No. 19-391

IN THE
Supreme Court of the United States

ASSURED GUARANTY CORP.; ASSURED GUARANTY MUNICIPAL CORP.; AND NATIONAL PUBLIC FINANCE GUARANTEE CORPORATION,

Petitioners,

v.

FINANCIAL OVERSIGHT AND MANAGEMENT BOARD FOR PUERTO RICO, ET AL.,

Respondents.

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

REPLY BRIEF IN SUPPORT OF CERTIORARI

MARK C. ELLENBERG
HOWARD R. HAWKINS, JR.
WILLIAM J. NATBONY
ELLEN M. HALSTEAD
THOMAS J. CURTIN
CASEY J. SERVAIS
CADWALADER, WICKERSHAM & TAFT LLP
200 Liberty Street
New York, NY 10281

Counsel for Assured Guaranty Corp. and Assured Guaranty Municipal Corp.

NEAL KUMAR KATYAL
Counsel of Record
MITCHELL P. REICH
REEDY C. SWANSON
DANIELLE DESAULNIERS STEMPEL*
HOGAN LOVELLS US LLP
555 Thirteenth Street, N.W.
Washington, D.C. 20004
(202) 637-5600
neal.katyal@hoganlovells.com

Counsel for Petitioners

** Admitted only in Maryland; practice supervised by principals of the firm admitted in D.C.*

Additional counsel listed on inside cover

JONATHAN POLKES
MARCIA GOLDSTEIN
GREGORY SILBERT
KELLY DIBLASI
GABRIEL A. MORGAN
WEIL, GOTSHAL &
MANGES LLP
767 Fifth Avenue
New York, NY 10153

Counsel for National Public Finance Guarantee Corporation

THOMAS P. SCHMIDT
HOGAN LOVELLS US LLP
390 Madison Ave.
New York, NY 10017

Counsel for Petitioners

RULE 29.6 DISCLOSURE STATEMENT

The Rule 29.6 disclosure statement in the petition remains accurate.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

TABLE OF AUTHORITIES—Continued

Page(s)

OTHER AUTHORITIES:

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

IN THE
Supreme Court of the United States

No. 19-391

ASSURED GUARANTY CORP.; ASSURED GUARANTY MUNICIPAL CORP.; AND NATIONAL PUBLIC FINANCE GUARANTEE CORPORATION,

Petitioners,

v.

FINANCIAL OVERSIGHT AND MANAGEMENT BOARD FOR PUERTO RICO, ET AL.,

Respondents.

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

REPLY BRIEF IN SUPPORT OF CERTIORARI

INTRODUCTION

As Judge Lynch explained, this case presents an issue "of extraordinary importance." Pet. App. 83a (Lynch, J., dissenting from denial of rehearing en banc). It affects not only "Title III proceedings in the Commonwealth," but the enforceability of "special revenue bonds nationwide," the property rights of numerous bondholders, and the credit of municipalities themselves. *Id.* "[F]urther review is warranted * * * by the Supreme Court." *Id.*

The Board contends that the petition overstates matters because the credit downgrades the decision immediately precipitated affected only about $8.5 *billion* in municipal debt. That contention is self-refuting. More than that, these initial downgrades are just a harbinger of the much greater upheaval to come if the decision below is allowed to stand. *See* Sec. Indus. & Fin. Mkts. Ass'n (SIFMA) Amicus Br. 2-5. Indeed, the proper answer to the question presented undergirds trillions of dollars of municipal debt, and vehicles for this Court to take that question up are scarce. The Court should seize this opportunity.

The Board also tries to muddy the extent of the longstanding consensus against the First Circuit's position. It offers a blinkered reading of *In re Jefferson County*, 474 B.R. 228 (Bankr. N.D. Ala. 2012) that ignores the decision's plain holding. And it quibbles with just how lopsided the split in the commentariat is in petitioners' favor. But the Board does not and cannot disturb a fundamental point: The First Circuit's decision is aberrant, wrong, and hugely consequential.

The Court should grant certiorari in this case and in *Ambac Assurance Corp.* v. *Financial Oversight & Mgmt. Bd. for Puerto Rico*, No. 19-387, and reverse the judgment below.

ARGUMENT

I. THE DECISION BELOW UPSET THE ESTABLISHED UNDERSTANDING OF SECTION 922(d).

The petition explains that the First Circuit departed from the overwhelming consensus among courts,

commentators, and investors that Section 922(d) permits the continued enforcement of special revenue bonds during the pendency of a municipal bankruptcy proceeding. Pet. 14-19. The Board offers little in response. It does not dispute that the First Circuit upset the understanding shared by numerous leading authorities. Opp. 15-16. And it *admits* that the First Circuit's decision led to the downgrade of billions of dollars of municipal revenue bonds, *id.* at 3-4, 30-32—as stark a demonstration as one can imagine that the decision upset settled market expectations. The Board resorts to flyspecking a few authorities to make the First Circuit's departure appear less severe, but none of those efforts at minimization succeeds.

The Board first contends that *Jefferson County* "did not even address the question of whether § 922(d) requires a debtor to turn over pledged special revenues." Opp. 11. That assertion cannot survive examination of the opinion, which expressly states that Section 922(d) "*required* payments of the Net [Special] Revenues to the Indenture Trustee," adds that such funds were "*not protected* from further actions by [the creditors' representative] to acquire them from the County," and rejects the very section of Collier's treatise on which the Board relies here. *In re Jefferson County*, 474 B.R. at 271-272 (emphases added); *see id.* at 267 n.15. Indeed, the Board's own authority recognizes that *Jefferson County* sided with petitioner's view on this question. *See* 6 Collier on Bankruptcy ¶ 922.05 (16th ed. 2019 update).

The Board also claims that a 2011 white paper from the National Association of Bond Lawyers embraced its view of Section 922(d). *See* Opp. 12-13.

Even that white paper was at best equivocal on this point, observing that creditors can require the turnover of special revenues by "court order." Nat'l Ass'n of Bond Lawyers, Municipal Bankruptcy: A Guide for Public Finance Attorneys 53-54 (2011). And the Board curiously neglects to mention that, in 2015, the Association abandoned even that equivocal embrace of the Board's position, observing instead that although "[m]unicipal debtors *have argued* that" continued payment is not required * * * [t]he bankruptcy court in *Jefferson County* rejected this argument." Nat'l Ass'n of Bond Lawyers, Municipal Bankruptcy: A Guide for Public Finance Attorneys 49 (3d. ed. 2015) (emphasis added).

The Board's other authorities are equally unhelpful. In *Examining Chapter 9 Municipal Bankruptcy Cases*, the author stated—in direct contradiction of the Board's position here—that Section 922 "*ensur[es]* that * * * special revenues remain subject to their interests and are *not* diverted to pay a municipality's general obligations." Francisco Vazquez, *Examining Chapter 9 Municipal Bankruptcy Cases*, 2011 WL 5053640, at *15 (emphases added). Contrary to the Board's suggestion (at 13), James Spiotto has specifically *disagreed* with the First Circuit's decision below. Pet. 29. And the Board's remaining sources (at 15) simply use the word "may" in passing when discussing Section 922(d); they do not state or suggest that Section 922(d) is *limited* to permitting voluntary payments. *See* Admin. Office of the U.S. Courts, Bankruptcy Basics 51 (rev. 3d ed. 2011); Fed. Judicial Ctr., Navigating Chapter 9 of the Bankruptcy Code 87 (1st ed. 2017).

That leaves the Board with nothing but Collier's treatise. But, as the petition explained, that treatise rests its conclusion on an (incorrect) analysis of legislative history, not statutory text. Pet. 19. And however authoritative Collier may be on some matters, its view on this issue has been comprehensively rejected by other commentators. The Board itself concedes that three leading sources, including the Bankruptcy Code Manual, squarely reject Collier's position. Opp. 15 & n.4. And although the Board claims that four other sources summarize "various views" on this question, *id.* at 16 & n.6, the only "view" they identify as supportive of the Board's position is Collier's, with which those sources express disagreement.[1]

Finally, to the extent the legal authorities leave any doubt, the response of ratings agencies to the decision below eliminates any question that the First Circuit's decision upset settled expectations. In response to the decision below, Moody's Investor Service has already downgraded the ratings of more than $8.5 *billion* in special revenue bonds.[2] That is

---

[1] *See* Kevin A. Kordana, *Tax Increases in Municipal Bankruptcies*, 83 Va. L. Rev. 1035, 1050 n.77 (1977); Alexander D. Flaschsbart, *Municipal Bonds in Bankruptcy: § 902(2) and the Proper Scope of "Special Revenues" in Chapter 9*, 72 Wash. & Lee L. Rev. 955, 990 & n.189 (2015); Robert S. Amdursky, *The 1988 Municipal Bankruptcy Amendments: History, Purposes, and Effects*, 22 Urb. Law. 1, 13 (1990); David L. Dubrow, *Chapter 9 of the Bankruptcy Code: A Viable Option for Municipalities in Fiscal Crisis?*, 24 Urb. Law. 539, 572-573 (1992).

[2] *Rating Action: Moody's Downgrades Cleveland, OH's Senior Lien Water Revenue Bonds to Aa2; Outlook Stable*, Moody's Investors Service (July 29, 2019),

hardly an "ordinary" reaction to a single court of appeals decision that supposedly reflects the prevailing interpretation of the law. Opp. 34. And it is just the tip of the multi-trillion-dollar iceberg. As another bond ratings agency explained, the initial response to the First Circuit's decision was likely "restrained" because market participants assume that Assured "will appeal and successfully overturn

---

https://www.moodys.com/research/Moodysdowngrades-Cleveland-OHs-senior-lien-waterrevenue-bonds-to--PR_905922284; *Rating Action: Moody's Downgrades Granite City (City of) Wastewater Treatment Plant Enterprise, IL's Revenue Bonds to A2*, Moody's Investors Service (July 22, 2019), https://www.moodys.com/research/Moodys-downgrades-Granite-City-City-of-Wastewater-Treatment-Plant-Enterprise--PR_905937760; *Rating Action: Moody's Downgrades to A2 the Rating on Johnsonville (City of) SC Water & Sewer Enterprise's Revenue Debt*, Moody's Investors Service (July 2, 2019) https://www.moodys.com/research/Moodys-downgrades-to-A2-the-rating-on-Johnsonville-City-of--PR_905930140; *Rating Action: Moody's Downgrades to Aa2 Dallas Waterworks & Sewer Enterprise, TX's Revenue Bonds; Outlook Stable*, Moody's Investors Service (June 26, 2019), https://www.moodys.com/research/Moodys-downgrades-to-Aa2-Dallas-Waterworks-Sewer-Enterprise-TXs-revenue--PR_905914053; *Rating Action: Moody's Downgrades Illinois State Toll Highway Authority to A1 and Assigns A1 Rating to Toll Highway Senior Revenue Bonds, 2019 Series A; Outlook Stable*, Moody's Investors Service (May 31, 2019), https://www.moodys.com/research/Moodysdowngrades-Illinois-State-Toll-Highway-Authority-to-A1-and--PR_905818650; *see Rating Action: Moody's Places 8 Ratings Under Review for Downgrade in Wake of Recent Court Ruling on Special Revenue Pledges*, Moody's Investors Service (May 13, 2019), https://www.moodys.com/research/Moodys-places-8-ratings-underreview-for-downgrade-in-wake--PR_905836610.

this ruling."[3] Indeed, a source the Board cites (at 30, 34) recognizes that investors are unlikely to "ignore[]" the "highly visible * * * risks" created by the First Circuit's decision, and recommends that investors begin "shift[ing]" their portfolios towards other investments. Guggenheim Investments, *Municipal Bonds: Unwavering Demand* (Aug. 22, 2019); *see also* Gunjan Banerji, *Muni-Bond Ratings Are All Over The Place. Here's Why.*, Wall St. J. (Dec. 6, 2019) (reporting that the First Circuit's decision has "undercut assumptions about how muni bonds would fare in bankruptcy" and "shaken" investors' confidence).

Remarkably, the Board claims that a cascade of multi-billion-dollar credit downgrades is too minimal an economic consequence to merit this Court's attention, because other segments of the multi-trillion-dollar municipal bond market have not been affected. Opp. 29-30. But the Court does not need an entire sector of the Nation's economy to topple before granting certiorari; demonstrable evidence of billions of dollars in upset expectations is "important" enough. S. Ct. R. 10(a). And, in any event, the Board's denominator of "a million municipal bonds," Opp. 31, is markedly inflated, as it includes general obligation bonds, which comprise a sizable portion of the municipal bond market and which are not implicated by Section 922(d).

The Board also ignores the damage that the First Circuit's decision will wreak on the market for *new*

---

[3] Comment, Kroll Bond Rating Agency, First Circuit Follies: Puerto Rico Ruling Slams Municipal Investors . . . Again 2 (Apr. 2, 2019), https://www.krollbondratings.com/show_report/17230.

special revenue bonds. As SIFMA explains, the ratings agencies' downgrades mean that the First Circuit's opinion "will have the effect of increasing borrowing costs of financially troubled municipalities, thus adding greater stress on those distressed municipalities." SIFMA Amicus Br. 4. This Court should intervene to ensure that a single appellate court does not disturb the settled understanding of the law on which numerous investors and municipalities have relied for decades.

II. THE FIRST CIRCUIT'S DECISION IS WRONG.

Review is also warranted because the First Circuit's decision is wrong. The Board contends that Section 922(d) does nothing more than "permit[]" a debtor or bond trustee to "apply [special] revenues to debt service" if it "chooses." Opp. 18-19. But that toothless interpretation flouts the provision's text, defeats its core purpose, and would reduce Section 922(d) to a practical nullity.

First, the Board's reading deprives the provision's "notwithstanding" clause—and the provision as a whole—of any practical effect. Section 922(d) states that it applies "[n]otwithstanding section 362 of this title and subsection (a) of this section * * *." 11 U.S.C. § 922(d). Section 362 "stays * * * *collection and enforcement proceedings* against the debtor and his property." *Pennsylvania Dep't of Pub. Welfare* v. *Davenport*, 495 U.S. 552, 560 (1990) (emphasis added); *see* Pet. 15-16. Similarly, Section 922(a) prohibits the "enforcement" of claims and liens "against the debtor." 11 U.S.C. § 922(a)(1)-(2). It follows that Section 922(d) permits creditors to bring such "enforcement" actions against debtors with

pledged special revenues; otherwise, Section 922(d) would not operate "[n]otwithstanding" Sections 362 and 922(a) at all.

The Board claims that its reading leaves Section 922(d) and its "notwithstanding" clause with a sliver of work to do, by clarifying that where a debtor voluntarily turns over its pledged special revenues, a creditor is not prohibited from "cashing [the] checks" it receives. Opp. 21-22 (quoting 3 Collier on Bankruptcy ¶ 362.03 (16th ed. 2019 update)). But nothing in the stay provisions bars that anodyne conduct; by their express terms, those provisions prohibit "enforcement" and "collect[ion]" actions. 11 U.S.C. §§ 362(a), 922(a); *see* 6 Collier on Bankruptcy ¶ 922.02 (16th ed. 2019 update) (acknowledging the limited scope of Section 922(a)); Opp. 1 (admitting that "§ 362(a) * * * stays all judicial actions and non-judicial acts to *compel* payment of a debtor's debts" (emphasis added)). The Board's cases (at 21-22 & n.8) do not state otherwise: In each one, courts found violations of the automatic stay because a creditor "refused to relinquish possession" of property in which the debtor continued to claim equitable title. *E.g.*, *Thompson* v. *Gen. Motors Acceptance Corp.*, 566 F.3d 699, 700 (7th Cir. 2009) (applying 11 U.S.C. § 362(a)(3)); *see* Opp. 21-22 & n.8 (same). Not one of those cases even hinted that creditors could not retain assets *voluntarily* turned over by the debtor—and the sole case the panel cited to support that proposition turns out to have said precisely the opposite. *See In re Hellums*, 772 F.2d 379, 381 (7th Cir. 1985) (per curiam); Pet. 22-23.

Second, the Board's reading contravenes the plain text of Section 922(d), which exempts from the

automatic stay the "application of pledged special revenues *in a manner consistent with section 92[8] of this title* to payment of indebtedness." 11 U.S.C. § 922(d) (emphasis added); *see* Pet. 8 n.3. Section 928 in turn provides that pledged special revenues "shall remain subject to any lien," less any revenues required to pay "necessary operating expenses." 11 U.S.C. § 928(a)-(b). Read together, these provisions thus state that, with the exception of necessary operating expenses, the automatic stay does not prohibit conduct to obtain payment of pledged special revenues "in a manner" authorized by "any lien" on those revenues—that is, pursuant to any legal requirements and enforcement mechanisms a lien imposes.

The Board's contrary reading strains credulity. It asserts that Congress meant that special revenues remain "subject to liens," but that a creditor may not "enforce such a lien." Opp. 23. The only function of a lien, however, is to secure a right to payment. It is difficult to comprehend why Congress would have stated that assets remain subject to a lien that creditors must stand helplessly by as a debtor violates. And the Board's reading simply ignores the statutory language stating that special revenues are not only "*subject to* any lien," but also are to be paid "*in a manner consistent with*" any such lien. 11 U.S.C. §§ 922(d), 928(a) (emphases added).[4]

---

[4] The Board is therefore incorrect to suggest (at 20) that Section 922(d) lacks any language authorizing creditors to bring actions compelling payment. A creditor's right to compel payment comes from "any lien" enforceable under state or Commonwealth law. 11 U.S.C. § 928(a). Section 922(d) pro-

Third, the Board's reading would defeat the central purpose of Section 922(d). This provision was enacted in response to well-publicized distress among municipalities, to ensure that revenue bonds would retain their attractiveness as sources of municipal financing. *See* Pet. 6-9, 29-30. Leaving debtors free to dissipate special revenues except where they voluntarily "choose[]" not to, Opp. 18-19, would remove any meaningful protection for these bonds and substantially diminish their value as secure investments—as the reaction of the municipal bond market dramatically confirms. *See supra* pp. 5-8.

The Board, in contrast, does not even attempt to explain how its reading serves Congress's aims. It simply quotes the same out-of-context snippets of legislative history as the panel and the en banc concurrence, *see* Opp. 26-28, without grappling with the contrary evidence of the drafters' intent identified by the petition and Judge Lynch. *See* Pet. 29-30; Pet. App. 89a-94a. This Court should not permit the First Circuit to reduce this vital protection of creditors' property rights to a gewgaw.

III. THIS COURT'S INTERVENTION IS URGENTLY NEEDED, AND THIS CASE PRESENTS A RARE VEHICLE.

The question presented is of enormous and immediate practical importance. Pet. 32-33; *see* Pet. App. 83a. As noted above, Moody's has already down-

---

vides that the automatic stay does not prevent a creditor from enforcing liens on special revenues, and thus permits creditors to compel payment through any appropriate means provided by state or Commonwealth law.

graded the ratings of more than $8.5 *billion* in special revenue bonds in response to the decision below, and more downgrades are almost certain to follow if certiorari is denied. Absent this Court's intervention, creditors will be forced to stand idly by as their assets are dissipated, in defiance of their settled expectations and the statute's clear text. And municipalities throughout the country—along with Puerto Rico and its instrumentalities—will be hampered in their ability to raise badly needed financing, as the costs of special revenue bonds will inevitably increase once they are stripped of their core protections in bankruptcy. *See* SIFMA Amicus Br. 10-14.

The Board offers no plausible response to these concerns. It suggests that special revenue bonds are too small a sector of the municipal bond market to merit this Court's attention. Opp. 31-32. But Congress plainly believed otherwise when it enacted Sections 922(d) and 928 specifically to ensure the protection of those bonds. And the magnitude of the already-felt impact on the revenue bond market speaks for itself.

Nor should this Court wait to address the issue. On average, fewer than ten municipal bankruptcy cases are filed per year, and contested legal issues often settle before there is an opportunity for appellate review. Pet. 19 n.5. Another opportunity to resolve this manifestly important question may not come along soon—and, by that point, the economic consequences that bondholders and municipalities suffer in the interim will be irreparable.

The Board identifies no colorable vehicle concerns. It claims that Assured may ultimately be unable to recover pledged revenues for a variety of reasons not

addressed by the First Circuit. Opp. 34-36. Those arguments lack merit: The mere fact that HTA operates at a deficit, for instance, does not mean that *all* of its expenditures are "*necessary* operating expenses," 11 U.S.C. § 928(b) (emphasis added), and even the First Circuit did not accept the Board's contention that Assured's liens fall outside the scope of Section 922(d) entirely, *see* Opp. 34-35. But regardless of their merit, these arguments would not present any barrier to this Court's review of the question presented; they would simply remain open to the Board on remand. The U.S. Reports are replete with cases in which this Court resolves a threshold question and remands for additional proceedings. *See, e.g.*, *Manuel* v. *City of Joliet*, 137 S. Ct. 911, 922 (2017); *Nautilus, Inc.* v. *Biosig Instruments, Inc.*, 572 U.S. 898, 913 (2014). This Court should seize the opportunity to review a significant error of law, which defies the longstanding legal consensus, and which has already wreaked uncommonly large consequences for investors, the Commonwealth of Puerto Rico, and municipalities across the country.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

NEAL KUMAR KATYAL
Counsel of Record
MITCHELL P. REICH
REEDY C. SWANSON
DANIELLE DESAULNIERS STEMPEL*
HOGAN LOVELLS US LLP
555 Thirteenth Street, N.W.
Washington, D.C. 20004
(202) 637-5600
neal.katyal@hoganlovells.com

THOMAS P. SCHMIDT
HOGAN LOVELLS US LLP
390 Madison Ave.
New York, NY 10017

Counsel for Petitioners

** Admitted only in Maryland; practice supervised by principals of the firm admitted in D.C.*

MARK C. ELLENBERG
HOWARD R. HAWKINS, JR.
WILLIAM J. NATBONY
ELLEN M. HALSTEAD
THOMAS J. CURTIN
CASEY J. SERVAIS
CADWALADER, WICKERSHAM & TAFT LLP
200 Liberty Street
New York, NY 10281

Counsel for Assured Guaranty Corp. and Assured Guaranty Municipal Corp.

JONATHAN POLKES
MARCIA GOLDSTEIN
GREGORY SILBERT
KELLY DIBLASI
GABRIEL A. MORGAN
WEIL, GOTSHAL & MANGES LLP
767 Fifth Avenue
New York, NY 10153

Counsel for National Public Finance Guarantee Corporation

DECEMBER 2019