No. 23-124

IN THE

Supreme Court of the United States

WILLIAM K. HARRINGTON, UNITED STATES TRUSTEE, REGION 2,

Petitioner,

v.

PURDUE PHARMA L.P. ET AL.,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Second Circuit

BRIEF OF *AMICUS CURIAE* KIM HAROLD PETERSON IN SUPPORT OF PETITIONER

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INTEREST OF AMICUS CURIAE[1]

Kim Harold Peterson, a successful California real estate developer, along with his companies, were the unwitting victims of a multi-million-dollar Ponzi scheme. *See generally SEC v. Champion-Cain*, No. 3:19-cv-1628-LAB-AHG (S.D. Cal. 2019) ("*Champion-Cain*"). The scheme was orchestrated by an individual named Gina Champion-Cain with co-conspirators Chicago Title Company and Chicago Title Insurance Company (collectively "Chicago Title"). To redress the theft of his and his companies' funds, Peterson sued Chicago Title in California state court while also filing claims in a federal securities receivership over Cain's entity. *See Kim Funding, LLC v. Chicago Title Co.*, No. 37-2019-66633 (S.D. Superior Court); *Champion-Cain*, ECF Nos. 807-13, 807-14, Investor Proof of Claim Forms (May 31, 2022).

Following a recent settlement between the court-appointed Receiver and Chicago Title, however, the District Court in the federal receivership entered a bar order extinguishing Peterson's state court claims against Chicago Title. *Champion-Cain*, ECF No. 926, Order Overruling Obj., *et al.* at 13 (Nov. 22, 2022). The district court did so both over Peterson's objections and without allowing him a share in the distributions as compensation for his original losses or his released claims. *Ibid.*; *see also Champion-Cain*, 2023 WL 2215955 (S.D. Cal. Feb 24, 2003).

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[1] No counsel for a party authored this brief in whole or in part. No person other than amicus curiae or his counsel made a monetary contribution to this brief's preparation or submission.

The similarities between the approved release of claims in Peterson's receivership case and the *Purdue Pharma* bankruptcy do not end with the lack of consent or compensation. Rather, as discussed, both rely on courts' equitable authority, whether inherent in federal jurisprudence or codified in the Bankruptcy Code. Like Petitioner here, Peterson has a vested interest in ensuring that courts do not violate the core constitutional due process protections afforded litigants in the name of exercising their equitable powers. More so when the command to do equity is misinterpreted or distorted to allow wealthy tortfeasors to purchase immunity, to deprive litigants of their property interest without their day in court, and to prohibit ordinary citizens access to justice over their objections and without compensation.

INTRODUCTION AND SUMMARY OF ARGUMENT

The similarities between the nonconsensual release of claims in *Purdue Pharma* and in *Champion-Cain* are striking. As in *Purdue Pharma*, the released party in *Champion-Cain* is a joint tortfeasor with the receivership debtors and the released claims include fraud and other intentional torts. Like the objecting parties in *Purdue Pharma*, Peterson did not consent to release his claims against Chicago Title, let alone without being allowed to share in distributions funded by Chicago Title's settlement with the Receiver. Just as the complicit and wealthy Sackler family did in *Purdue Pharma*, Chicago Title also purchased a release from future liability with the untested and speculative justification that its settlement would compensate more claimants for a greater percentage of their losses immediately. And just like the Sackler Family did as nondebtors to tether the nonconsensual releases to the *res* in bankruptcy, Chicago Title also raised the hypothetical specter of indemnity claims against the receivership entities to tie the nonconsensual releases to the *res* in the receivership estate. Moreover, like the bankruptcy court in *Purdue Pharma*, the district court in *Champion-Cain* "wielded an extraordinarily powerful tool" by extinguishing claims against a third party without the consent of or compensation to the claim holders. *In re Purdue Pharma*, 69 F.4th 45, 86 (2d Cir. 2023).

On closer examination, the key distinction between the two cases—that one is a bankruptcy governed by the Bankruptcy Code while the other is a receivership subject to federal equitable jurisprudence—turns out to be one without a difference. This is because, though the courts in *Purdue Pharma* examined the propriety of the nonconsensual releases under the Bankruptcy Code, the provisions they primarily examined—11 U.S.C. §§ 105(a) and 1123(b)(6)—merely codify bankruptcy courts' inherent equitable authority. In short, the Second Circuit in *Purdue Pharma* relied on the *same* equitable powers as the district court in *Champion-Cain* to deem constitutional nonconsensual releases against an alleged intentional tortfeasor without consent from or compensation to the releasing parties.

As a result, this case presents the Court with a rare opportunity to evaluate and correct the troubling trend where courts ostensibly sitting in equity—whether overseeing a bankruptcy or a federal receivership—issue injunctive relief to solvent non-debtor or non-receivership defendants in the form of nonconsensual releases of third-party claims against them without the consent of or compensation to the claimholders. In the bankruptcy context, much of the debate about whether such releases are permissible focuses in the first instance about whether Congress authorized that relief in the Bankruptcy Code. But because the Code sections at issue merely codify courts' traditional equitable powers, the real quandary is the limits of federal courts' equitable powers. As discussed, nonconsensual releases were never traditionally part of equity jurisprudence, meaning a court sitting in equity has no power to approve them, whether under the guise of the Bankruptcy Code or based on implied equitable authority to oversee receiverships.

In both bankruptcy and receivership proceedings, nonconsensual third-party releases—especially where the barred parties are not compensated—violate litigants' constitutional rights by depriving them of their property interest without due process and just compensation. The practice of federal courts entering bar orders to enjoin or release third-party claims as part of settlements in bankruptcy and receivership proceedings—an unprecedented remedy neither seen nor authorized in traditional equity jurisprudence—allows solvent defendants to misuse the federal system to avoid liability to their victims. This Court should clarify that the inherent equitable authority of federal courts does not encompass the entry of nonconsensual bar orders enjoining claims against non-debtors or non-receivership defendants without compensation.

ARGUMENT

I. Courts Overseeing Bankruptcy and Receiverships Derive Their Equitable Powers From the Same Source.

Bankruptcy proceedings and equity receiverships have a common aim: to gather and safeguard the assets of a debtor for fair division among its creditors in a coordinated manner. *See SEC v. Wealth Mgmt. LLC*, 628 F.3d 323, 334 (7th Cir. 2010); *Brown, Bonnell & Co. v. Lake Superior Iron Co.*, 134 U.S. 530, 533–35 (1890). Receiverships date back to at least sixteenth century England, when they were used to protect remaindermen where the value of land was at risk of diminution. *See* Ralph E. Clark, *A Treatise on the Law and Practice of Receivers* § 4 at 4, § 309 at 516 (3d ed. 1959). Receiverships were later expanded to cover estates of indebted decedents and indebted corporations. *See* Garrard Glenn, *The Basis of Federal Receivership*, 25 Colum. L. Rev. 434, 438–46 (1925). Federal courts long used receiverships to reorganize corporate debtors before modern bankruptcy laws. *Burnrite Coal Briquette*, 274 U.S. 208, 217 (1927) (noting that federal courts appointed receivers under "general equity powers"); *accord Digital Media Sols., LLC v. S. Univ. of Ohio, LLC*, 59 F.4th 772, 773 (6th Cir. 2023).

Meanwhile, modern bankruptcy reorganization law originated with Section 77B of the Bankruptcy Act of 1934, which sought to codify the practices of equity receiverships. *Duparquet Huot & Moneuse Co. v. Evans*, 297 U.S. 216, 222–24 (1936). That section stated that a bankruptcy court's powers are those "which a Federal court would have had it appointed a receiver in equity of the property of the debtor[.]" *Id.* at 221. Today, bankruptcy laws serve as the primary method for this coordination of corporate debtors. *See* 1 Collier on Bankruptcy ¶ 1.01[1], at 1–4 (R. Levin & H. Sommer eds., 16th ed. 2022). Yet equity receiverships also remain prevalent throughout the country, particularly in the securities realm. *See, e.g., SEC v. Hardy*, 803 F.2d 1034, 1037 (9th Cir. 1986) (noting that many equitable receiverships involve SEC-initiated receiverships).

The shared legal roots of bankruptcy proceedings and equity receiverships gives courts overseeing them a common source for their authority: inherent equitable powers, also known as their residual authority. In the Bankruptcy Code, a bankruptcy court's residual equitable authority is codified in 11 U.S. §§ 105(a) and 1123(b)(6), which provisions are recognized to incorporate "the traditional standards in equity practice." *Taggart v. Lorenzen*, 139 S. Ct. 1795, 1801 (2019); *see also Young v. United States*, 535 U.S. 43, 50 (2002) (bankruptcy courts apply "the principles and rules of equity jurisprudence") (internal quotations omitted). For federal courts overseeing equity receiverships, the same equitable authority is provided in Federal Rule of Civil Procedure 66, which instructs receivers to follow "historical practices in federal courts." *See also* 28 U.S.C.§ 754 (establishing *in rem* jurisdiction while providing the court-appointed receiver with control over "all receivership property.").

In implicit recognition of the parallels between bankruptcy and receivership proceedings, district courts administering federal equity receiverships often look to bankruptcy law and related equity jurisprudence for guidance. *See, e.g., SEC v. Cap. Consultants, LLC*, 397 F.3d 733, 745 (9th Cir. 2005) (finding bankruptcy law "analogous" to, and therefore persuasive in, administrating receivership estates); *SEC v. Stanford Int'l Bank, Limited*, 927 F.3d 830, 840 (5th Cir. 2019) ("Courts often look to the related context of bankruptcy when deciding cases involving receivership estates."). Yet these same courts also ignore bankruptcy precedent when expedient, and without any reasoned explanation. For example, in *Champion-Cain*, the district court acknowledged that third-party releases are not permissible in the Ninth Circuit in bankruptcy cases. *Champion-Cain*, Order Overruling Objections *et al.*, ECF No. 926 at 13 (Nov. 22, 2022). But it nevertheless found that it had the power to release the claims against Chicago Title, asserting without explanation that it was not "bound by the strictures of bankruptcy law." *Ibid.*

Whereas receivership objectors frequently lack the wherewithal to seek review beyond the Circuit level, the grant of certiorari in *Purdue Pharma* allows this Court to recognize the reality that the constitutional validity of nonconsensual third-party releases is not just a question of bankruptcy law. Rather, the propriety of nonconsensual third party releases ultimately goes to the scope of all federal courts' equitable powers and their exercise in accordance with the United States Constitution for the simple reason that the source of the courts' equitable powers under the Bankruptcy Code and in equity receiverships is the *same*—that is, the "equity exercised by the High Court of Chancery in England at the time of the adoption of the Constitution and the enactment of the original Judiciary Act, 1789." *Grupo Mexicano de Desarrollo S.A. v. Alliance Bond Fund, Inc.*, 527 U.S. 308, 319 (1999).

II. Nonconsensual Third-Party Releases Were Not Traditionally Encompassed Within the Powers of Courts of Equity.

Traditional, historical equitable principles provide no basis for the remedy of enjoining or releasing third-party claims without consent or compensation in either the bankruptcy or the receivership context. Though Congress gave the lower federal courts original jurisdiction "of all suits . . . in equity," the "equitable powers conferred by the Judiciary Act of 1789 did not include the power to create remedies previously unknown to equity jurisprudence." *Grupo*, 527 U.S. at 332. As a result, all federal court's historical practice of equity looks to the principles applied by the English Court of Chancery before the Judiciary Act of 1789. *Gordon v. Washington*, 295 U.S. 30, 36 (1935); 28 U.S.C. § 41(1).

Nonconsensual non-debtor releases were not a remedy traditionally awarded by courts of equity. *Grupo*, 527 U.S. at 332–33; *Dow Corning*, 280 F.3d at 657 (non-debtor releases were "unprecedented in traditional equity jurisprudence"). Historically, a receivership court with *quasi*-in rem jurisdiction lacked the power to enjoin *in personam* suits against a debtor because that judgment would determine only their "personal liability" and would not "involve the possession or control" of the debtor's property. *Kline v. Burke Constr. Co.*, 260 U.S. 226 (1922); *Riehle v.*

Margolies, 279 U.S. 218, 223–28 (1929) (noting that "court sitting in equity" could not enjoin *in personam* suit against receivership debtor); *accord Penn Gen. Cas. Co. v. Commonwealth of Pennsylvania ex rel. Schnader*, 294 U.S. 189, 195 (1935). And as the Sixth Circuit recently noted, "[i]f a court lacked the power to enjoin in personam claims against a *receivership debtor*, it would make no sense to allow a court to enjoin in personam claims against *non-receivership entities*." *Digital Media*, 59 F.4th at 787.

Likewise, a "receivership court traditionally could issue injunctions to protect only the debtor assets that its creditors could execute upon. The court lacked any equitable power to 'protect assets outside the receivership.'" *Digital Media*, 59 F.4th at 787 (quoting *Greenbaum v. Lehrenkrauss Corp.*, 73 F.2d 285, 286 (2d Cir. 1934)). For example, the Second Circuit held that an injunction by a receivership court prohibiting a suit to liquidate an affiliate of a receivership debtor was "contrary to the whole theory of an equity receivership." *Greenbaum*, 73 F.2d at 287.

The debate at issue in this case—whether nonconsensual non-debtor releases are permissible under bankruptcy courts' residual authority codified in the Bankruptcy Code—shows that such releases are *not* grounded in traditional equity principles. As an initial matter, this debate is relatively recent. "The practice of enjoining suits between non-debtors seems to have long been considered improper even in the bankruptcy context, and non-debtor releases have obtained a judicial foothold only in the last several decades." *Digital Media*, 59 F.4th at 788. Second, circuit courts "on both sides recognize that only statutory authority—not any inherent equitable authority—can give bankruptcy courts the power to permit non-debtor releases." *Ibid.*

Yet inherent equitable authority is what receivership courts rely upon to enter these nonconsensual non-receivership debtor releases. Courts often point to the district court's "broad powers and wide discretion to determine . . . relief in an equity receivership. *SEC v. Safety Fin. Serv., Inc.*, 674 F.2d 368, 372–73 (5th Cir. 1982); *see also SEC v. Wenke*, 622 F.2d 1363, 1369 (9th Cir. 1980) (discussing courts' "inherent equitable authority" to fashion relief as according them discretion to approve releases against receivership entities). While this authority clearly extends to protecting the property placed in receiverships—for example, by barring litigation against the receivership itself—there is no basis in equitable jurisprudence for barring suits against non-receivership debtors over the objection of third parties. *Compare Wenke*, 622 F.2d 1369 (barring litigation against receivership entities) *with Digital Media*, 59 F.4th at 787 (denying bar order as to non-receivership debtors because it exceeded traditional equity principles). The "prohibition on enjoining unrelated, third-party claims without the third parties' consent . . . is a maxim of law not abrogated by the district court's equitable power to fashion ancillary relief measures." *Stanford Int'l Bank*, 927 F.3d at 842.

As the Fifth Circuit observed, "federal district courts have no greater power in equity receiverships to ignore these bedrock propositions, because a 'court in equity may not do that which the law forbids.'" *Id.*

at 842–43. A court sitting in equity can only exercise its powers in a way that comports with "the accepted principles of equity." *Gordon*, 295 U.S. at 36; *Pusey & Jones Co. v. Hanssen*, 261 U.S. 491, 500 (1923). Equity, then, does not allow courts to enjoin nonparties or "to craft a 'nuclear weapon' of the law." *Grupo*, 527 U.S. at 332. This principle should apply with equal force to bankruptcy courts exercising their residual equitable authority.

III. Nonconsensual Third-Party Releases Violate the Constitution in the Receivership Context as Much as in the Bankruptcy Arena.

Because the source of the courts' equitable powers in bankruptcy and federal equity receiverships is the same, and because the purposes of each are the same—to marshal assets, preserve value, and distribute them to creditors in a fair and equitable manner—this Court should clarify once and for all that bankruptcy courts and district courts overseeing receiverships as courts of equity are bound by the same rules prohibiting nonconsensual third-party releases. Alternatively, if they are not so bound, the Court should articulate the meaningful distinctions between the two schemes so that a receivership court can exercise its equity powers differently than those of a bankruptcy court and within its proscribed limits.

Whether in bankruptcy or in receivership proceedings, creditors with direct claims possess a "chose in action" which is "is a constitutionally recognized property interest possessed by each of the plaintiffs" under the Fifth and Fourteenth

Amendments. *Phillips Petroleum v. Shutts*, 472 U.S. 797, 807 (1985); *see also Tulsa Prof'l Collection Servs. v. Pope*, 485 U.S. 478, 485 (1988) ("Little doubt remains that a [cause of action] is property protected by the Fourteenth Amendment"). By extinguishing third party claims against solvent defendants without consent, courts deprive claimants of their property rights without due process as much in a bankruptcy reorganization as in a receivership proceedings.

One rejoinder is that due process only requires notice and opportunity to be heard, *Mullane*, 339 U.S. 306, 314 (1950), and courts generally require notice and allow parties to file objections to any proposed settlement with a bar order. *See, e.g., SEC v. Champion-Cain*, ECF No. 789, Order Directing Receiver to File Notice Plan (May 19, 2022); *In re Purdue Pharma L.P.*, 19-23649, ECF No. 2988, Order Approving [] Notice Procedures (Bankr. S.D.N.Y. June 3, 2021). Indeed, the district court in *Champion-Cain* found that due process was satisfied when Peterson was provided notice and an opportunity to be heard despite the summary nature of the receivership proceeding. *SEC v. Champion-Cain*, ECF No. 926, Order Overruling Obj. *et al.* at 13–14 (Nov. 22, 2022).

But where courts of equity enter bar orders, summary procedures such as those utilized by both courts here result in constitutional violations. First, as the Solicitor General persuasively argues, unless there is an opt-out provision from bar orders, all that is provided is the illusion of due process. Brief of United States at 42. Even when acting in equity, courts cannot approve a settlement by which two parties bargain away the rights of others who do not consent. As Justice Harlan wrote, "parties cannot, by giving each other consideration, purchase from a court of equity a continuing injunction." *Sys. Fed. No. 91, Ry. Employees' Dep't, AFL-CIO v. Wright*, 364 U.S. 642, 651 (1961). Second, a bar order does not lend itself to a summary proceeding because it is essentially a final adjudication on the merits of those claims in favor of the released party. *In re Digital Impact, Inc.*, 223 B.R. 1, 12, 13 (N.D. Okla. 1998). Under such circumstances, the barred parties are entitled to an actual adjudication of their rights through an adversarial process based on admissible evidence. *United States v. City of Hialeah*, 140 F.3d 968, 977 (11th Cir. 1998) ("a nonconsenting party's rights cannot be abrogated merely upon a showing of a prima facie case; that can only be done in a judgment entered following trial (or summary judgment"). Thus, use of summary procedures when nonconsensual third-party releases are at stake cannot comport with due process. *See In re Sportstuff, Inc.*, 430 B.R. 170, 181 (B.A.P. 8th Cir. 2010) (finding that the "opportunity to object to a settlement does not take the place of a trial on the merits").

This Court's jurisprudence in other areas of the law confirms this result. In *Local No. 93 v. City of Cleveland*, 478 U.S. 501, 529 (1986), a civil rights case involving a consent decree, this Court stated that "[o]f course, parties who choose to resolve litigation through settlement may not dispose of the claims of a third party, and *a fortiori* may not impose duties or obligations on a third party, without that party's agreement." Likewise, in securities fraud class actions, courts hold that they lack the power to bar non-settling parties' independent claims. *See Heritage*

Bond, 546 F.3d at 676–80 (assessing power to bar independent claims under federal common law); *AAL High Yield Bond Fund v. Deloitte & Touche LLP*, 361 F.3d 1305, 1311–12 (11th Cir. 2004) (partial settlement cannot bar independent claims of non-settling parties); *Gerber v. MTC Elec. Techs. Co.*, 329 F.3d 297, 305–07 (2d Cir. 2003) (same). Finally, in class actions, due process requires that a plaintiff be "provided with an opportunity to remove himself from the class." *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 812 (1985).

This country has a "deep-rooted historic tradition that everyone should have his own day in court." *Martin v. Wilks*,490 U.S. 755, 761–62 (1989). This is why courts recognize that the "right to proceed in court should not be denied except under the most extreme circumstances." *Klein v. Adams & Peck*, 436 F.2d 337, 339 (2d Cir. 1971). Nevertheless, what should be rare is now becoming the rule in bankruptcy reorganizations such as the one at issue and in five other circuits that have held that nonconsensual third-party releases are permissible in at least some circumstances. *See, e.g., In re Millennium Lab Holdings II, LLC*, 945 F.3d 126, 139 (3d Cir. 2019); *In re A.H. Robins Co.*, 880 F.2d 694, 701–02 (4th Cir. 1989); *In re Dow Corning Corp.*, 280 F.3d 648, 656–60 (6th Cir. 2002); *In re Airadigm Commc'ns, Inc.*, 519 F.3d 640, 655–57 (7th Cir. 2008); *In re Seaside Eng'g & Surveying, Inc.*, 780 F.3d 1070, 1075–79 (11th Cir. 2015). And such releases have likewise become commonplace in receiverships generally. *See, e.g., Zacarias v. Stanford Int'l Bank, Ltd.*, 945 F.3d 883 (5th Cir. 2019); *SEC v. DeYoung*, 850 F.3d 1172, 1183 n.5 (10th Cir. 2017) (collecting cases where district courts entered bar orders in favor of third parties to secure settlements); *SEC v. Aequitas Mgmt., LLC*, 2020 WL 7318305, at *1 (D. Or. Nov. 10, 2020) (citing numerous district court receivership actions that barred third-party claims).

The remaining justifications for approving nonconsensual releases without compensation also hold little water. For example, the notion that the release of claims allows the released party to make a greater contribution is belied by the developments in the instant case, where holdout states were able to leverage even more contributions from the Sackler family pending the Second Circuit's decision. The possibility of courts refusing to approve a nonconsensual release against the remaining objectors without compensation would presumably also force at least additional contributions to compensate the claimholders for releasing their claims. Likewise, the notion that any indemnification or contribution claims by wrongdoers against the debtor or the receivership entities sufficiently links non-debtors to the *res* is too attenuated to defeat the rights of third parties against those wrongdoers. As the Sixth Circuit has recognized, any view in which a joint tortfeasor can sue an accomplice for the harms it has caused a third party and then "settle" with the accomplice to eliminate its liability to the third party "is quite wrong." *Digital Media*, 59 F.4th at 784.

Particularly where fraud or other claims alleging intentional wrongdoing are the subject of the release, tort victims should not be deprived of their day in court without consent. Sometimes the "day in court" is what tort victims truly seek, and their ability to bring a wrongdoer to trial should not be bargained away by someone else, especially without due process and just compensation. Nonconsensual third-party releases do not align with the Constitution nor traditional practices of equity. Both a non-debtor in bankruptcy and a non-receivership debtor should have to pay for the consent to the permanent and broad-ranging release from liability it seeks. Absent consent, the courts should allow parties to opt out or provide a true adjudication on the merits before releasing or barring such claims.

CONCLUSION

This Court should reverse the Second Circuit and confirm, once and for all, that the equitable powers of *all* federal courts of equity are subject to the same limits regarding the approval of nonconsensual third-party releases to third parties, whether in the context of a bankruptcy or a receivership proceeding. Alternatively, this Court should clarify the meaningful difference that has yet to be articulated between the equitable powers codified in the Bankruptcy Code governing bankruptcy courts' ability to approve nonconsensual third-party releases without compensation verses the equitable powers implicitly conferred upon federal courts overseeing equity receiverships to do so.

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Respectfully submitted,

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