No. 24-1062

In the
Supreme Court of the United States

THE HERTZ CORPORATION, et al.,

Petitioners,

v.

WELLS FARGO BANK, N.A., U.S. BANK NATIONAL ASSOCIATION,

Respondents.

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

REPLY BRIEF

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

REPLY BRIEF

The brief in opposition confirms the need for this Court's review. It concedes that a "host of additional decisions" have disagreed with the panel majority, that there is "arguable tension" between the decision below and the Second Circuit's reasoning in *LATAM*, and that the panel majority's "emphasis on principles of absolute priority" (which it barely defends) is wholly absent from the other divided decisions that have reached the same wrong result. BIO.17-21 & n.4. And while it attempts to dispute the importance of the question presented, it cannot deny that the issue implicates fundamental principles of bankruptcy law and statutory interpretation, has recurred in multiple cases, and has repeatedly determined the distribution of hundreds of millions of dollars. This Court should grant certiorari.

I. The Decision Below Contravenes Clear Text And Settled Precedent.

1. The panel majority's decision contradicts the plain text of the Bankruptcy Code and this Court's settled precedent. The Code is unambiguous. A claim must be disallowed "to the extent that … such claim is for unmatured interest," regardless of whether the debtor is solvent or notions of absolute priority. 11 U.S.C. §502(b)(2). And the text is clear and precedent is unanimous that a creditor whose claim is disallowed *by the Code* is not impaired, because impairment depends on whether "*the plan* … leaves unaltered the legal, equitable, and contractual rights to which such claim … entitles the holder," not what the Code does. *Id.* §1124(1) (emphasis added). The panel unanimously recognized that under that clear

statutory text, the claims here sought unmatured interest, that they were therefore disallowed under §502(b)(2), and that disallowance by the Code did not create impairment. App.16-22, 30 n.20. That should have ended this case. *Nat'l Ass'n of Mfrs. v. Dep't of Def.*, 583 U.S. 109, 127 (2018) (statutory construction "begins with the statutory text," and when the text is unambiguous, "ends there as well").

Instead of stopping there, the panel majority held that "the pre-Code absolute priority rule"—which the majority deemed "enacted" into the Code via §1129(b)—entitles creditors to "be paid in full" *even on claims that the Code disallows* before junior claimants "take anything at all." App.24-25, 35. That contravenes not only §502(b)(2) and §1124(1), but also §1129(b) itself, which explicitly applies only to *impaired* creditors and which this Court has already recognized "does not codify any authoritative pre-Code version of the absolute priority rule." *Bank of Am. Nat'l Tr. & Sav. Ass'n v. 203 N. LaSalle St. P'ship*, 526 U.S. 434, 448 (1999); *see* Pet.16-17. And the panel majority's elevation of pre-Code practice over the Code's text cannot be squared with this Court's precedent, which makes clear that pre-Code practice plays zero role when there is "no textual ambiguity" to resolve. *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 566 U.S. 639, 649 (2012); *see* Pet.18. The panel majority also misread this Court's decision in *Czyzweski v. Jevic Holding Corp.*, 580 U.S. 451 (2017), which confirms that absolute priority under the Code operates *subject to* the Code's statutory disallowance and impairment provisions, not vice-versa. Pet.18-20.

2. Strikingly, Wells Fargo barely defends the panel majority's *sua sponte* reasoning, preferring instead to champion the arguments it advanced below that the panel unanimously rejected. It spends only a page in defense of the panel majority's reasoning, and that scant discussion does not even mention §1129(b) or *Jevic*, despite the panel's heavy reliance on both. That silence all but admits that the panel's reasoning is untenable.

Rather than defend the panel majority's reasoning, Wells Fargo recasts it as holding that the plan was required to respect Wells Fargo's "equitable … rights" to leave it unimpaired under §1124(1). BIO.12. But the panel majority barely mentioned that "equitable … rights" language, and certainly did not ground its absolute-priority reasoning on that provision. The reason is clear: The Code disallows *all* claims "for unmatured interest," whether premised on legal or equitable rights. 11 U.S.C. §502(b). As the panel majority recognized, that disallowance by the Code does not create plan impairment under §1124(1). *See infra* pp.___. Undeterred, the panel majority elevated the pre-Code absolute priority rule over the text of §502(b)(2). That was error. Pet.14-21.

Wells Fargo asserts that the panel majority was "cognizant" of the principle that pre-Code practice cannot be used as an "extratextual supplement." BIO.12. But that is precisely why the panel majority strained so hard to insist that §1129(b) "incorporates the common law absolute priority rule," App.32—a maneuver Wells Fargo cannot bring itself to defend, presumably because this Court has already rejected it, *see 203 N. LaSalle*, 526 U.S. at 448.

3. Instead of defending the panel majority's *sua sponte* reasoning, Wells Fargo reiterates the argument it made below, denying the well-established difference between plan impairment (which creates an impaired class) and Code disallowance (which does not). BIO.13-14. The panel unanimously rejected that misguided theory, *see* App.30 n.20; App.45—as has a "monolithic mountain of authority" from *every court to address the question*, and the leading treatise on the issue to boot. *In re Ultra Petroleum Corp.*, 943 F.3d 758, 760, 763-64 (5th Cir. 2019); *see also, e.g.*, *In re PG&E Corp.*, 46 F.4th 1047, 1063 n.11 (9th Cir. 2022). That is why Wells Fargo acknowledges, with considerable understatement, that "various" lower courts have rejected its theory, by which it means *all* of them. BIO.13-14.

That unanimity is unsurprising, because Wells Fargo's theory is obviously wrong. Wells Fargo asserts that the well-established distinction between "Code impairment" and "plan impairment" has "no basis in the Bankruptcy Code." BIO.13. But that distinction comes directly from the text of §1124(1), which leaves a claim unimpaired as long as "*the plan* … leaves unaltered" the claimant's rights, regardless of how *the Code* may alter those rights. 11 U.S.C. §1124(1) (emphasis added); *see Ultra*, 943 F.3d at 763. A plan that simply "incorporates the Code's disallowance provisions" does not itself impair the claimant's rights. *Ultra*, 943 F.3d at 762. *Contra* BIO.14. Regardless, if Wells Fargo's Code-impairment argument were correct, it would mean that multiple circuit decisions, including the decision below, are erroneous, and only strengthen the case for plenary review.

4. Wells Fargo next invokes "the Code's basic structure," but that structure undermines its arguments. The panel majority's theory would work havoc across the Code, effectively eliminating its disallowance provisions in every solvent-debtor case. Pet.21-23. Wells Fargo offers no response to that obvious problem.

Instead, Wells Fargo asserts that enforcing the Code's disallowance provisions would leave unimpaired creditors "worse off" than impaired creditors, because impaired creditors receive specific statutory protections. BIO.14-15. But impaired creditors receive those protections *because they are impaired*; unimpaired creditors do not receive those statutory protections, because (by definition) the plan affords unimpaired creditors everything they are entitled to obtain under the Code. *See* 11 U.S.C. §1124(1). The Code does not entitle unimpaired creditors to "full repayment" or "absolute priority," but that is because explicit Code provisions disallow certain claims. *See, e.g.*, *Ultra*, 943 F.3d at 763.

Wells Fargo also suggests that applying the Code by its terms would leave unimpaired creditors—but not impaired creditors—entitled to no post-petition interest at all. BIO.15-17. If that were true, it would be a result compelled by clear text, as at least two judges have suggested. *See PG&E*, 46 F.4th at 1068-75 (Ikuta, J., dissenting); App.44 n.1. The better view, however (and the view reflected in the actual plan proposed and approved by the bankruptcy court here), is that the disallowance of claims "*for* unmatured interest," 11 U.S.C. §502(b)(2) (emphasis added), does not affect creditors' rights to post-petition interest *on* their *allowed* claims at the rate that the Code envisions in solvent-debtor cases, which is the federal judgment rate, *see* 11 U.S.C. §726(a)(5); App.75-76; *see also In re Cardelucci*, 285 F.3d 1231, 1234-36 (9th Cir. 2002). But the one thing the Code does not allow is resurrecting the same claims for contractual interest that §502(b) unambiguously disallows via the pre-Code absolute priority rule. That result is plainly wrong, Pet.14-23, and this Court should not allow that error to stand.

II. The Decision Below Contributes To The Growing Confusion In The Lower Courts.

1. The decision below not only erred, but further deepened the ongoing conflict and confusion in the lower courts. Wells Fargo does not dispute that numerous courts have held that the plain text of §502(b) applies to limit or disallow claims even when the debtor is solvent, and that those decisions cannot be squared with the panel majority's novel understanding of the absolute-priority rule. Pet.24-26. Instead, Wells Fargo dismisses that "host of additional decisions" in a footnote as mostly "nonprecedential" district-court and bankruptcy-court decisions. BIO.21 n.4. But it is hardly surprising that district courts and expert bankruptcy courts have faced this issue more often than the courts of appeals—and as Wells Fargo tacitly concedes, those most familiar with the Code and practicalities of bankruptcy have routinely reached the opposite of the panel majority's conclusion. Pet.24-26.

In any event, the panel majority's decision also conflicts with federal circuit precedent. In *Cardelucci*, for example, the Ninth Circuit held that an unsecured creditor in a solvent-debtor Chapter 11 case was entitled to recover post-petition interest only at "the legal rate" under 11 U.S.C. §726(a)(5), which the Ninth Circuit concluded was the federal judgment rate rather than the state statutory interest rate that would have applied outside of bankruptcy. 285 F.3d at 1234-36. That holding cannot be reconciled with the panel majority's contrary conclusions that "creditors' obligations [must] be paid in full" if the debtor is solvent, and that creditors in solvent-debtor cases are entitled to "the equitable rate of post-petition interest, whatever that may be" rather than the federal judgment rate. App.35. Recognizing that problem, Wells Fargo (like the Ninth Circuit in *PG&E*) tries to avoid it by limiting *Cardelucci* to impaired creditors. BIO.21 n.4. But even with that limitation, *Cardelucci* still squarely conflicts with the panel majority's conclusion that the absolute-priority rule entitles creditors to post-petition interest at their contractual or state-law rates (or some other equitable rate) before junior claimants receive anything—a rule that would have required the opposite result in *Cardelucci* itself.

2. Wells Fargo likewise has no persuasive answer to the stark conflict between the decision below and the Second Circuit's decision in *LATAM*—which is why Wells Fargo concedes the "arguable tension" between the two decisions. BIO.21. That is again a considerable understatement. As Wells Fargo recognizes (and the panel majority admitted), the Second Circuit in *LATAM* squarely rejected the panel

majority's view that the Bankruptcy Code "incorporates the common law absolute priority rule" and "requires creditors' obligations be paid in full before owners … take anything at all." App.32, 35; *see* 55 F.4th 387-89 (rejecting the argument that a "solvent-debtor exception aris[ing] from the absolute priority rule" requires paying post-petition interest at contract rates "whenever a plan will return value to equity"); App.30 n.19; App.34 n.22 ("The Second Circuit disagreed in *LATAM*[.]"). Instead, the Second Circuit correctly recognized that "[t]he Code does not codify any authoritative pre-Code version of the absolute priority rule," 55 F.4th at 388 (quoting *203 N. LaSalle*, 526 U.S. at 448), and that instead "[u]nder the Code, the absolute priority rule comes into effect only when a class of impaired creditors votes to reject a plan," *id.* That is the exact opposite of the rule the Third Circuit adopted below. Pet.26-29.

Wells Fargo attempts to downplay that stark division by claiming that there is no "conflict in bottom-line results" between the decision below and *LATAM*, because the Second Circuit ultimately found the debtor in *LATAM* insolvent. BIO.21. But Wells Fargo concedes the *LATAM* creditors "might have prevailed" under the panel majority's approach, making clear that the split *does* have real-world consequences. BIO.20. And while Wells Fargo suggests petitioners might not have prevailed in the Second Circuit, BIO.20, that suggestion assumes the Second Circuit would adopt a solvent-debtor exception based on some *other* rationale, which *LATAM* declined to do, *In re LATAM Airlines Group S.A.*, 55 F.4th 377, 383 (2d Cir. 2022) ("We have not yet addressed whether the solvent-debtor exception survived the enactment of the Code.”). Whatever the Second Circuit may do concerning a solvent-debtor exception, it has squarely rejected an absolute-priority exception, putting it in acknowledged conflict with the decision below.

3. Last but not least, the panel majority’s novel reasoning underscores the disarray in the lower courts on this issue. Pet.29-31. Although the majorities in all three divided decisions agreed on the bottom-line result (each time drawing a sharp and persuasive dissent), they markedly diverged in their explanation for that result, with the panel majority below declining to embrace the reasoning of the Fifth and Ninth Circuits and instead relying on absolute-priority principles that no other circuit has adopted. Pet.31; *see* App.24-35.

Wells Fargo acknowledges that “inconsistency,” but insists it does “not warrant this Court’s intervention.” BIO.17. But that inconsistency does not stand alone, and it underscores that once courts abandon plain text in favor of pre-Code practices, inconsistent reasoning is all but guaranteed. If legislative history is akin to identifying friends at a cocktail party, *see Conroy v. Aniskoff*, 507 U.S. 511, 519 (1993) (Scalia, J., concurring in the judgment), courts can even more readily identify some pre-Code practice they prefer to the result compelled by the statutory text.

Alternatively, Wells Fargo tries to dismiss the conflict in reasoning as “an issue of nomenclature, rather than substance.” BIO.18. That assertion blinks reality. The Third Circuit had the benefit of the *Ultra* and *PG&E* decisions and consciously departed from their solvent-debtor-exception reasoning by opting for an absolute-priority-rule exception instead. That conscious departure was prompted by a recognition that this Court's cases reject a free-floating embrace of pre-Code practice in the face of clear text like that of §502(b). Accordingly, the Third Circuit chose to disregard §502(b) in favor of the novel theory that the Bankruptcy Code "incorporates the common law absolute priority rule." App.32. That theory has its own problems—including creating a conflict with both *LATAM* and this Court's decision in *203 N. LaSalle*, 526 U.S. at 448 ("[T]he Code does not codify any authoritative pre-Code version of the absolute priority rule."). That conscious departure cannot be dismissed as a difference of nomenclature.

The difference in reasoning also had different consequences when it comes to the flexibility of future courts in departing from contractual interest rates. The panel majority broke with the Fifth Circuit (and joined the Ninth Circuit) by adding an atextual exception to its atextual rule, using the equitable roots of the absolute-priority rule to allow courts to employ "compelling equitable considerations" to deviate from contractual interest rates and award post-petition interest at "the equitable rate … whatever that may be." App.35-36; *see* Pet.31. Wells Fargo minimizes that second-order conflict by proclaiming it "unclear whether the Fifth Circuit has categorically rejected the possibility that equitable considerations could justify a departure from the contract rate of interest." BIO.19. But *Ultra* alone among the three cases "did not mention the possibility of any such equitable exception," BIO.18, and its reasoning does not leave any room for equitable departures. *In re Ultra*

Petroleum Corp., 51 F.4th 138, 160 (5th Cir. 2022). Wells Fargo suggests that this subsidiary conflict is irrelevant, because the decision below took the more debtor-friendly approach. BIO.19. But this subsidiary conflict just underscores the confusion that is inevitable when courts depart from the plain text.

In short, Wells Fargo has no answer to the straightforward reality that "trial and appellate courts have reached different conclusions" as to whether the pre-Code solvent-debtor exception survived the enactment of the Code, and "will likely continue to do so until the issues are finally determined by the Supreme Court or Congress amends the statute." *In re Mullins*, 633 B.R. 1, 3-4 (Bankr. D. Mass. 2021). This Court should grant certiorari and end that acknowledged conflict.

III. The Question Presented Is Exceptionally Important.

Wells Fargo also cannot meaningfully dispute the recurring and exceptionally important nature of the question presented. It concedes that this issue has arisen repeatedly in the lower courts and has determined the distribution of hundreds of millions of dollars in multiple cases. BIO.21; *see* Pet.32-33. Massive financial stakes "standing alon[e]" may not be enough to warrant certiorari, BIO.21, but a recurring legal issue on which the lower courts are divided that *also* regularly implicates nine-figure sums is well worth this Court's attention.

Wells Fargo asserts that the obvious adverse consequences of the decision below are "entirely speculative," claiming that there is "no evidence" that the panel majority's approach has caused "undue administrative complexity or produced wasteful litigation" to date. BIO.22. But the "administrative nightmare" that bankruptcy courts will face if they must apply a plethora of varying contractual or state-law post-petition interest rates (with potential equitable deviations) in solvent-debtor cases is beyond obvious, especially when it may not be clear whether a particular debtor is solvent at all. *Cardelucci*, 285 F.3d at 1236; *see* Pet.33-34. It is hardly "speculative" to recognize the manifold complications and opportunities for litigation that the decision below creates. *Contra* BIO.22.

Finally, Wells Fargo falls back on this Court's denial of certiorari in *Ultra* and *PG&E*. BIO.22. But the decision below changes the calculus by rejecting the reasoning of both *Ultra* and *PG&E* in favor of an absolute-priority approach that opens a conflict with this Court's decision in *203 N. LaSalle* and the Second Circuit in *LATAM*, all while blaming the result on this Court's decision in *Jevic*, a maneuver Wells Fargo neither acknowledges nor defends. In short, further percolation produced the decisions below—a decision by an experienced bankruptcy judge who carefully reviewed and rejected *Ultra* and *PG&E* only to be reversed by a decision rejecting the reasoning of those decisions in favor of a novel absolute-priority exception that no one briefed and Wells Fargo barely defends. Those developments make crystal clear that further percolation will only beget further confusion and conflict. The time has come to restore clarity and predictability on this important and recurring issue.

CONCLUSION

This Court should grant certiorari.

Respectfully submitted,

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