1   IN THE SUPREME COURT OF THE UNITED STATES

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3 CASIMIR CZYZEWSKI, ET AL.,   :

4   Petitioners   :   No. 15-649

5   v.   :

6 JEVIC HOLDING CORP., ET AL.,   :

7   Respondents.   :

8 - - - - - - - - - - - - - - - - - - x

9   Washington, D.C.

10   Wednesday, December 7, 2016

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12   The above-entitled matter came on for oral

13 argument before the Supreme Court of the United States

14 at 10:04 a.m.

15 APPEARANCES:

16 DANIELLE SPINELLI, ESQ., Washington, D.C.; on behalf

17   of the Petitioners.

18 SARAH E. HARRINGTON, ESQ., Assistant to the Solicitor

19   General, Department of Justice, Washington, D.C.; for

20   United States, as amicus curiae, supporting the

21   Petitioners.

22 CHRISTOPHER LANDAU, ESQ., Washington, D.C.; on behalf

23   of the Respondents.

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1   C O N T E N T S

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 1               P R O C E E D I N G S

 2                                      (10:04 a.m.)

 3               CHIEF JUSTICE ROBERTS:  We'll hear argument

 4    this morning in Case 15-649, Czyzewski v. Jevic Holding

 5    Corporation.

 6               Ms. Spinelli.

 7               ORAL ARGUMENT OF DANIELLE SPINELLI

 8                 ON BEHALF OF THE PETITIONERS

 9               MS. SPINELLI:  Mr. Chief Justice, and may it

10    please the Court:

11               Chapter 11 provides one way to distribute

12    estate assets to creditors on account of their

13    prepetition claims through a confirmed plan that adheres

14    to the code's priority scheme.  If a Chapter 11 plan

15    can't be confirmed, the bankruptcy court can convert the

16    case to Chapter 7, which also requires that creditors be

17    paid in order of priority, or it can simply dismiss the

18    case without distributing assets to creditors at all,

19    returning all parties to their prebankruptcy position.

20               No provision of the Bankruptcy Code permits

21    what happened here:  an order dismissing a Chapter 11

22    case that distributed all the estate's assets to

23    creditors, but deliberately skipped over our clients'

24    priority claims.

25               JUSTICE SOTOMAYOR:  May I ask you:  Did the
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1   settlement bar you from suing the debtor for the WARN

2   Act claims?

3   MS. SPINELLI: No, it did not.

4   JUSTICE SOTOMAYOR: And there was no money

5   left to the debtor. So did it bar you from suing Sun

6   Life for a fraudulent transfer, which --

7   MS. SPINELLI: It did.

8   JUSTICE SOTOMAYOR: It did.

9   MS. SPINELLI: It did, Justice Sotomayor,

10   and I think that's -- that's critical. What this

11   settlement did is it took away our client's right to

12   pursue either the debtor or Sun and CIT on account of

13   their undisputed WARN Act claims, which were in the area

14   of $12 million.

15   JUSTICE SOTOMAYOR: All right. In the court

16   below, I understand that the -- that you represented

17   that if this settlement went through, that you would

18   have -- I'm sorry -- that if -- without the settlement,

19   you would really have nothing, because there was no

20   money in the estate.

21   So are you representing that your client

22   intends to sue Sun Life? Because that's the only way to

23   get money here.

24   MS. SPINELLI: Well, let me -- let me

25   respond to that, Justice Sotomayor. There are a few

1   things that could happen if this Court reverses the

2   order below and the case is remanded.

3   JUSTICE SOTOMAYOR: That's fine. Tell me

4   which one you're going to do.

5   MS. SPINELLI: Well, that's really up to the

6   bankruptcy court.

7   JUSTICE SOTOMAYOR: All right. So what do

8   you -- are you going to ask them to do?

9   MS. SPINELLI: What we had asked for before,

10   and what may well make the most sense, is conversion to

11   Chapter 7, in which case either the Chapter 7 trustee

12   could pursue the fraudulent-transfer claim --

13   JUSTICE SOTOMAYOR: But there is no money in

14   the estate to do that. So how will the trustee do that?

15   MS. SPINELLI: The trustee would have to

16   retain contingency counsel, and that does happen. I was

17   involved in a Chapter 7 case where the trustee pursued

18   an avoidance action successfully with contingency

19   counsel.

20   Failing that, if the trustee decided not to

21   do that, after the bankruptcy is over, the

22   fraudulent-transfer claim would revest in the creditors,

23   and our clients could then bring that claim themselves.

24   JUSTICE ALITO: There is a difference --

25   there seems to be a difference between what you have

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 1    said on this point in your briefs and in your argument

 2    this morning and what you told the Third Circuit or what

 3    -- did you -- did your firm represent -- appear in the

 4    Third Circuit?

 5              MS. SPINELLI:  Not until the rehearing

 6    stage.

 7              JUSTICE ALITO:  Well, in the Third Circuit

 8    oral argument, it was said over and over, well, we just

 9    want to make sure that the law is filed -- is followed.

10    That's what we are interested in.

11              Isn't that right?

12              MS. SPINELLI:  We certainly do want to make

13    sure that the law is followed.  I mean, we --

14              JUSTICE ALITO:  If you were pressed as to

15    what practical difference the case meant to you and --

16    and the answer was, we -- you know, we want to uphold

17    the law.

18              MS. SPINELLI:  Justice Alito, I don't

19    believe that's the case.  The case does make a practical

20    difference.  It always has made a practical difference.

21    That's the only reason our clients have been pursuing

22    it.  And the practical difference it makes is that on

23    remand, they will have an opportunity to recover on

24    account of their undisputed WARN Act claims, which, as

25    of now, they're -- they have been deprived of.
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1   JUSTICE ALITO: But can you point to

2   anything you said in the Third Circuit, in writing or

3   orally, that -- along those lines, that you -- that

4   there was some practical course of action that -- that

5   you -- some tangible thing that you were going to

6   pursue?

7   MS. SPINELLI: What we told the Third

8   Circuit is that if this case went back on remand and

9   were converted to Chapter 7, then the

10   fraudulent-transfer action could be pursued. I believe

11   that's what -- that's the argument that we made below.

12   JUSTICE ALITO: Can I ask one other -- one

13   other thing? Something strange seems to have happened

14   between the petition stage and the briefing stage in the

15   case.

16   The question that you asked us to take was

17   whether a bankruptcy court may authorize the

18   distribution of settlement proceeds in a manner that

19   violates the statutory priority scheme. And you said

20   there's a square conflict on that issue, with the Second

21   Circuit and the Third Circuit on one side and the Fifth

22   Circuit on the other side.

23   MS. SPINELLI: Correct.

24   JUSTICE ALITO: And we took the case.

25   But then the question that you address in

1   your brief refers to "structured dismissal." There is

2   nothing about structured dismissal in the question that

3   you asked us to take, and there is no conflict on the

4   question of structured dismissal, is there?

5   MS. SPINELLI: And, Justice Alito, we're not

6   asking this Court to decide the question of whether

7   structured dismissals are valid. We did not change the

8   substance of the question presented here.

9   JUSTICE ALITO: Now, you're not asking us to

10   decide the broad question whether there can ever be a

11   structured dismissal. But you are asking us to decide

12   whether the priorities have to be followed in a

13   structural dismissal, and unless the answer to that

14   question follows from the answer to the question that

15   you presented in your petition, you have changed the

16   question that you have asked us to decide.

17   MS. SPINELLI: We did not change the

18   substance of the question presented. In the petition,

19   we had a paragraph of background explaining that this

20   was done through a structured dismissal. We then asked

21   the question, does the Bankruptcy Code -- may a

22   bankruptcy court authorize the distribution of

23   settlement proceeds in a manner that violates the Code's

24   priority scheme?

25   In the brief, we condensed that a bit so

1   that we didn't have the paragraph of background, and we

2   said, may a structured dismissal distribute estate

3   assets in violation of the priority scheme? There is no

4   substantive difference there. The authorization in this

5   case was done through a structured dismissal.

6   Settlement proceeds are estate assets.

7   The basic question in this case has always

8   been the same: Was the bankruptcy court entitled under

9   the Bankruptcy Code to authorize this distribution of

10   settlement proceeds, which are estate assets, in

11   violation of priority?

12   JUSTICE BREYER: Exactly. So what forbids

13   it? You started out by saying there is nothing in the

14   Code that permits this kind of settlement, which in fact

15   leaves out -- if -- it gives some money to lower-ranking

16   creditors without giving them to your client.

17   I think you're right. I don't see anything

18   permits it. The problem: What forbids it?

19   MS. SPINELLI: The structure of the Code

20   forbids it, Justice Breyer.

21   JUSTICE BREYER: The structure of the

22   Code --

23   MS. SPINELLI: If we --

24   JUSTICE BREYER: -- forbids it.

25   MS. SPINELLI: If we -- the structure and

1 the text of the Code. If we take a step back for a

2 moment, the way business bankruptcies work is that the

3 debtor files a petition.

4   That creates an estate, which includes all

5 the debtor's property, and it also includes causes of

6 action belonging to the estate.

7   That estate is then held in trust,

8 essentially for the benefit of creditors. It is

9 protected against creditors' claims through the

10 automatic stay.

11   The trustee or debtor-in-possession can

12 dispose of estate assets only in accordance with strict

13 limitations and subject to the bankruptcy court's

14 supervision. And at the end of the case, those assets

15 are distributed to creditors through a confirmed Chapter

16 11 plan, which requires adherence to priority; or,

17 failing that, the case can be converted to Chapter 7, in

18 which case the assets are also distributed in accordance

19 with priority.

20   Those careful, reticulated mechanisms for

21 the distribution of estate assets foreclose any

22 inference that Congress intended to allow courts to

23 disregard them and create a different method for

24 distributing assets that's not mentioned anywhere in the

25 Code that violates that --

1   JUSTICE KAGAN: Why do you think --

2   MS. SPINELLI: -- backbone priority scheme.

3   JUSTICE KAGAN: Why do you think, though, it

4   isn't mentioned someplace in the Code? I mean, did

5   Congress just not think that this might happen?

6   MS. SPINELLI: No, Justice Kagan. I think

7   the reason that Chapter 11 doesn't expressly apply the

8   priority rules to settlements is that settlements are

9   not intended to be a method of distributing estate

10   assets. I think it's very important to keep those two

11   things distinct. On the one hand, we have a settlement

12   of a cause of action belonging to the estate. The

13   estate relinquishes its rights in return for money, and

14   money goes into the estate. That is one thing.

15   Separately, there is a distribution of all

16   of the assets in the estate, including the proceeds of

17   the settlement. And that is done in Chapter 11 through

18   a Chapter 11 plan.

19   So Congress would not have specified that

20   priority applies to settlements, because settlements are

21   not a means for distribution of estate assets.

22   JUSTICE GINSBURG: There can --

23   MS. SPINELLI: Only the plan does that.

24   JUSTICE GINSBURG: There can be a dismissal.

25   There are three things. Two are covered,

1   Chapter 7 and Chapter 11. But this is a dismissal,

2   which means, as I understand it, you -- you return to

3   the preexisting situation.

4   MS. SPINELLI: That's correct.

5   JUSTICE GINSBURG: But -- but now you're

6   saying the -- there are assets, and the Court has to do

7   something about the distribution of those assets.

8   MS. SPINELLI: Correct -- correct, Justice

9   Ginsburg. The -- there are -- there are two methods for

10   distributing estate assets contemplated by the corporate

11   provisions of the Bankruptcy Code, either a Chapter 11

12   plan or the Chapter 7 distribution set out in Section

13   726, both of which require adherence to priority.

14   A case can also be dismissed. In that case,

15   there is no distribution of estate assets at all.

16   That's not contemplated in conjunction with a dismissal.

17   Rather, the parties are returned to their prebankruptcy

18   positions, and the bankruptcy --

19   JUSTICE KENNEDY: But the -- but the Code

20   does say, 349, "unless the Court, for cause, orders

21   otherwise." Can you tell us how -- how that is -- what

22   -- what was the likely purpose for that? Because --

23   MS. SPINELLI: Justice Kennedy, what the --

24   JUSTICE KENNEDY: -- from the very literal

25   standpoint, it does cover what the Respondents' position

1   is -- is -- is here. Why is it inapplicable and why

2   is -- does it fall in face of the overall description

3   that you just gave to Justice Ginsburg?

4   MS. SPINELLI: Justice Kennedy, what the

5   legislative history tells us is that the "for cause"

6   provision in Section 349(b) was intended to protect

7   parties who took actions in reliance on the bankruptcy.

8   And I think it's important to look --

9   JUSTICE KENNEDY: Can you give me an

10   example?

11   MS. SPINELLI: I can. So one case that's

12   cited in our briefs is In re Wiese, which is a Seventh

13   Circuit case. In that case, there was a plan that had

14   been confirmed that -- in which the debtors released

15   their claim against the bank that had lent them money in

16   return for the bank's releasing its lien on some cash

17   that they had. That cash was then disbursed and

18   couldn't be gotten back.

19   The debtors then dismissed their case

20   shortly after the plan was confirmed, and the Seventh

21   Circuit said this was an appropriate case in which to

22   use the "for cause" provision. Typically, the release

23   that occurred in the plan would be undone, but in order

24   to avoid unfairness to the bank, which had taken --

25   which had taken action in reliance on the plan, the

1   Court was not going to do that. Instead, it was going

2   to hold the debtors to their release.

3   JUSTICE KENNEDY: Well -- well, if -- if

4   fairness is -- is the -- the -- the basis for the for

5   cause order, the Respondent will say, well, this is

6   fair, because most creditors were paid, so whether

7   you -- you can hear the arguments.

8   MS. SPINELLI: I --

9   JUSTICE KENNEDY: I mean, we just talk about

10   fairness. That's -- that's -- that's different from the

11   careful answer you gave to Justice Ginsburg a -- about

12   the prior scheme.

13   MS. SPINELLI: Yes, Justice Kennedy.

14   Section 349(b) doesn't create that kind of gaping hole

15   in the scheme I just described. It's important to

16   understand what it actually does. I think it's a

17   relatively limited provision.

18   So Section 349 says that -- that the default

19   when a bankruptcy case is dismissed is that certain

20   transactions that occurred during the case, such as

21   avoidance actions, get unwound, liens that have been

22   voided are reinstated, and property remaining in the

23   estate is returned to its prebankruptcy owner. In other

24   words, the bankruptcy is undone as far as possible.

25   The cause exception is an exception to that.

1   So what the cause exception permits a bankruptcy court

2   to do is to maintain the status quo at the time of

3   dismissal when there is good reason to do so. And the

4   typical good reason would be reliance by a party on

5   something that happened during the bankruptcy case. But

6   Section --

7   CHIEF JUSTICE ROBERTS: Go ahead.

8   MS. SPINELLI: But Section 349(b) doesn't

9   then permit the court to go beyond that and do something

10   that's not contemplated in conjunction with a dismissal

11   at all, but doesn't involve maintaining the status quo,

12   but involves actually distributing assets to creditors

13   in violation of the priority scheme.

14   CHIEF JUSTICE ROBERTS: You -- you said that

15   that reading was supported in the legislative history,

16   if I understood you correctly. What -- what is the

17   nature of that legislative history?

18   MS. SPINELLI: The legislative history

19   essentially -- there's not a lot of it, but what it

20   essentially says is the bankruptcy courts should use

21   that provision, the cause provision --

22   CHIEF JUSTICE ROBERTS: I mean, I -- where

23   is that? In -- in the -- in the -- a Senate Report?

24   What?

25   MS. SPINELLI: I apologize, Your Honor. I

1 believe -- we -- we cited it in our brief. And I

2 believe it is in the House -- the 1977 House Report.

3   CHIEF JUSTICE ROBERTS: Okay. Thank you.

4   JUSTICE KAGAN: May I ask, Ms. Spinelli,

5 just quickly: What's the scope of the holding that you

6 would like us to issue?

7   I suppose this comes back to Justice Alito's

8 question of what's actually on the table.

9   MS. SPINELLI: Uh-huh.

10   JUSTICE KAGAN: All settlements? All

11 structured dismissals? Just this particular kind? And

12 if just this particular kind, how would you characterize

13 it?

14   MS. SPINELLI: What we think this Court

15 should hold is that settlement proceeds cannot be

16 distributed in violation of priority. I mean, a --

17   JUSTICE KAGAN: So a settlement that is a --

18 a -- that -- that distributes protest -- proceeds.

19   MS. SPINELLI: Correct. But it -- to be

20 more specific, the -- the order that was entered here,

21 we believe, would -- could never be lawful, regardless

22 of the stage of the case at which it was entered.

23   So we are not saying this order would

24 only -- this order is only unlawful because it was part

25 of a structured dismissal. We are saying it's unlawful

1   because it took estate assets and distributed them in

2   violation of priority.

3   JUSTICE ALITO: You're saying that -- that

4   there can never be a distribution of estate assets

5   except in compliance with the priorities?

6   MS. SPINELLI: No. There is one --

7   JUSTICE ALITO: One which -- that's not what

8   you just said?

9   MS. SPINELLI: That -- well, let me -- let

10   me qualify what I just said, then.

11   There is one express exception in the

12   code -- that's Section 510 -- provides that claims can

13   be subordinated to other claims under the principles of

14   equitable subordination, which, as this Court said in

15   Noland, are limited to a creditor's bad behavior that

16   harms the estate.

17   There are also some practices that occur in

18   bankruptcy court that -- whose validity I don't think

19   this Court needs to reach. For instance, critical

20   vendor orders are an example. Courts will sometimes

21   permit, on the first day of a case, a debtor to pay

22   certain vendors on account of their prepetition claims,

23   because doing so is necessary to the debtors maintaining

24   a going concern and reorganizing and coming out the

25   other end a viable business. That's based on a doctrine

1   that goes back many, many years before the Bankruptcy

2   Code called the Doctrine of Necessity. And the

3   reasoning behind that is because a going concern is

4   worth so much more than the debtor's assets liquidated

5   piecemeal. That creates the possibility of a greater

6   recovery for creditors higher up the priority chain.

7   What happened here is precisely the

8   opposite. There was no possibility of reorganization.

9   This was a naked priority violation for its own sake,

10   and whatever one thinks about critical vendor orders,

11   what happened here, taking value from senior creditors

12   and giving it to junior creditors for its own sake, is

13   not permitted.

14   May I reserve? Thank you.

15   CHIEF JUSTICE ROBERTS: Thank you, counsel.

16   Ms. Harrington.

17   ORAL ARGUMENT OF SARAH E. HARRINGTON

18   FOR UNITED STATES, AS AMICUS CURIAE,

19   SUPPORTING THE PETITIONERS

20   MS. HARRINGTON: Thank you, Mr. Chief

21   Justice, and may it please the Court:

22   I'd like to start, if I could, with Justice

23   Kagan's last question, which is: What would we like the

24   Court to hold in this case?

25   We think the Court should hold that a

1   bankruptcy court can never resolve a bankruptcy by

2   ordering the distribution of estate assets in a manner

3   that violates the Code's detailed priority system

4   without the consent of the impaired priority

5   claimholder.

6   CHIEF JUSTICE ROBERTS: You don't even have

7   the extraordinary circumstances exception?

8   MS. HARRINGTON: No, we don't -- I mean,

9   basically, the extraordinary circumstances exception

10   that the Third Circuit wanted to apply would bring in

11   any case that is administratively insolvent, and that's

12   a large proportion of business bankruptcies.

13   That kind of exception also gives parties

14   the -- the wrong incentive to make essentially

15   self-serving assertions about what they would or would

16   not do if the particular disposition that they desire is

17   not approved.

18   JUSTICE BREYER: You'd presumably qualify

19   that with the statutory provision that was just

20   mentioned, and my guess was you want to qualify that as

21   well with the -- with this emergency creditor, you know,

22   where you're going to sink the -- the person who has a

23   prepetition was just discussed.

24   MS. HARRINGTON: Well, the prepetition

25   distributions that were just discussed, I think that --

1 that does present a separate question that we think --

2   JUSTICE BREYER: Yeah. All right. All --

3 that's all I wanted to know. You don't want a holding

4 here that is going to knock that out.

5   MS. HARRINGTON: Right, but -- so I said

6 that a -- a court could not resolve a case by ordering

7 the distribution of assets that would violate their

8 priority scheme.

9   Now, in our view, "the priority scheme" is

10 sort of a broad term that includes both equitable

11 subordination law, subordination principles, which are

12 not applicable here, and also includes the ability of

13 the priority claimholder to consent to impairment of its

14 rights.

15   I think it's important to keep in mind here

16 that the priority claimholders here, Petitioners did not

17 settle. This is not a case where the people whose

18 rights were impaired agreed to it, and you can't have --

19 you can't call a settlement basically the agreement of

20 other parties whose rights were not impaired and who, in

21 fact, benefited from the impairment of the Petitioners'

22 rights.

23   JUSTICE ALITO: What would be your principal

24 basis for distinguishing the exception that Ms. Spinelli

25 outlined at the end of her argument from what happened

1   here?

2   I thought your argument was that the

3   priority scheme applies to everything that happens in a

4   Chapter 7 and a Chapter 11.

5   MS. HARRINGTON: Yes. So in our view,

6   prepetition distributions in Chapter 11 that violate the

7   priority scheme are not permissible under any

8   circumstances unless there is consent of the impaired

9   priority claimholder. And so critical vendor orders, if

10   they are done over the objection of the -- of the

11   claimholder who skipped, we think those are not

12   permissible.

13   Now, most of the time those sort of first

14   order distributions happen in a plane of reorganization,

15   not in a plane of -- in a case of reorganization, not a

16   liquidation case. They happen with the consent of the

17   senior claimholders, and they are generally premised on

18   a -- on a prediction that -- that allowing that kind of

19   distribution will ultimately result in every creditor

20   getting more money at the end of the day. So none of

21   those factors apply here.

22   You didn't have consent. This is not an

23   ongoing concern, and there is certainly no finding that

24   everybody is going to get more money at the end of the

25   day.

1   JUSTICE ALITO: Ms. Harrington --

2   JUSTICE SOTOMAYOR: If --

3   JUSTICE ALITO: Yeah, if I could just -- go

4   ahead.

5   JUSTICE SOTOMAYOR: Please.

6   JUSTICE ALITO: There is another logically

7   prior question. And I don't know what you -- what do

8   you think we should do with the question of whether the

9   bankruptcy court has to approve settlements at all?

10   MS. HARRINGTON: We think that --

11   JUSTICE ALITO: There is nothing in the Code

12   that says that they have to.

13   MS. HARRINGTON: So we think that -- that a

14   bankruptcy court does have to approve a settlement that

15   disposes of a claim held by the estate or asserted

16   against the estate. We don't think this Court needs to

17   reach that question in this case if it doesn't want to,

18   because we think it's very clear that a -- what a

19   settlement cannot do is provide for the distribution of

20   estate assets.

21   I think it's important to remember, State

22   assets don't belong to the debtor, and they don't belong

23   to a subset of creditors. They belong to the estate.

24   And so the Code provides only specific ways that those

25   assets can be distributed. In Chapter 11, that's

1 through a plan.

2   JUSTICE KAGAN: Just to make sure I

3 understand the scope of what you're saying we should

4 decide: Would that also knock out the thing that was

5 approved in Iridium itself?

6   MS. HARRINGTON: Yes, we think it would. If

7 you limit your holding to the resolution of the case,

8 then it would not, because Iridium did not involve the

9 resolution of the case.

10   We think the principle applies more broadly

11 to prepetition and distributions as well, when you don't

12 have consent. But if the course -- if the Court prefers

13 not to, it doesn't need to reach that question in this

14 case.

15   CHIEF JUSTICE ROBERTS: So you don't agree

16 completely with Judge Scirica's dissent?

17   MS. HARRINGTON: We don't. I mean, I would

18 point out, again, that he is a -- he is a dissenter in

19 this case, and so he -- even he didn't think that this

20 case would -- would qualify, but we -- we don't think

21 there is anything in the -- in the Code that would allow

22 parties to override the priority claimholders' assertion

23 of their rights.

24   Now, it's important to keep in mind that

25 Chapter 11 is very -- is very flexible. It allows

1   basically any type of plan to be confirmed if all the

2   parties can agree on the terms of a plan. That was the

3   innovation in Chapter 11 in 1978. It didn't exist in

4   the Bankruptcy Act, and I think that sort of clearly

5   expresses Congress' intent that parties, if they can

6   come to an agreement that deviates from sort of the

7   usual course, then they should do it and that that --

8   that agreement should be memorialized in a plan, not in

9   some other disposition.

10   JUSTICE KENNEDY: Can you tell me, just as a

11   matter of practice, of practice and experience, do

12   priority creditors in a settlement, structured

13   settlement agreements, often allow junior creditors

14   to -- to receive something?

15   MS. HARRINGTON: Well, they often do in

16   plans. In -- in our -- in our experience, when there is

17   a structured dismissal like the kind at issue here,

18   usually those -- the parties turn to that kind of

19   disposition, because they can't obtain the consent of

20   the parties that they would need to get a plan

21   confirmed. And so basically what you have is an

22   agreement that is, in essence, an unconfirmable plan.

23   And instead of trying to get that confirmed, they call

24   it a structured dismissal to override the consent of the

25   priority claimholders.

1   And so in those cases, no, but -- but -- but

2   I think priority claimholders all the time agree to an

3   impairment of their rights, and, in fact, the priority

4   claimholders, other than Petitioners who were paid in

5   this case, agreed to take, you know, some cents on the

6   dollar like the tax claimholders and -- and the

7   administrative expenses.

8   JUSTICE SOTOMAYOR: Do you believe that the

9   question presented here did not address the issue before

10   us? Do you see a difference between the question

11   presented that talked about the absolute priority rule

12   as it relates to settlement proceeds and the "structured

13   dismissal" here.

14   MS. HARRINGTON: I don't think so. I think

15   the -- the change in wording was meant to sort of

16   give -- give the particular context that -- that the

17   question arises in this case. And if any -- if there is

18   any difference, it's just a narrower sort of set of what

19   the law --

20   JUSTICE SOTOMAYOR: Well, I -- I -- it goes

21   to a more fundamental question, which is, is there a

22   difference or in our ruling whether we say no settlement

23   proceeds can be distributed in violation of the absolute

24   priority rule from a statement that no dismissal,

25   structured dismissal, can be entered in violation of the

1   absolute priority rule.

2   MS. HARRINGTON: I think the --

3   JUSTICE SOTOMAYOR: I do think there is a

4   difference.

5   MS. HARRINGTON: Well, I think the -- your

6   first formulation is a little bit broader than the

7   second formulation. And then, like I said, we think the

8   rule would apply also to preplanned -- preplanned

9   dispositions of estate assets.

10   If you wanted to limit your holding just to

11   sort of the resolution of a case in a way that is kind

12   of a substitute for a plan, then I think you could just

13   say a structured dismissal can't authorize the

14   distribution of estate assets.

15   But I'd like to, again, sort of distinguish

16   the settlement of the claim from the distribution of

17   estate assets. The two things were put together in this

18   case, and they are put together throughout Respondents'

19   brief. But they are really separate things. There's

20   nothing in the Code that would authorize a debtor or

21   some subset of creditors to distribute estate assets.

22   They don't get -- they don't have any say in how estate

23   assets are distributed. The Code and Congress have the

24   say in that.

25   JUSTICE GINSBURG: Well, how can you have

1 a -- a settlement if it can't be carried out? I mean,

2 if you -- you're saying one thing is the settlement, and

3 that's okay. And the other thing is the distribution of

4 the assets, but that's what the settlement provides for.

5   MS. HARRINGTON: Well, what the settlement

6 should provide for is basically a liquidation of a

7 claim. And so if you have a claim by the estate against

8 a third party, here a creditor, you basically reduce

9 that claim to a dollar amount, and those dollars become

10 property of the estate.

11   If you have a settlement of a claim that's

12 asserted by a creditor against the estate, then it's the

13 same kind of thing: You sort of liquidate the claim,

14 you reduce it to a dollar amount, and that becomes the

15 claim against the estate held by the creditor. But

16 nothing in the Code would authorize -- and I think it's

17 a -- it would be a violation of the priority system and

18 generally of the system that distributes estate assets

19 to have parties agree on the side of how estate assets

20 should be distributed. Those estate assets are not the

21 property of the debtor once the bankruptcy starts.

22 They're not the property of the creditors. And so you

23 really need to look to the Code provisions to see how

24 estate assets should be distributed. In --

25   JUSTICE ALITO: What --

1   MS. HARRINGTON: Go ahead.

2   JUSTICE ALITO: What is your response to the

3   argument that your argument regarding Section 103(a)

4   makes the provisions that specifically make the

5   priorities applicable in Chapter 7 and Chapter 11

6   superfluous?

7   MS. HARRINGTON: Well, it doesn't, because

8   if you look at those provisions, and one of them is

9   Section 1129(a)(9), and then it's Section, I think, 726

10   in Chapter 7, they don't just say Section 507 priority

11   scheme applies. They also specify exceptions, and they

12   specify the manner in which it applies.

13   And so in Section 1129(a)(9), it says,

14   priority claimholders can agree to an impairment of

15   their rights. That exception is not included in

16   Section 7 -- in the -- in the Chapter 7 analog. It also

17   says -- tells you what it means to pay a priority

18   claimholder either through cash or through deferred cash

19   payments. Depending on the type of 507 claim, the --

20   the parties have a right to demand one or the other.

21   And so there is more to it than just saying, oh, Section

22   507 applies. It tells you how it applies and in what

23   circumstances.

24   JUSTICE ALITO: So those are just exception

25   provisions?

1   MS. HARRINGTON: Exception, but it also sort

2   of tells you what it means to fully -- in -- in the

3   Chapter 11 context, it tells you what it means to pay a

4   priority claimholder. And so some priority

5   claimholders, I guess, can demand cash on the date of

6   confirmation; others have to agree in some circumstances

7   to deferred cash payments. And so there is definitely

8   more content to.

9   In the Chapter 7 context, it also tells you

10   which type of 507 claims are allowed based on when the

11   associated proof of claim was filed. So those -- in

12   both cases, they kind of -- they add more substance than

13   the Respondents would have you believe.

14   I'd just like to point out that Congress

15   enacted the priority scheme precisely to prohibit the

16   kind of collusive looking agreements that happened here,

17   where you have high-priority and low-priority creditors

18   kind of squeezing out the middle creditors. And the

19   Court should not allow parties to make an end run around

20   that prohibition by just scrapping the main settlement

21   or -- or structured dismissal on what is really, in

22   essence, an unconfirmable plan.

23   We think that's what happened here. The

24   parties -- some of the parties reached an agreement.

25   The agreement couldn't be confirmed as a plan because it

1   abrogated the rights of priority claimholders and they

2   did not consent.

3   CHIEF JUSTICE ROBERTS: Thank you, counsel.

4   MS. HARRINGTON: Thank you.

5   CHIEF JUSTICE ROBERTS: Mr. Landau.

6   ORAL ARGUMENT OF CHRISTOPHER LANDAU

7   ON BEHALF OF THE RESPONDENTS

8   MR. LANDAU: Thank you, Mr. Chief Justice,

9   and may it please the Court:

10   Petitioners say that the bankruptcy court

11   here was required to reject the settlement that made all

12   other unsecured creditors better off without making

13   Petitioners any worse off. Nothing in the Code requires

14   that result.

15   The absolute priority rule, and this is

16   critical, applies in Chapter 11 only to plans --

17   JUSTICE SOTOMAYOR: You took away -- you

18   took away a legal right from them.

19   MR. LANDAU: Well, Your Honor --

20   JUSTICE SOTOMAYOR: They had a legal right

21   to sue Sun Life. They had a legal right to pursue their

22   other claims. And the settlement extinguished those

23   rights.

24   MR. LANDAU: And I think the question -- the

25   critical question here is, are we in a -- in a place

1   where the disposition of estate assets was required to

2   comply with the absolute priority rule? This is the

3   absolute gist of the case.

4   By its terms -- I think this goes back to a

5   question that Justice Kagan asked earlier -- the Code

6   speaks to when the absolute priority rule applies in

7   Chapter 11, and it applies to plans. Whenever you have

8   dispositions of assets before plans, they are subject to

9   judicial review. The use, sale, and lease of -- of

10 assets is subject to judicial review under Section

11 363(b), but that is a discretionary standard.

12   Now, in applying the discretionary standard,

13 it's absolutely critical to make sure that there is no

14 evasion of requirements for -- for a plan. And -- and

15 the Second Circuit in Iridium and the Third Circuit here

16 recognize that and said, this is the rare case where

17 that's true. But I think the --

18   JUSTICE SOTOMAYOR: I don't know why this is

19 a rare case.

20   MR. LANDAU: Well, it --

21   JUSTICE SOTOMAYOR: I mean, every structured

22 settlement of this kind is trying to exclude one set of

23 creditors.

24   MR. LANDAU: No. It -- it's a --

25   JUSTICE SOTOMAYOR: And this is exactly what

1   this did, and it did it in collusion among the senior

2   and junior creditors to the exclusion of the disfavored

3   creditor.

4   MR. LANDAU: If, in fact, you were to

5   concede -- start saying, well, this is the person who's

6   wearing the white hat, this is the person who's wearing

7   the black hat --

8   JUSTICE SOTOMAYOR: I'm not -- I'm not --

9   MR. LANDAU: It can't --

10   JUSTICE SOTOMAYOR: I'm just trying --

11   MR. LANDAU: Well -- I don't -- yeah.

12   JUSTICE SOTOMAYOR: -- to figure out what

13 creates the exception.

14   MR. LANDAU: The narrow legal issue before

15 this Court is simply: Looking at the Code, does the

16 absolute priority rule as such apply outside the context

17 of plans?

18   JUSTICE BREYER: You -- you were beginning

19 your first statement -- if you remember, you were just

20 about to give us a special reason, which I wanted to

21 hear.

22   MR. LANDAU: Oh. Well -- well, the -- these

23 Petitioners received a substantial distribution of

24 assets on -- on -- on the first day of the bankruptcy,

25 as -- to pay for their prefiling -- their prepetition

1   wage-and-benefits claims. They got millions of dollars;

2   in fact, far more than the settlement. So this is

3   why -- it's no accident --

4   JUSTICE BREYER: I don't see what this has

5   to do with that. But my problem is quite simple. What

6   was -- this is not your asset --

7   MR. LANDAU: That's correct.

8   JUSTICE BREYER: -- that's -- this is --

9   this is an asset of the estate?

10   MR. LANDAU: That's correct, Your Honor.

11   JUSTICE BREYER: All right. So there is an

12   asset of an estate.

13   MR. LANDAU: Right.

14   JUSTICE BREYER: It's a claim against a

15   third party.

16   MR. LANDAU: Yes.

17   JUSTICE BREYER: Very well.

18   MR. LANDAU: Right.

19   JUSTICE BREYER: And now there is a person,

20   probably the trustee or a committee, that's going to

21   pursue that claim.

22   MR. LANDAU: Correct.

23   JUSTICE BREYER: Then the claim is settled.

24   MR. LANDAU: Correct.

25   JUSTICE BREYER: Now, at least on request

1   when you're in Chapter 11, doesn't the judge, the

2   bankruptcy judge, have to approve that settlement?

3   MR. LANDAU: Not the settlement, per se.

4   JUSTICE BREYER: No? Why not?

5   MR. LANDAU: Because there's no provision in

6   the Code -- this is what we explained in our brief --

7   that specific -- it's post-1978. There used to be -- in

8   the pre- 1978 world, there was a prevision that required

9   review of settlements qua settlements.

10   Post-'78, there is a provision, 363(b) --

11   JUSTICE BREYER: Ah.

12   MR. LANDAU: -- that requires judicial

13   review of use, sale, or lease of assets. In this case,

14   they intersect, because this settlement actually not

15   only brought money into the estate, but actually then

16   said --

17   JUSTICE BREYER: But suppose they had

18   settled it for a dollar, and one of the creditors says,

19   this is all corrupt. I'm not saying they did in this

20   case. But, I mean, wouldn't -- wouldn't -- there's an

21   asset of the estate. They bring a lawsuit. They reach

22   a settlement. Suppose it's a totally crooked

23   settlement.

24   MR. LANDAU: Your Honor, the --

25   JUSTICE BREYER: What happens?

1   MR. LANDAU: Again, this is a Code case,

2   Your Honor. And there's no --

3   JUSTICE BREYER: I'm not talking about this

4   case. I just want the background in my mind.

5   MR. LANDAU: Right. I think the --

6   JUSTICE BREYER: There is no power of the --

7   of the bankruptcy judge to even look at a settlement

8   that the company in bankruptcy has made of an asset;

9   namely, the claim that he has against another party.

10   MR. LANDAU: There is no provision

11   governing --

12   JUSTICE BREYER: Okay.

13   MR. LANDAU: -- settlements qua settlements.

14   What there is a provision -- and I want to make this

15   very clear, Your Honor, because I'm not sure this was as

16   clear in our brief as it should have been, and I

17   apologize if it wasn't.

18   The fact that there's no provision for

19   approving settlements qua settlements doesn't mean --

20   which there had been under the old regime -- doesn't

21   mean that when you have a settlement that actually

22   disposes of estate assets, like this settlement did,

23   that that disposition of estate assets is not subject to

24   the traditional Rule 363(b) review by the Court of any

25   use, sale, or lease.

1   JUSTICE BREYER: Oh. Fine. Okay. It's the

2   same --

3   MR. LANDAU: They're in the same -- yeah.

4   JUSTICE BREYER: Thank you.

5   MR. LANDAU: I just wanted to make it clear.

6   JUSTICE BREYER: In that place, once we are

7   in that place --

8   MR. LANDAU: Yes.

9   JUSTICE BREYER: -- what we have is a

10   settlement, not corrupt, not crooked, perfectly fine and

11   honest and so forth, but what it does is it takes

12   Congress's 1, 2, 3, 4, 5, and it says, what we'd like to

13   do is 5, 4, 3, 2, 1.

14   MR. LANDAU: Correct.

15   JUSTICE BREYER: Now, what that seems to do

16   is it seems to be quite contrary to the order of -- of

17   battle or the order of distribution that Congress has

18   said should apply to the assets of the estate --

19   MR. LANDAU: And --

20   JUSTICE BREYER: -- of which this is one.

21   MR. LANDAU: And you are absolutely right.

22   And -- and as the Second Circuit said in -- in Iridium,

23   and as the Third Circuit said in this case, that is the

24   most important concern in the 363(b) discretionary

25   analysis, to make sure that there is no evasion of that

1   scheme.

2   JUSTICE BREYER: Well, so -- right. Now,

3   you provide a case. Congress has said 1, 2, 3, 4, 5 for

4   estate asset.

5   MR. LANDAU: Right.

6   JUSTICE BREYER: You have an estate asset,

7   and you want to do -- I exaggerate -- 5, 4, 3, 2, 1.

8   MR. LANDAU: Right. Well --

9   JUSTICE BREYER: So where does the

10   bankruptcy trustee or any court get the power to say

11   that a group of people can, in fact, reverse the order

12   in which these assets will be distributed?

13   MR. LANDAU: This is --

14   JUSTICE BREYER: That is -- that is what is

15   bothering me, and presumably the government, and

16   certainly the workers here, who are -- who are upset

17   about it.

18   MR. LANDAU: Correct. Well, Your Honor, and

19   I think the -- the -- the clear answer to that is, as a

20   general rule, they can't. But this case explains

21   exactly why Iridium said there may be some rare

22   exceptions, because once you are in this more

23   discretionary 363(b) land, the -- the priority scheme is

24   going to be the most important.

25   This case is a great example, Your Honor,

 1   because in this case we have findings that there could

 2   be no confirmable Chapter 11 plan because the estate was

 3   administratively insolvent.

 4   So the Code system that you just described,

 5   the waterfall of priorities, would not apply in Chapter

 6   11 because there was no way to go to a Chapter 11 plan.

 7   JUSTICE KENNEDY: But -- but I'm sure it

 8   often happens that there can be no confirmable plan

 9   because the creditors -- priority creditors are not

10   going to concede. So that happens all the time when you

11   go through Chapter 7.

12   MR. LANDAU: Right. And that --

13   JUSTICE KENNEDY: And that's not a rare --

14   so this is not a rare case.

15   MR. LANDAU: But I'm -- this is only the

16   first prong, Your Honor. Then the Court also analyzed,

17   well, the alternative, then, is conversion to Chapter 7,

18   and we have findings there, too, that any conversion to

19   a Chapter 7 liquidation, in fact, the estate asset --

20   there would be no settlement there, because at that

21   point, once you've gone through the expense and delay of

22   converting to Chapter 7, it wouldn't make sense to

23   settle. That's -- there's many reasons that you might

24   want to -- be willing to settle at the beginning of the

25   case, but --

1   JUSTICE KENNEDY: But -- but this seems --

2   but the essence of the case is not really an objection

3   to approval of the settlement; it's the objection of the

4   distribution of the assets.

5   MR. LANDAU: Absolutely. And that's -- I

6   think that's so critical, Your Honor, and -- and their

7   objection would actually completely come back to bite

8   them because there is no legal difference between a

9   distribution of assets on the first day where they

10   recovered $6 million in this case in their prepetition

11   wage and benefit claims.

12   That's why, to go back to Justice Alito's

13   question earlier, it was not a slip of the pen that led

14   them to change their question presented from the

15   question -- from the petition to the merits brief. They

16   know perfectly well that a rule that the absolute

17   priority rule applies to every distribution of assets

18   would have creamed the workers in this case and would in

19   future cases, because such workers are often the

20   beneficiaries of these first day orders that pay -- that

21   pay wage and benefit claims, that pay critical vendor

22   orders.

23   Once you're talking about a world, as they

24   seem to be suggesting, that all preplan distributions of

25   assets are subject to the absolute priority rule --

1   that's not in the Code. That's the gist -- that's the

2   crux of the dispute here. That was a circuit split that

3   this Court granted cert to -- to resolve.

4   CHIEF JUSTICE ROBERTS: I thought they -- I

5   thought they had a priority at the initial stage that

6   required them to be paid the $6 million that you're

7   talking about.

8   MR. LANDAU: They were not. There were

9   people above them in the chain. There were

10   administrative creditors. There were secure -- they did

11   not have the top priority at that point, and that was

12   not subject to the priority system.

13   JUSTICE GINSBURG: But they had the priority

14   ahead of the unsecured general creditors that did get

15   $1.7 million. What they are saying is that under the

16   priorities, that belonged to us, not creditors who were

17   lower down.

18   MR. LANDAU: Correct. And I think that

19   there was -- that there was a finding here that, in

20   fact, the alternative to this settlement was not a

21   settlement where they actually would have -- was not a

22   Chapter 11 plan because they would have recovered

23   nothing in a Chapter 11 plan because there could have

24   been no Chapter 11 plan. It was not confirmable.

25   And in conversion to Chapter 7, they

1 wouldn't have gotten anything either, because all the

2 money would have gone to the secured creditor.

3   JUSTICE BREYER: But that's -- I see that

4 point, which you've made several times, is a very good

5 point. I -- clarify a basic misunderstanding on my

6 part. What's a structured settlement?

7   MR. LANDAU: Well, I think a structured

8 settlement is -- it's not a legal term. It's something

9 they've come up with in this case.

10   JUSTICE BREYER: Why not just call it a

11 settlement?

12   MR. LANDAU: I think you could. And I think

13 in that --

14   JUSTICE BREYER: Let's call it a settlement.

15   MR. LANDAU: Perfect.

16   JUSTICE BREYER: So now a company finds,

17 very surprisingly, that there, underneath the building,

18 is Jean LaFitte's gold treasure.

19   (Laughter.)

20   JUSTICE BREYER: See? But there is somebody

21 down there who has it. He says, give it to me; it's

22 ours. He says, I'll give it to you, but I want you to

23 use it to pay my friend who happens to be my cousin, who

24 is the 19th ranked creditor.

25   MR. LANDAU: Right.

1   JUSTICE BREYER: And as long as you give the

2   majority to him, okay, then you can give the rest to the

3   others.

4   All right. Now, that would seem to be a

5   possibility at least from your argument in this case.

6   MR. LANDAU: Your Honor, I think what you

7   are saying or the -- the point that you're getting to

8   can be resolved through the traditional 363(b) analysis,

9   which allows for play in the joints, unlike their

10   unyielding and absolute -- absolute priority rule.

11   Under you're hypothetical, Your Honor, there

12   would be money there. And in that case, it looks like

13   that would be an evasion of -- there could be a plan

14   there.

15   JUSTICE BREYER: By the way, if you want me

16   to, I will make up my hypothetical so that giving half

17   the gold to this person is just as wonderful as you

18   would like, and I will also change the hypothetical

19   around, if you could do or I could do, so that not

20   giving the money to this person would be just terrible.

21   MR. LANDAU: Right.

22   JUSTICE BREYER: The Earth will come to an

23   end. So the question is, do you think Congress gave to

24   the trustee or to you or to somebody else the power to

25   deviate with Jean LaFitte's gold or with these

1 particular -- this particular set of money or any other

2 set of money?

3   MR. LANDAU: I think --

4   JUSTICE BREYER: It seems to me a dangerous

5 principle to get into, but if you can tell me or that

6 normally happens, I'm open to --

7   MR. LANDAU: Well, it -- it -- it doesn't

8 normally happen. I think that is the lesson of Iridium

9 and this case. The Third Circuit said as a general

10 matter, if -- if the creditors were to come together and

11 say, you know, we really just don't like this one

12 creditor, even though that person has a high priority.

13 We're going to structure this so that that person gets

14 disfavored.

15   Well, under the 363(b) analysis, if that

16 person would have actually have had an alternative where

17 they recovered something --

18   JUSTICE KAGAN: Let me ask you --

19   MR. LANDAU: -- that would be a problem.

20   JUSTICE KAGAN: -- Mr. Ernest, sort of a

21 similar question. You -- here's two different kinds of

22 bankruptcy schemes. One scheme just says every time you

23 distribute assets, you have to follow the following

24 order: one, two, three, four, five.

25   MR. LANDAU: Right.

1   JUSTICE KAGAN: That's -- and that's it.

2   You just have to follow that order.

3   MR. LANDAU: Correct.

4   JUSTICE KAGAN: That's one Bankruptcy Code.

5   Here's another Bankruptcy Code: It says

6   presumptively, you have to follow one, two, three, four,

7   five, but if there is a Pareto-superior solution, in

8   other words, a solution in which some people are made

9   off and nobody -- in which some people are -- get better

10   outcomes and nobody gets a worse outcome --

11   MR. LANDAU: Yep.

12   JUSTICE KAGAN: -- if there is such a

13   solution, you can go with that. And that might be a

14   completely sensible bankruptcy provision --

15   MR. LANDAU: Right.

16   JUSTICE KAGAN: -- for Congress to have

17   enacted.

18   MR. LANDAU: Right.

19   JUSTICE KAGAN: The question is whether

20   Congress did enact it and what you can point to in the

21   Bankruptcy Code that suggests that the continual

22   statement that it's just one, two, three, four, five is

23   subject to a kind of equitable exception for

24   Pareto-superior outcomes.

25   MR. LANDAU: Yes. I can -- I can exactly

1   answer that question. The line that Congress drew in

2   the Code is the absolute priority rule with its -- with

3   its specific one, two, three, four, five that apply as a

4   matter of law and is unyielding, applies to plans. When

5   you are not in the world of plans, you are in the world

6   of 363(b), which has play in the joints. And so the

7   Pareto optimality that you just said, Your Honor, is

8   something that is appropriate in a 363(b) analysis.

9   Now, as the Second Circuit pointed out in

10   Iridium and the Third Circuit pointed out here, a

11   critical consideration in that discretionary analysis is

12   to make sure it is not being done for the purpose of

13   evading what would otherwise be something that could

14   proceed to the stage where Congress made the absolute

15   priority rule applicable.

16   JUSTICE SOTOMAYOR: But I don't understand

17   how you get to an extraordinary circumstance in that --

18   in this situation. It seems to me that wanting to

19   exclude the claims of one or more creditors is the

20   ordinary situation. Every junior creditor wants money.

21   They're happy to exclude anybody they can --

22   MR. LANDAU: Right.

23   JUSTICE SOTOMAYOR: -- or anybody who will

24   concede to doing it.

25   MR. LANDAU: Right.

1   JUSTICE SOTOMAYOR: So how do you protect

2   the excluded creditor from being preyed on by one of the

3   other creditors? We already know the junior creditors

4   have a self-interest.

5   MR. LANDAU: Absolutely, Your Honor.

6   JUSTICE SOTOMAYOR: The senior creditors

7   have --

8   MR. LANDAU: Yes.

9   JUSTICE SOTOMAYOR: It happens to be one of

10   the biggest senior creditors here is the one who was

11   insisting upon excluding the junior creditor.

12   MR. LANDAU: Yes.

13   JUSTICE SOTOMAYOR: So where do we go? How

14   do we defined "extraordinary"?

15   MR. LANDAU: In that 363(b) world, Your

16   Honor, that governs the use, sale and lease of assets,

17   when a court looks at that, a court can say, is the

18   creditor who is claiming that he or she or it is being

19   unfairly squeezed out, in your hypothetical, can show

20   that there is some mechanism under which that person

21   would otherwise, absent the settlement or the

22   disposition of assets that is -- is contemplated at

23   issue before the Court, would actually make off better.

24   The critical problem here is that there were

25   findings -- there was a hearing in the bankruptcy court

1 on this. It went up to the district court in review and

2 then to the Third Circuit. And there were findings.

3 The findings were -- and these were critical -- that

4 there could have been no proceeding to a Chapter 11

5 confirmation. So the idea that this would have

6 proceeded to a place where the -- the person squeezed

7 out in your hypothetical would have actually recovered

8 something in Chapter 11 --

9   JUSTICE KAGAN: But, Mr. Landau --

10   MR. LANDAU: -- is counterfactual.

11   JUSTICE KAGAN: I mean, you might be right

12 or you might be wrong about that. Let's just assume

13 that you are right, that -- that this is one of these

14 extraordinary circumstances in which some people can be

15 made better off and nobody will be made worse off.

16 Still the question is, where is the authorization for

17 that in the Bankruptcy Code? Because that's like a big

18 principle. I mean -- and I think we would have known

19 about it if that's the way bankruptcy proceedings were

20 supposed to go. And -- and you suggest while it's in

21 this "for cause" language, but this "for cause"

22 language, I mean, this is a pretty specific provision

23 that we're talking about.

24   What it says is that when you can't reach a

25 plan and the case has to be dismissed, this is attached

1 to a provision that says everything has to be rolled

2 back.

3   MR. LANDAU: Right.

4   JUSTICE KAGAN: And -- and this says, well,

5 not -- you know, maybe, if there is a good reason, not

6 everything has to be --

7   MR. LANDAU: Right.

8   JUSTICE KAGAN: -- rolled back to exactly

9 the way it was.

10   But that's a really different kind of

11 provision than saying, in courts, you get to decide

12 or -- or -- or parties, really, you get to decide, and

13 then courts get to -- get to approve an outcome of a

14 bankruptcy proceeding that does not follow the usual

15 priority rules just because these particular parties,

16 not all of them, but these particular parties think it

17 will make some people better off without making other

18 peoples worse off.

19   MR. LANDAU: Well, the key point is 363(b).

20 That is the general provision that requires bankruptcy

21 courts to review the use, sale, or lease of assets.

22   When you have -- what -- what they are

23 objecting to here in this settlement is the fact not

24 only that it brings money in, but that it actually then

25 distributes money to different people in a way that they

1   say doesn't comply with the absolute priority rule. So

2   it's the 363(b) discretion. That is the standard about

3   best interests of the estate. It's been phrased various

4   ways; that -- that's really a judicial gloss in the

5   language of the statute, and that's probably -- you

6   know, the absolute contours of 363(b) are not really

7   within the question presented here.

8   The question presented here really is: Are

9   we in a world where there is any discretion at all,

10   versus a world where the absolute priority rule applies

11   by its terms?

12   JUSTICE BREYER: Well, this 363(b) -- is

13   there -- I mean, this -- you would -- they say -- you're

14   just saying they did it the wrong way when they reached

15   the settlement; then this -- the -- the Petitioners here

16   should have gone to the bankruptcy judge and said,

17   Judge, you know, there is an odd thing about this

18   settlement. They're not only paying in $3 million or

19   whatever, but they want to tell you how to distribute

20   it.

21   MR. LANDAU: And they --

22   JUSTICE BREYER: And they want to tell you

23   how to distribute it, and we want you to distribute it

24   according to the rules, and not according to what they

25   say.

1   That's what you say they should have done.

2   MR. LANDAU: Well, that's what they did do,

3   and exactly what they --

4   JUSTICE BREYER: Well, if that's what they

5   did do, what's the problem?

6   MR. LANDAU: Yes -- no, but they --

7   JUSTICE BREYER: And then you're saying they

8   have discretion there.

9   MR. LANDAU: Yes.

10   JUSTICE BREYER: So the question is: Do

11   they have discretion --

12   MR. LANDAU: Yes.

13   JUSTICE BREYER: -- to depart from -- okay.

14   I got it.

15   MR. LANDAU: And -- and they say --

16   JUSTICE BREYER: Do they have discretion

17   depart from the -- do they have discretion to depart

18   from the priorities as set by Congress?

19   MR. LANDAU: Exactly. What I'm saying is

20   that the -- you know --

21   JUSTICE BREYER: Over the objection of one

22   of the creditors.

23   MR. LANDAU: The basic dispute before this

24   Court in this case is --

25   JUSTICE BREYER: Okay. That's helpful.

1   MR. LANDAU: -- does the absolute priority

2   rule apply to distributions of plan assets -- of -- of

3   estate assets, excuse me -- before a plan? They say

4   yes, it does. We say no, it doesn't.

5   It -- you -- distribution of estate assets,

6   whether it's on the first day through a first-day order,

7   a critical vendor order, is all subject --

8   JUSTICE BREYER: Oh, well, once -- then I'm

9   back with Justice Kagan. I'm pretty worried about that

10 provision.

11   MR. LANDAU: Well -- but --

12   JUSTICE BREYER: And the reason I'm worried

13 about it is -- and you'll be worried about it, all you

14 have to do is represent some client or represent some --

15 a bank, for example, that thinks it has secured --

16 thinks it has a secured interest in something, and lo

17 and behold, there is a $40 billion settlement, and they

18 make it conditional that the money go to the widows and

19 orphans --

20   MR. LANDAU: Okay, but -- but --

21   JUSTICE BREYER: -- so we reverse it here,

22 and then the --

23   MR. LANDAU: But, Your Honor, just to be

24 clear.

25   JUSTICE BREYER: Yeah.

1   MR. LANDAU: Discretion doesn't mean win.

2   And -- and I think the Second Circuit in Iridium and the

3   Third Circuit in this case were very, very clear that

4   the most important consideration for a court to look at

5   in -- in assessing a distribution of assets that doesn't

6   comfort with the priority rule is: Is there a

7   compelling reason why it doesn't? We --

8   CHIEF JUSTICE ROBERTS: But that's, I think,

9   where the -- the -- the issue comes down. I mean, the

10   reasonableness of your position is directly related to

11   how extraordinary the extraordinary circumstances have

12   to be.

13   I mean, you're -- you're -- you're

14   suggesting that the main criteria in approving under

15   363(b) is pretty much what the priorities are under --

16   under Chapter 11.

17   MR. LANDAU: Right.

18   CHIEF JUSTICE ROBERTS: Now, if there is a

19   very close requirement there, then, you know, what

20   you're asking for is not that extraordinary.

21   MR. LANDAU: It isn't -- I just --

22   CHIEF JUSTICE ROBERTS: If, however -- well,

23   if, however, that -- it -- it's -- that priority simply

24   informs the exercise of discretion by the judge under

25   363(b) and is not as tight a requirement, well, then,

1   it's -- you know, then it is pretty extraordinary.

2   And -- and it -- it makes a difference.

3   Under -- under the -- the Chapter 11 regime,

4   people's leverage in negotiating the plan depends to

5   some extent on their priorities. Under the -- the --

6   the settlement regime, it's, you know, the -- the

7   leverage is reshuffled, and it's more or less who can

8   gang up on who but who else.

9   MR. LANDAU: Right. But Congress drew a

10   line --

11   CHIEF JUSTICE ROBERTS: I'm sorry. Could

12   you answer my concerns?

13   MR. LANDAU: Just -- Congress drew a line

14   that the absolute priority rule as such applies to

15   plans. When you're talking about distributions of

16   assets other than plans, you're in that discretionary

17   regime.

18   That -- the question presented to this Court

19   by the petition is the dispute between AWECO on the one

20   and Iridium on the other, which is, is it -- is it the

21   absolute priority rule that governs preplan

22   distributions, or is it this discretionary regime?

23   One can, in other cases, work on the --

24   the -- and so you can resolve this case by simply saying

25   they are wrong to say the absolute priority rule applies

1 outside the context of plan.

2   The extent to which you get into the

3 exercise of discretion is something that they didn't

4 present in the question presented. They didn't say the

5 Third Circuit erred --

6   CHIEF JUSTICE ROBERTS: Right, but if we are

7 concerned about --

8   MR. LANDAU: -- in applying the

9 discretionary Iridium standard.

10   CHIEF JUSTICE ROBERTS: If -- if we are

11 concerned about how extraordinary the extraordinary

12 circumstances are -- in other words, your position looks

13 more reasonable the tighter the extraordinariness

14 requirement is -- what -- what type of language would

15 you require -- I mean, you're saying, oh, well, just say

16 you can do this and then it will work out over time how

17 extraordinary it is.

18   But what would you say if you want -- if you

19 felt an obligation to tighten the extraordinary

20 requirement?

21   MR. LANDAU: I don't think I could improve

22 on the language that the Second Circuit used in Iridium

23 and the Third Circuit used here, saying that it is

24 the -- the most important consideration is conformity

25 with the absolute priority rule. So that if there is a

1   confirmable plan that is -- is -- that -- that where the

2   person complaining that they were cut out would actually

3   get something in the absolute prior -- through the

4   application of the absolute priority rule, that would be

5   almost implausible to think that it could ever be

6   approved.

7   The -- the fundamental problem --

8   JUSTICE KAGAN: But then doesn't that run

9   into -- this is what Ms. Harrington ended her remarks by

10 saying, is that you're just saying the plans that the

11 Bankruptcy Code declare not confirmable are, in fact,

12 going to be confirmed through this alternative

13 procedure?

14   MR. LANDAU: No, Your Honor. Again, the --

15 now we are talking about the means for terminating

16 Chapter 11 plans, which is a little bit different than

17 the question presented, which is all about the

18 distribution of assets. But just -- just to be clear,

19 so Section 1112 of the Code says that if a -- if Chapter

20 11 plan can't be confirmed, you have two alternatives.

21 You either go to Chapter 7 conversion or to dismissal.

22 Chapter -- there are specific findings here that Chapter

23 7 conversion made no sense because the -- the

24 trustee would -- the -- the estate did not have the

25 money to pursue the claim on its own and nobody would

1   bring this case on a contingency basis.

2   Now, the -- the -- the Petitioners here were

3   participating at that hearing in the bankruptcy court

4   where this was done. They didn't raise their hands and

5   say, hey, we'd be willing to pursue this on a

6   contingency basis, which is why it's somewhat

7   farfetched, to say the least, that they're now

8   suggesting that theoretically well, they -- they were

9   deprived of this opportunity to pursue this claim

10   outside of bankruptcy. They were given the opportunity

11   to pursue the claim on behalf of the estate in

12   bankruptcy, and nobody wanted to do that.

13   JUSTICE SOTOMAYOR: Mr. Landau, is there a

14   difference, in your mind, because there might be in

15   mine, between a settlement that settles an individual

16   claim, the emergency creditor claim that your -- that

17   your opponent spoke about, where there is not a total

18   distribution of the assets of the company, from a plan

19   that's really just an alternative plan, because that's

20   what this structured settlement was?

21   In my mind, something that would be an

22   extraordinary circumstance --

23   MR. LANDAU: Right.

24   JUSTICE SOTOMAYOR: -- would be something

25   that did something like the first thing, and not

1 necessarily the second.

2   MR. LANDAU: I think Your Honor is making a

3 very important point, which is, the application of the

4 363(b) discretion may well vary depending on the

5 circumstances of the case and, just -- and your first

6 hypothetical, maybe -- you know that -- that -- that

7 is -- now we are talking about, you know, the way that

8 that 363(b) analysis applies, and it may apply

9 differently --

10   JUSTICE SOTOMAYOR: So would you tell --

11   MR. LANDAU: -- on the first day of the

12 bankruptcy versus the last day of the bankruptcy.

13   JUSTICE SOTOMAYOR: -- me why Sun Life --

14 Sun Life cared?

15   If it got its settlement -- i.e., it was

16 going to pay $2 million and get all the claims against

17 it released -- what was its reason for not wanting the

18 proceeds to be distributed according to the absolute

19 priority rule?

20   MR. LANDAU: It wanted a global settlement

21 of all claims and they got that with all other

22 creditors. The -- the -- the creditors -- the

23 Petitioners here refused to settle their WARN claims

24 that their -- those are their claims outside the context

25 of this claim get settled, for less than a hundred cents

1   on the dollar. So they were -- they were holdouts,

2   essentially, refusing to join the global settlement of

3   everything.

4   JUSTICE SOTOMAYOR: Well, I'm -- I'm sorry.

5   Does this mean that the junior creditors wouldn't have

6   agreed to this settlement because the senior creditors

7   could have? What did the senior creditors, who were in

8   line -- in line care about how much was left over to

9   junior creditors, including Sun Life?

10   MR. LANDAU: Well, I think that the point is

11   that Sun would not have entered into the settlement at

12   all unless -- which -- which benefited all the

13   creditors, including the junior creditors --

14   JUSTICE SOTOMAYOR: But why?

15   MR. LANDAU: Why --

16   JUSTICE SOTOMAYOR: Why does it care?

17   MR. LANDAU: Why does Sun? Well, for --

18   JUSTICE SOTOMAYOR: Why does Sun Life care?

19   MR. LANDAU: In the absence of a global

20   settlement of this WARN claim outside of the -- against

21   Sun, Sun didn't want to have a settlement that -- that

22   funded the litigation against it. Now, it --

23   JUSTICE SOTOMAYOR: No, the settlement would

24   have been the one that occurred.

25   MR. LANDAU: No, because it --

1   JUSTICE SOTOMAYOR: If it --

2   MR. LANDAU: There's two different claims.

3 The claim that was settled was the estate's fraudulent

4 conveyance claim. These particular Petitioners had a

5 separate WARN claim against Sun and the debtor. And it

6 was -- in the context of settling the fraudulent

7 conveyance claim against the estate, Sun only wanted to

8 have a global settlement to put this whole litigation

9 behind it. And they said, we're not going to settle the

10 fraudulent conveyance claim in a way that funds

11 the prepetition --

12   JUSTICE SOTOMAYOR: So do you think they can

13 still sue you for those fraudulent conveyance claims?

14   MR. LANDAU: Not for the fraudulent --

15   JUSTICE SOTOMAYOR: Not you; Sun Life.

16   MR. LANDAU: Not -- they can certainly sue

17 the -- the -- they can certainly pursue their WARN

18 claims, and they did. That was their choice not to

19 participate in the settlement --

20   JUSTICE SOTOMAYOR: The fraudulent-transfer

21 claim?

22   MR. LANDAU: No. The fraudulent-transfer

23 claim was ended. But I think the key point, there are

24 findings here that the fraudulent-transfer claim was

25 essentially worthless to them, because there was no

1   money to pursue it, and --

2   JUSTICE SOTOMAYOR: You don't understand.

3   My basic question was --

4   MR. LANDAU: Okay.

5   JUSTICE SOTOMAYOR: -- what did Sun Life

6   care if the fraudulent conveyance claim was going to be

7   resolved and released?

8   MR. LANDAU: Because --

9   JUSTICE SOTOMAYOR: Why did it care to

10   exclude these truck drivers from receiving whatever they

11   demanded?

12   MR. LANDAU: Because that would have funded

13   the truck drivers to pursue their separate WARN claims

14   against us. So we didn't want them --

15   JUSTICE SOTOMAYOR: But that eventually --

16   you had already --

17   MR. LANDAU: No.

18   JUSTICE SOTOMAYOR: Sun Life had already won

19   that.

20   MR. LANDAU: No. We only won later.

21   That -- it's -- it's the timing of that, I think, Your

22   Honor, that really gets to the point.

23   I think the fundamental point here is we're

24   really talking about a rule where they're saying the

25   absolute priority rule in flexibly and invariably

1   applies even before a plan.

2   Our position, on the other hand, is that the

3   use/sale of assets at any point before the plan is

4   governed by 363(b). There are -- that's a discretionary

5   regime. And as the Second Circuit said in Iridium and

6   the Third Circuit said here, it is absolutely critical

7   to look at making sure that it's not an evasion of the

8   plan.

9   But -- but -- but the question that this

10   Court was asked to resolve is, is it the -- the rigid

11   and unyielding absolute priority rule or the 363(b)?

12   And the Code answers this question. And -- and so I

13   think in this case that the --

14   JUSTICE BREYER: What the Code in 363(b)

15   says is the trustee can sell a suit. Okay? That's what

16   it says. It says nothing about --

17   MR. LANDAU: Yes, but --

18   JUSTICE BREYER: It says nothing about what

19   the terms are. It says nothing about what the

20   settlement is. And the question for us, I guess, is, in

21   those words, which make no reference to it --

22   MR. LANDAU: But --

23   JUSTICE BREYER: -- can you settle it on

24   terms that will, in fact, take these assets that belong

25   to the company and distribute them in a way that is

1 contrary to 1, 2, 3, 4, 5?

2   MR. LANDAU: But -- but the distribution is

3 a use of the estate assets, Your Honor. So again, it

4 goes to, can you -- what are the constraints on using

5 the estate assets?

6   And I -- I really encourage you to look at

7 the very tight way in which the Second Circuit in

8 Iridium said, we want to be super careful in this. To

9 say we want to be super careful is not to say -- is just

10 to say that the Fifth Circuit overstated it by saying

11 you can never do it. In other words, the Fifth Circuit

12 has an absolute bright-line rule. We don't care how

13 Pareto-optimal --

14   JUSTICE BREYER: Right.

15   MR. LANDAU: -- this is.

16   And I think the basic point was made by the

17 bankruptcy court here. The Bankruptcy Code is not a

18 suicide pact. So if, in fact, you have a situation

19 where the settlement or -- and the distribution proposed

20 makes others better without making these folks worse

21 off, there is nothing in the Code that prohibits that.

22   CHIEF JUSTICE ROBERTS: Thank you, counsel.

23   MR. LANDAU: Thank you.

24   CHIEF JUSTICE ROBERTS: Two minutes,

25 Ms. Spinelli.

1   REBUTTAL ARGUMENT OF DANIELLE SPINELLI

2   ON BEHALF OF THE PETITIONERS

3   MS. SPINELLI: Respondents' position fails

4   because Section 363(b) is not a means of distributing

5   estate assets. The -- the 363(b) discretion that

6   Mr. Landau referred to is discretion to approve a

7   settlement or a sale of an estate asset, not to

8   distribute the settlement or sale proceeds in violation

9   of priority.

10   Assets are distributed under Chapter 11

11 through a Chapter 11 plan. That's it. And our

12 fundamental point here is that those assets cannot be

13 distributed on account of prepetition claims in

14 violation of priority.

15   To the extent there is a potential exception

16 for the Doctrine of Necessity, that's hotly disputed.

17 Courts disagree about whether that exception exists.

18 And that's not an issue this Court needs to resolve

19 because the Doctrine of Necessity, by its nature, is

20 designed for situations in which a payment to

21 prepetition creditors is necessary to the reorganization

22 of the debtor. There is no dispute that that wasn't the

23 case here. And as for our first-day order paying the

24 wages of the drivers, that was consented to, and no one

25 is saying that you're not allowed to consent to a

1 priority violation.

2   The only point we are making about

3 structured dismissals is that there is no superpower

4 associated with structured dismissals that provides for

5 an exception to that general rule that one cannot

6 distribute estate property on account of prepetition

7 claims in violation of priority.

8   Respondents' rule would wreak havoc on the

9 basic process of bankruptcy. If debtors could

10 distribute estate property to creditors at any time

11 without regard to the priority scheme before a plan,

12 there wouldn't be much left of the scheme. Debtors

13 could simply reach a deal with junior creditors and

14 distribute property leaving inadequate resources to pay

15 senior creditors.

16   CHIEF JUSTICE ROBERTS: Thank you, counsel.

17   The case is submitted.

18   (Whereupon, at 11:05 a.m., the case in the

19 above-entitled matter was submitted.)

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