added). The specific question was whether the members of the Board constituted "Officers of the United States" within the meaning of the provision.

After the commencement of Puerto Rico's bankruptcy proceedings, several creditors moved to dismiss the case on the ground that the Board has been improperly constituted. After

the bankruptcy judge denied their motions, the creditors appealed to the First Circuit, which reversed on the basis that the selection of the Board's members did indeed violate the Appointments Clause. On June 20, 2019, the Supreme Court granted certiorari. On June 20, 2020, it reversed the First Circuit.

In conducting its analysis, the Court found it necessary to reconcile the Appointments Clause with a different set of constitutional provisions: those that empower Congress to create local offices for the District of Columbia and for the Territories of the United Stated, including Puerto Rico. *See* Art. I, § 8m cl. 17; Art. IV, § 3, cl. 2. As the Court observed, the term "Officials of the Unites States" has never been understood to cover local officials appointed under these additional provisions. The question became whether the members of the Board are, on balance, local territorial officials. Reasoning that the Board's duties were indeed local in nature, the Court concluded that the Appointments Clause did not apply in this instance.

In reaching its conclusion, the Court first observed that Congress enacted PROMESA under Article IV of the Constitution, which governs its authority to legislate for the Territories. Although federal personnel acting in Puerto Rico could fall within the scope of the Appointments Clause, territorial officials that have primarily local powers and duties are not "Officials of the United States." As the Court observed, Puerto Rico pays the Board's expenses. The Board's ability to issue subpoenas is subject to limits on personal jurisdiction enforceable under Puerto Rico law. The Board works with the elected government of Puerto Rico and controls the issuance of new debt for Puerto Rico. The Board was authorized to initiate bankruptcy proceedings for Puerto Rico and its instrumentalities in the same manner as any other local government. All told, these indicate the local nature of the duties of the Board. Accordingly, the appointments were proper.

G. Tempnology and the Effect of Rejection

Section 365 of the Bankruptcy Code permits a trustee (or debtor-in-possession) in a bankruptcy case to reject an executory contract. The question raised in *Tempnology* is the effect of rejection. Does it simply mean that the trustee (or debtor) is excused from performing the contract and liable in damages for breach? Or does it also mean that the contract is effectively rescinded, taking away any rights it might have conferred on the non-rejecting party? The First Circuit concluded that the effect in the case was essentially to terminate the non-breaching party's rights.

Before filing for bankruptcy, Tempnology, LLC developed and patented certain cooling fabrics for use in athletic apparel and accessories. Tempnology granted a non-exclusive license to Mission Product Holdings to use Tempnology's marks and an exclusive right to distribute Tempnology's patented products within a certain territory. After Tempnology filed for bankruptcy, it rejected its agreement with Mission, planning to relicense the technology and distribute its products on more favorable terms. Mission argued that Tempnology's rejection of the contract did not terminate Mission's right to use the marks and distribute the products; it simply constituted breach of the agreement. Tempnology contended that rejection did indeed terminate Mission's rights, leaving Tempnology free to do business with someone else. As noted, the First Circuit agreed with Tempnology. On Mission's petition for certiorari, the Supreme Court granted review limited to the first question raised in the petition: whether rejection of a license agreement terminates the rights of the licensee. The Court declined review of Mission's second question:

whether an exclusive right to sell is a right to intellectual property protected under section 365(n) of the Code.

This is not the first time that a court of appeals has ruled that the effect of rejection is to rescind an agreement, depriving the non-rejecting party of its rights. In 1985, the Fourth Circuit ruled in the *Lubrizol* case that the debtor's rejection of a technology license stripped the licensee of its right to use the technology. *See Lubrizon Enterprises, Inc. v. Richmond Metal Finishers, Inc.*, 756 F.2d 1043 (4th Cir. 1985). In response to *Lubrizol*, Congress swiftly enacted section 365(n), which provides that, when a debtor rejects a license of "intellectual property," the licensee may nonetheless opt to retain its right to use the relevant technology. The trouble, however, lies in the Code's definition of "intellectual property." The phrase includes patents and copyrights, but does not mention trademarks. Some have interpreted this to mean that trademarks are not protected and that rejection does indeed rescind the licensee's rights. Others have contended that section 365(n) represents a broad repudiation of *Lubrizol* and that licensees of trademarks are protected to the same extent as licensees of patents and copyrights, with the failure to include trademarks within the definition of intellectual property as perhaps just an oversight. Still others have contended that *Lubrizol* was simply wrong and that the only consequence of rejection is that the agreement is breached (as section 365(g) expressly provides); the licensee's right to continue using the mark is not ended regardless of what section 365(n) provides.

In its merits brief, Mission raised essentially three arguments why its rights were not terminated. First, it contended that, as section 365(g) expressly provides, rejection constitutes breach, not rescission, with only the ordinary consequences of breach. Notably, it argued that rejection is not an avoidance concept and thus cannot give the debtor greater rights than it would

have outside of bankruptcy. Thus, its rights as a licensee are not terminated. Mission faulted the First Circuit for failing to apply these basic principles.

Second, Mission argued that rejection of the agreement did not otherwise revoke any of its licensing rights under the agreement, including its exclusive right to distribute the patented product and its non-exclusive right to use the Tempnology marks, because these are essentially forms of property rights that rejection does not reach. In making this argument, Mission construed both its right to use the Tempnology marks and its right to sell the Tempnology product as types of technology licenses (a characterization rejected by the First Circuit, which concluded that Mission's right to sell was simply the right of an ordinary distributor). Specifically, Mission argued that its exclusive right to sell encompassed the right to sell products "practicing Tempnology's patents and bearing its trademarks."

Third, Mission contended that section 364(n) does not support the inference that, because trademarks are not expressly included in the definition of "intellectual property," therefore they are not protected. Mission argued that there is no reason to treat trademarks differently from patents and copyrights. Finally, Mission argued that the reorganization policies of Chapter 11 do not justify treating rejection as an avoidance power.

In its merits brief, Tempnology presented essentially three responses. First, it contended that the treatment of Mission's exclusive right to sell was outside the singular question that the Court accepted for review. According to Tempnology, its agreement with Mission distinguished Mission's non-exclusive license to use Tempnology's intellectual property and Mission's exclusive product distribution rights. Tempnology noted that the Court had granted review only with respect to Mission's rights as a licensee and the effect of rejection thereon, and not with respect to Mission's additional question concerning its distribution rights. Tempnology contended

further that, if Mission's distribution rights were not at issue, the case is moot because Mission's non-exclusive license to use Tempnology's intellectual property expired in 2016.

Assuming a live controversy, Tempnology next argued that a rejected contract is unenforceable against the debtor's estate, except to the extent the Bankruptcy Code otherwise provides. As a result, once a contract is rejected, the non-rejecting party's only recourse is to assert a claim for damages, not the debtor's performance of its obligations. Because Congress has not granted licensees of trademarks any special remedies, Mission's only remedy is to assert a claim for damages for breach. According to Tempnology, this is supported by the reality that the non-rejecting party to a rejected agreement has no right to have its claim treated as one entitled to administrative priority. In support of its position, Tempnology also argued that Mission's exclusive right to distribute Tempnology products is not a property right; it is simply a contract right to sell products that Tempnology manufactures, that incorporate Tempnology's patented processes or materials, or that bear the Tempnology marks. Nothing in section 365 protects such distribution rights.

Third, Tempnology argued that there are good reasons to treat trademarks differently from other kinds of intellectual property protected under section 365(n). Unlike patents and copyrights, trademarks and the goodwill accompanying them must always be owned by a single owner, who has the right to exercise control over the nature and quality of the relevant goods or services covered by the mark. A licensee simply does not acquire the rights of an owner, and thus does not acquire a property right in the same sense as the licensee of a copyright or patent. That is especially so where, as here, the licensee holds a non-exclusive license. In addition, Tempnology argued that treating Mission's rights in the manner endorsed by the First Circuit was essential to facilitate the reorganization of businesses like Tempnology.

Numerous amici filed briefs supporting Mission's position. Two amicus briefs were filed in support of neither party. No amicus brief was filed in support of Tempnology. Oral argument was conducted on February 20, 2019. On May 20, 2019, the Supreme Court issued its opinion reversing the First Circuit.

The Court began by addressing the effect of rejection, specifically whether it constitutes a breach of the agreement giving rise to a claim for damages, or whether it has the effect of rescission. Concluding that rejection merely has the effect of breach, the Court reasoned that Tempnology's rejection in this case did not terminate any of Mission's rights. In reaching its conclusion, the Court observed that the power to reject a contract is not the power to avoid a non-debtor party's rights, and that a debtor may not effectively use its authority to reject a contract to expand its own rights. Nor did the Court believe that, when Congress specifically intervened after *Lubrizol* to protect patent and copyright interests, its failure to mention trademarks meant Congress intended debtors to be able to circumvent those rights. That argument, the Court reasoned, paid too little attention to the main provisions governing rejection (*e.g.*, that it constitutes a breach) and too much to subsidiary provisions (*e.g.*, section 365(n)) specifying further details in particular cases in response to specific problems that required legislative correction (*e.g.*, *Lubrizol*). It might be true, the Court observed, that permitting a debtor to use rejection to terminate the rights of a non-debtor party might assist with the debtor's reorganization. It is likewise true, the Court noted, that one of the main goals of bankruptcy is to facilitate reorganization. Nonetheless, the Court stated, the Code "does not permit anything and everything that might advance that goal."

H. Taggart and the Effect of Good Faith in Addressing Violations of the Discharge Injunction

Section 524(a) provides that the grant of a discharge in a bankruptcy case "operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any [discharged] debt as a personal liability of the debtor, whether or not discharge of such debt is waived . . . ." 11 U.S.C. § 524(a). Respondents (a group of individuals) sued petitioner (Taggart) in state court for wrongfully transferring their interests in a limited liability company without honoring their right of first refusal. On the eve of trial, Taggart filed for Chapter 7 bankruptcy relief and ultimately obtained a discharge. Thereafter, Taggart sought to be dismissed from the state-court litigation, owing to the discharge granted in his bankruptcy case. The trial court, however, refused, determining that Taggart was a necessary party, even though the parties had agreed not to pursue a money judgment against him. After respondents prevailed at trial, they sought attorneys' fees from Taggart, arguing that his post-bankruptcy participation in the case fell outside the reach of the discharge injunction.

In response, Taggart moved to reopen his bankruptcy case and sought to hold respondents in contempt for violating the discharge injunction. The issue was simultaneously litigated in both state and federal court. Ultimately, various courts determined that respondents had indeed violated the discharge injunction. The bankruptcy court in particular found the violation to be willful and determined (as is relevant here) that there is no "good faith belief" defense. The court awarded $5,000.00 in noneconomic damages and approximately $105,000.00 in fees and costs that Taggart had incurred. The court also added $2,000.00 in punitive damages for respondents' failure to timely vacate the state-court judgment against Taggart.

On appeal, the bankruptcy appellate panel reversed, concluding that the bankruptcy court had erred in determining that respondents' subjective or good faith beliefs were irrelevant. On

further appeal, the Ninth Circuit affirmed the bankruptcy appellate panel, concluding that respondents could not be held in contempt because they believed in good faith that the discharge injunction was inapplicable. According to the Ninth Circuit, a creditor's good faith belief excuses a violation of the discharge injunction, even if the creditor's belief is unreasonable. Because it was uncontested that respondents possessed a good faith belief that the discharge injunction did not apply to their claims, their belief, even if unreasonable, protected them from contempt. In seeking certiorari review, Taggart contended that the Ninth Circuit's standard conflicts irreconcilably with that of the Eleventh Circuit as set forth in various cases, including *In re Hardy*, 97 F.3d 1384 (11th Cir. 1996), in which the court concluded that relief is available for violations of the discharge injunction irrespective of the creditor's good faith. Taggart likewise contended that the Ninth Circuit's standard conflicts with decisions from the First and Fourth Circuits. The Court granted certiorari on January 4, 2019.

On June 3, 2019, the Court issued its decision reversing the Ninth Circuit. Rejecting both a "strict liability approach," and likewise the Ninth Circuit's standard that effectively excused a violation if the creditor has a subjective "good faith belief" that the discharge order does not apply to the creditor's conduct, the Court instead adopted a different test: a creditor may be held in civil contempt for violating the discharge injunction if "there is no fair ground for doubt as to whether the order barred the creditor's conduct." Rephrasing its standard, the Court explained: "[i]n other words, civil contempt may be appropriate if there is no objectively reasonable basis for concluding that the creditor's conduct might be unlawful."

In reaching its conclusion, the Court began by considering sections 524 of the Code, which "operates as an injunction" to prevent debt-collection activity with respect to discharged obligations, and section 105, which authorizes a court to "issue any order, process, or judgment

that is necessary or appropriate to carry out the provisions of this title." 11 U.S.C. §§ 105(a), 524(a). Applying the canon that, when a statutory term is transplanted from another legal source, it "brings the old soil with it," the Court concluded that these provisions, drawn generally from the law of injunctions, should be interpreted in a manner consistent with how injunctions are generally enforced.

As the Court noted, injunctions are generally enforceable through civil contempt. And in general, civil contempt is warranted only when there is "no fair ground for doubt" as to the wrongfulness of the defendant's conduct. Observing that this standard is an objective one, the Court rejected the Ninth Circuit's subjective approach. As the Court reasoned, the absence of willfulness does not excuse civil contempt. The Court concluded: "[u]nder the fair ground of doubt standard, civil contempt therefore may be appropriate when the creditor violates a discharge order based on an objectively unreasonable understanding of the discharge order or the statutes that govern its scope."

I. Village at Lakeridge and Appellate Standards of Review

In a Chapter 11 cram-down case, if a class of claims is impaired, at least one impaired class must vote in favor of the plan in order for the plan to be confirmed, excluding insider votes. 11 U.S.C. § 1129(a)(10). The Code defines insiders to include various persons (known as statutory insiders), but the list is not exhaustive. Others who are sufficiently close to the debtor may also be deemed to be insiders (known as non-statutory insiders). The issue the Supreme Court took for consideration is *not* the resolution of various disputes over the correct test for determining whether a creditor is a non-statutory insider, but rather the standard of review that an appellate court should use in reviewing the decision of a bankruptcy court applying the relevant criteria (whatever they

are) to the facts of the case to determine whether the creditor is a non-statutory insider. Ordinarily, courts of appeals review questions of law *de novo*, and questions of fact under the clearly erroneous standard. When it comes to applying the law to the facts, however, some courts have characteristically reviewed the bankruptcy judge's *application* of the law to the facts (assuming the bankruptcy judge has stated the legal test correctly) under the clearly erroneous standard, while others have reviewed it *de novo*.

The facts of the case are colorful. MBP Equity Partners was the equity owner of the Village at Lakeridge, the debtor. U.S. Bank held an approximately $10 million claim against Lakeridge secured by a mortgage lien. MBP held an unsecured claim against Lakeridge in the amount of approximately $2.76 million. Lakeridge proposed to confirm a cram down plan that impaired the rights of U.S. Bank and needed at least one impaired class to vote in favor of the plan, but the claim it held was obviously the claim of an insider. So MBP, acting through one of its board members (Ms. Bartlett), sold its claim to an investor (Dr. Rabkin) for $5,000. Ms. Bartlett and Dr. Rabkin were romantically involved.

The bankruptcy court determined that Dr. Rabkin was not a non-statutory insider. The bankruptcy appellate panel reversed, and the Ninth Circuit reversed the bankruptcy appellate panel. The Ninth Circuit reasoned that it reviewed the bankruptcy court's determinations of fact under the clearly erroneous standard, and its conclusions of law *de novo*. Classifying the bankruptcy court's application of the law to the facts as falling within the scope of its clearly erroneous review, a majority of the three-judge panel concluded that the decision was not clearly erroneous (the bankruptcy court having more or less stated the correct legal standard).

In the Supreme Court, U.S. Bank argued that the bankruptcy judge's application of the law to the facts should be reviewed *de novo*, just like questions of law generally. U.S. Bank contended

that, among other things, doing so offers important law-clarifying benefits. Lakeridge argued that the bankruptcy judge's application of the law to the facts should be reviewed under the clearly erroneous standard, just like pure questions of fact. Lakeridge argued that the application of the legal standard to the facts is essentially like determinations of fact that the bankruptcy judge is in the best position to assess. The United States filed an amicus brief siding with Lakeridge.

At oral argument, the Justices asked a number of far-ranging questions about method, the capacity of appellate judges to conduct appellate review, and the practical implications of one standard over the other. In rendering its decision, the Court decided for the debtor (and the United States), concluding that a clear error standard applied.

In conducting its analysis of the legal issue of what standard of review properly applies, the court first differentiated three distinct kinds of inquiry: those that are purely legal (*i.e.*, what is the relevant legal rule or test), those that are purely factual (*i.e.*, what happened in the case of relevance to that test), and those that that are a combination of the two (*i.e.*, how is the law to be applied to the particular facts). On the first question, the Court noted (without deciding its merits) that the Ninth Circuit applies a two-part test for non-statutory insider status: whether the person's relationship with the debtor was similar to those listed as statutory insiders, and whether the relevant transaction had been conducted at less than arm's length. The Court took this standard as the given test in deciding the case. Ordinarily such questions are reviewed *de novo*, but the Court did not grant certiorari on this purely legal question. Accordingly, the Court did not decide its merits (although several justices stated in concurrence that they doubted the Ninth Circuit's test was correct).

On the second question, the Court observed that the bankruptcy court made numerous "basic" or "historic" findings of facts regarding what actually happened in the case. The Court

noted that the set of relevant facts in any particular instance will turn on the legal test used. In this case, the relevant factual determinations included those surrounding Rabkin's relationship with Bartlett, such as whether they lived together or paid each other's living expenses, and Rabkin's motives for purchasing the claim against the debtor. The Court observed that such determinations are ordinarily reviewed on appeal under the clearly erroneous standard, which affords great deference to the trial court's findings.

On the third question, which was the real bone of contention, the Court characterized the inquiry as involving so-called "mixed questions" of law and fact. Essentially, the third question involves considering whether the facts satisfy the legal test chosen for the resolution of the matter. As noted, the bankruptcy court had determined that the facts did not show the kind of transaction necessary to confer insider status. The question the Court was called up to answer was whether this determination should be reviewed *de novo* or for clear error.

The Court observed that, in general, there is no clear-cut answer to this question because mixed questions of law and fact are not all alike. Sometimes they require a court to expound on the law, such as when they require the elaboration of a legal standard. In such instances, the Court reasoned that appellate courts should review the trial court's determination *de novo*. In other instances, however, the determination is much more intensely factual. In such instances, the Court determined that appellate courts should review the trial court's determination under the highly deferential clearly erroneous rule.

In this case, the Court held that the determination of Rabkin's insider status under the relevant legal test was about as fact-bound as it gets. The nature of the inquiry was such that the bankruptcy court was required to take a raft of case-specific facts and make a determination of whether, on balance, they showed that the parties were acting more like strangers or more like

insiders. Conversely, the Court reasoned that, in making its determination, the bankruptcy court was required to do relatively little legal work (other than selecting the correct legal standard). Rather, the bankruptcy court's work essentially involved characterizing the totality of the facts.

The Court's decision thus leaves it up to the lower appellate courts to figure out in each case what is more predominant in the application of the law to the fact—the law or the facts. In some instances, this is likely to be relatively straightforward. In others, it is likely to be more complex. For example, if the law is relatively unsettled, and the application of the law to the facts requires significant illustration of the kinds of things the law is intended to encompass, one would imagine the appellate court opting for *de novo* review. In more run-of-the mill cases in which factual analysis predominates, however, the appellate court is likely to opt for the clear error standard.

J. Merit and Pass-Through Transfers Under Section 546(e)

Section 546(e) of the Bankruptcy Code renders unavoidable a transfer "by or to (or for the benefit of)" a financial institution. 11 U.S.C. § 546(e). The issue addressed in the case is whether a transfer that simply passes through a financial institution is insulated from avoidance, or whether the section protects only those transfers in which a financial interest holds a beneficial interest. The Seventh Circuit, following the Eleventh Circuit, ruled that the section shelters only those transfers in which the financial institution holds a beneficial interest, and not where the financial institution serves merely as a conduit. In contrast, the Second, Third, Sixth, Eighth, and Tenth Circuits have held to the contrary.

The facts of the case, although layered, are straightforward. Valley View, the debtor, wanted to establish a racing track and casino in Pennsylvania, for which it needed both a racing

license and a gaming license. Valley View was in competition with Bedford Downs for the last racing license in the state when the two decided to combine forces through a leveraged buyout in which Valley View agreed to buy the stock of Bedford Downs with borrowed funds from Credit Suisse and other lenders. The purchase money was escrowed at Citizens Bank. Merit Management, the owner of approximately thirty percent of Bedford Downs, surrendered its stock to Citizens Bank in exchange for approximately $16.5 million.

Unable to obtain a gaming license, Valley View filed for bankruptcy in 2009. FTI Consulting, as trustee under the litigation trust tasked with pursuing Valley View's avoidance actions, brought suit against Merit Management in Illinois under sections 544, 548, and 550 of the Bankruptcy Code. FTI's theory was that the $16.5 million transfer to Merit Management was a fraudulent conveyance. Merit Management argued that section 546(e) rendered the transfer unavoidable on the basis of the involvement of Credit Suisse as lender and Citizens Bank as escrow agent. The district court ruled in favor of Merit Management and FTI appealed to the Seventh Circuit.

The Seventh Circuit reversed. It determined that the relevant text of section 546(e) is ambiguous. It analogized the situation to one in which a person sends a postcard through the U.S. Postal Service. On the one hand, the sender can be thought of as sending the card by or through the mail. On the other hand, the postal service can be thought of as doing the sending. Because the language is ambiguous, the court looked to the section's history and purpose, as well as other indicia of meaning.

In particular, the court traced the history of section 546 through the course of three amendments. The first, in 1982, added protection for margin and settlement payments involving commodity brokers, forward contract merchants, stock brokers, and securities clearing agencies.

The second, in 1984, added financial institutions to the list. The third, in 2006, added the "(or for the benefit of)" language. After reviewing the history, the court reasoned that the intent was to protect the named parties with respect to transfers in which they have a beneficial interest, not simply in situations in which they serve merely as conduits for others. The court acknowledged that its decision deepened a pre-existing circuit split.

The Supreme Court granted certiorari to address the conflict among the courts of appeals. In the Supreme Court, Merit Management understandably focused heavily on the text of section 546(e), contending that it literally applied to the relevant transfer in question. In contrast, FTI understandably focused on the history and purpose of the section, as well as its place in context with other provisions of the Code. During oral argument, Justice Ginsburg was particularly interested in the fact that Merit Management is not a financial institution. Justice Kagan inquired whether the focus ought to be on the transfer being avoided, rather than the path the transfer took. The justices otherwise asked a number of pointed questions about section 546(e) and its operation.

In affirming the Seventh Circuit, the Court nonetheless began by rejecting the lower court's determination that the statutory language is ambiguous. After summarizing the avoidance powers generally, the Court then turned to the limitations on those powers set forth in section 546(e). After quoting the section, the Court reviewed its history, particularly the various amendments adding various provisions, culminating in the current text. With that as background (and after summarizing the facts) the Court identified the relevant question as whether "the transfer between Valley View and Merit implicates the safe harbor exception because the transfer was 'made by or to (or for the benefit of) a . . . financial institution.'" *Merit*, 138 S. Ct. at 892. In answering this question, the Court reasoned that it first had to identify the nature of the relevant transfer. Rejecting Merits' argument that it should look at each component part of the transfer individually,

the Court concluded that, as FTI argued, there was, in fact, only one overarching transfer—that between Valley View and Merit for $16.5 million. Because that transfer was not made by, to, or for the benefit of a financial institution, the safe harbor did not apply. The Court determined that this conclusion followed from the language of section 546(e), the context in which it is used, and the broader statutory structure of which section 546(e) is a part.

Beginning with the text, the Court reasoned that the very first clause of section 546(e)—"Notwithstanding sections 544, 545, 547, 548(a)(1)(B), and 548(b) of this title"—suggests that the relevant inquiry is on the transfer the trustee seeks to avoid—here the $16.5 million from Valley View to Merit. Likewise the very last clause—"except under section 548(a)(1)(A) of this title"—suggests the same thing because it creates an exception to the exception for an actually fraudulent transfer, again focusing on the transfer in question that the trustee is seeking to avoid. Further supporting its interpretation, the Court noted that the statutory text provides that a transfer the "trustee may not avoid" is designated in as "a transfer that *is*" either a settlement payment or made in connection with a securities contract. The Court considered relevant that the statutory language did not say "a transfer that involves" or that "is connected with" such things, but rather a transfer that "is" those things—further supporting its conclusion that what matters is the transfer the trustee is seeking to avoid, not its component parts.

The Court then turned to the relevant statutory structure. Here it adopted the reasoning of the Seventh Circuit—namely, that the system for avoiding transfers, together with the safe harbor from avoidance, are logically two sides of the same coin. Notably, the avoidance provisions designate the characteristics of transfers the trustee may avoid. Likewise, the safe harbor exception logically does the same. There is no reason, the Court concluded, "to examine the relevant

component parts when considering a limit to the avoiding power, where that limit is defined by reference to an otherwise avoidable transfer, as is the case with § 546(e) . . . ." *Id*., at 894-95.

In conducting its analysis, the Court also rejected Merit's argument that the phrase "(or for the benefit of)" added to section 546(e) in 2006 was intended to overrule the Eleventh Circuit's decision in *In re Munford, Inc.*, 98 F.3d 604, 610 (11th Cir. 1996), which held that the safe harbor was inapplicable to transfers in which a financial institution was only an intermediary. The Court reasoned that nothing in the text or its legislative history corroborated that proposition, and likewise that there was a simpler explanation: a number of avoidance provisions use this same language, so it made sense that Congress would add it to section 546(e) so that the provisions all matched. The Court likewise rejected Merit's argument that its interpretation was compelled by reference to the purpose of the safe harbor. Merit argued that section 546(e) was intended as a broad and comprehensive protection. The Court concluded, however, that Merit's purposive argument was unavailing because it conflicted with the plain language of the statute.

K. Lamar and the Fraud Discharge Exception

Section 523(a)(2)(A) excepts from discharge "any debt . . . for money, property [or] services . . . to the extent obtained by . . . false pretenses, a false representation, or actual fraud, *other than a statement respecting the debtor's . . . financial condition*." 11 U.S.C. § 523(a)(2) (emphasis added). If the creditor claims a debt should not be discharged under this provision owing to a false or fraudulent statement regarding the debtor's financial condition, section 523(a)(2)(B) additionally requires that the statement must be in writing and that the creditor must show the debtor's intent to deceive. In other words, there are heightened requirements for the non-dischargeabilty of a debt based on a statement respecting the debtor's financial condition. The

issue in the case is whether a debtor's statement regarding a tax refund that the debtor anticipated receiving is a statement respecting the debtor's financial condition such that the additional requirements apply, or whether it is simply a statement regarding a particular asset that otherwise falls within the scope of section 523(a)(2)(A).

The creditor in the case is a law firm that did work for the debtor. After the firm became concerned that the debtor was not paying his bills, the firm inquired about the debtor's ability to pay. The debtor represented orally that he was going to get a large tax refund. In fact, the tax refund that the debtor anticipated receiving was less than he represented and, when the debtor received it, he used it to pay other debts, leaving the firm unpaid. After the debtor filed for bankruptcy relief, the firm moved to have its claim determined to be non-dischargeable. The bankruptcy and district courts ruled for the firm. The Eleventh Circuit, however, ruled in favor of the debtor. On certiorari review, the Supreme Court affirmed the Eleventh Circuit.

In reaching its decision, the Court zeroed in on the meaning of the phrase "statement respecting the debtor's financial condition." The Court asked: "Does a statement about a single asset qualify, or must the statement be about the debtor's overall financial condition?" The Court reasoned that the answer to this question matters because the statement at issue was just about a single asset—the tax refund. The Court concluded that the relevant statutory language, particularly the term "respecting," makes it plain that a statement about a single asset can be a "statement respecting the debtor's financial condition." Accordingly, if the statement is not in writing, the associated debt may be discharged, even if the statement was untrue.

The Court began by observing that, one of the main purposes of the Nation's bankruptcy laws is "to aid the honest but unfortunate debtor by giving him a fresh start in life, free from debts, except of a certain character." *Lamar*, 138 S. Ct. at 1758 (citations and marks omitted). In order

to decide if the debt in this case is of such a "certain character," the Court determined that it had to closely examine the relevant text of section 523(a)(2) to see what it includes and excludes. The Court began its analysis by observing that there was no dispute regarding the meaning of the terms "statement" or "financial condition." What matters is the meaning of the "key word" that appears between these terms in the statutory text: the word "respecting." Rejecting Lamar's narrow reading of the term, the Court concluded that there was no basis to believe that the term had a meaning materially different from "about," "concerning," "with reference to," or "as regards." Because a statement regarding a single asset can be about or concerning or with reference to or as regards a debtor's financial condition, such a statement can also be one respecting a debtor's financial condition. Noting that the Court typically reads the word "respecting" broadly, it saw no reason to depart from that tradition in this setting—particularly where it concluded that adopting a more restricted interpretation would lead to anomalous results.

In further support of its analysis, the Court cited the legislative history. The relevant language has long been a part of the fraud discharge exception, and courts of appeals have long concluded that the language encompasses statements addressing just one or some of a debtor's assets or liabilities. Applying the canon that, when Congress uses the same language in a statute through multiple recodifications it presumably is aware of and intends to retain the judicial interpretations of it, the Court reasoned that this further bolstered its plain reading analysis. Finally, the Court rejected Lamar's argument that Appling's interpretation undermines the purpose of section 523(a)(3), or the general principle that bankruptcy relief is available only to the honest but unfortunate debtor. The Court noted that section 523(a)(2) attempts to balance debtor relief against a history of creditor abuse. As the Court observed, some finance companies had historically encouraged their borrower's falsity for the purpose of insulating their claims from

discharge in bankruptcy. The Court's advice: creditors should ensure that the debtor's statements on which they rely in extending credit are in writing.

L. Jevic and Structured Dismissals

The Bankruptcy Code authorizes the dismissal of Chapter 11 bankruptcy cases and generally provides that, unless the court for cause orders otherwise, dismissal has the effect of returning the parties to the status quo immediately prior to the commencement of the case. *See* 11 U.S.C. §§ 349, 1112. Rather than return the parties to the status quo, however, some courts have approved "structured dismissals" that effectively distribute the value of the debtor's assets in various ways, approve the release of various parties, and/or settle various claims. These structured dismissals may or may not comply with the Code's priority rules. The question presented in *Jevic* was whether a structured dismissal that did not comply with absolute priority is something a bankruptcy court is authorized to approve and, if so, under what circumstances.

Jevic Transportation was in the trucking business. Prior to filing for bankruptcy, Jevic engaged in a leverage buyout transaction in which Sun Capital Partners acquired the company. Various lenders led by CIT financed the buyout and provided Jevic with an $85 million revolving line of credit. After Jevic's finances continued to deteriorate, the company decided to file for bankruptcy. It ceased operations, notified its employees of their impending termination, and commenced a Chapter 11 proceeding in Delaware. At the time, Jevic owed its lenders and Sun approximately $53 million secured by liens on the company's assets. It owed an additional $20 million to taxing authorities and general unsecured creditors. An official committee of unsecured creditors was appointed.

After the commencement of the bankruptcy case, a group of Jevic's terminated truck drivers filed a class action against Jevic and Sun, alleging violations of federal and state WARN acts, under which Jevic was supposed to provide 60 days' written notice before laying them off. In addition, the creditors' committee brought a fraudulent transfer action against CIT and Sun, alleging that Sun, with CIT's help, took over Jevic with essentially none of its own money in an ill-conceived transaction that placed Jevic in an unreasonably precarious financial position.

Several years later, the bankruptcy court granted in part and denied in part CIT's motion to dismiss the litigation. Thereafter, representatives of the committee, Sun, CIT, Jevic, and the drivers convened to negotiate a settlement. Previously, all of Jevic's assets had been liquidated to pay the lender group led by CIT. By the time of the settlement discussions, all that was left of Jevic was about $1.7 million in cash, which was subject to Sun's lien, and the fraudulent transfer action against CIT and Sun.

Eventually the committee, Jevic, CIT, and Sun reached a settlement agreement with four essential features. First, the parties would release each other, and the fraudulent transfer litigation would be dismissed. Second, CIT would pay $2 million to fund the payment of administrative expenses. Third, Sun would assign its lien on the $1.7 million in cash to pay tax and administrative creditors first, and then to distribute something to general unsecured creditors. Fourth, the bankruptcy case would be dismissed. In this way, the settlement contemplated a structured dismissal that provided for the distribution of Jevic's remaining assets. It left out, however, the drivers, who had asserted approximately $8.3 million in wage claims entitled to priority under section 507(a)(4) of the Code. Apparently the drivers had been unable to reach a settlement against Sun on their WARN act claims, and Sun was unwilling to agree to any distribution to the drivers so long as their litigation against Sun remained pending.

The drivers and the U.S. Trustee objected to the proposed settlement and structured dismissal. In particular, they claimed that the dismissal violated the Code's priority scheme by authorizing a distribution to general unsecured creditors while the drivers' priority wage claims received nothing. Rejecting these arguments, the bankruptcy court approved the settlement and the structured dismissal. The court reasoned that other courts has granted similar relief in other cases. The court also observed that dire circumstances existed and that, absent the settlement, there was no meaningful prospect of any distribution to anyone other than the secured creditors because completing a Chapter 11 bankruptcy was impractical, as was conversion to a Chapter 7 case. In essence, there was no cash available to fund any further bankruptcy proceedings because all of the available cash was encumbered by Sun's lien.

Although the bankruptcy court observed that Chapter 11 plans cannot violate absolute priority over the objection of creditors, it concluded that there was no similar restriction for settlements. The court found that the drivers' claims against Jevic were essentially worthless because there was no unencumbered cash that could be distributed to them. On appeal, the district court affirmed, as did the Third Circuit, which held that, in rare instances such as the present case, courts could approve structured dismissals. The Third Circuit believed that, in this case, there was no real alternative and observed that, although structured dismissals might not be used simply to evade the Code's procedural protections and safeguards, there was in this matter no prospect of either a confirmable plan or a viable Chapter 7 case. In addition, the court determined that, although skipping a priority class in favor of distributions to a junior class raises justifiable concerns, it could be done where there are specific and credible grounds that justify the deviation. In this matter, although the drivers were left out in the cold, the bankruptcy court concluded correctly, the court believed, that the settlement best served the interests of the estate and its

creditors because further litigation would merely deplete the assets of the estate with little prospect of assisting anyone.

In the Supreme Court, the drivers argued that the absolute priority standard applied equally to settlements as well as plans of reorganization. The drivers reasoned that this was essential to effectuate Congress's policy choice in elevating certain creditors over others. Unlike financial creditors, employees are poor loss spreaders, hence their priority treatment, which should be respected.

In addition, the drivers noted, if they could be skipped over in this case, doing so would serve to open the door to further violations of absolute priority in the future. Settling parties, they noted, should not be permitted to get away with deviations from absolute priority simply because they claim they would not settle unless another creditor group is cut out. The drivers warned that, if approved, exceptional deviations from absolute priority would likely become commonplace. This, they contended, would have dire effects for the negotiation of Chapter 11 plans because it would effectively provide a green light for collusion and undermine the kind of predictability that adherence to absolute priority fosters. This, the drivers warned, would effectively marginalize creditors like the drivers in this case, who generally lack the clout of financial creditors.

In contrast, the several respondents argued that the concept of absolute priority does not superintend the approval of settlements. By the Code's terms, they argued, absolute priority has become codified in the confirmation provisions, but not the rules that govern settlements. Moreover, although a plan must comply with the Code's priority regime set forth in section 507, nothing in the Code mandates the same for settlement agreements.

Respondents also focused on the impossibility of alternative relief. Absent a settlement, there was likely to be nothing to distribute to anyone, other than the secured creditors. Simply put,

the settlement was the best vehicle to maximize distributions to creditors. Further, as the bankruptcy court determined, the drivers' claims were essentially worthless because there was essentially no cash available to distribute to them. The distribution to the unsecured creditors simply took funds out of the secured creditors' pockets, so there was no harm to the drivers in any event.

Countering the drivers' policy concerns, respondents argued that siding with the drivers would grant recalcitrant priority creditors too much leverage by encouraging them to demand payment even when doing so would destroy any hope of maximizing value through the settlement process. Although the drivers might have that leverage in the plan process, respondents argued that they do not have it in the settlement context.

Ruling for the drivers, the Supreme Court held that a distribution scheme ordered in the context of a structured dismissal cannot, without the consent of the affected parties, deviate from the ordinary priority rules applicable to distributions under the Bankruptcy Code. The Court noted that the Bankruptcy Code's priority scheme "constitutes a basic underpinning of business bankruptcy law." The Court reasoned that, because of the centrality of this scheme, if Congress had intended to depart from the existing priority rules in the context of the approval of dismissals under section 349, one would expect some affirmative indication of this intent, observing "Congress … does not … hide elephants in mouseholes."

Based on its review of the Code, the Court found nothing demonstrating such intent. Nor did the Court believe that precedent supported respondents' position. The Court distinguished situations in which lower courts have approved *interim* distributions that violate absolute priority where these distributions have served Code-related objectives, including various first-day orders. The Court observed that those kinds of distributions are commonly justified as enabling a

successful reorganization. In contrast, a structured dismissal involves a final disposition that does not serve the same goal. In particular, it does not preserve the debtor as a going concern, offer the prospect of making disfavored creditors better off, promote the possibility of a confirmable plan, restore the status quo, or protect the reliance interests of creditors who have obtained interests during the course of the bankruptcy case.

Finally, the Supreme Court flatly rejected a "rare case" exception based on "sufficient reasons" in particular cases. The Court was blunt in holding that "it is difficult to give precise content to the concept [of] 'sufficient reasons,'" and expressed the concern that a rare case exception could turn into a more general rule. Specifically, the Court stated that "Congress did not authorize a 'rare case' exception …. [and w]e cannot 'alter the balance struck by the statute'… not even in "rare cases."[2]

[2] Justice Thomas authored a dissent, joined by Justice Alito. The dissent noted that the Court had granted certiorari on a particular question, but the Petitioners had argued (and the Court decided) another question. Given the switch, the dissent would have dismissed the writ of certiorari as improvidently granted.