No. 20-8

IN THE
Supreme Court of the United States

DEUTSCHE BANK TRUST COMPANY AMERICAS, ET AL.,

Petitioners,

v.

ROBERT R. MCCORMICK FOUNDATION, ET AL.,

Respondents.

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

REPLY BRIEF FOR PETITIONERS

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REPLY BRIEF FOR PETITIONERS

Respondents defend a decision the Second Circuit didn't write and refute arguments petitioners haven't made. And, like a nervous poker player drawing to an inside straight, their opposition has a tell. Recognizing, perhaps, that the court of appeals wrongly applied a presumption in *favor of* preemption, wrongly concluded on that basis that state fraudulent-transfer statutes are preempted, and nullified this Court's *Merit* decision, respondents make a thinly veiled recusal request. That audacious gambit does not comply with this Court's Rules and is meritless. The petition should be granted.

I. The First And Second Questions Presented Merit Review Because The Second Circuit's Preemption Holdings Depart From Decisions Of This Court And Other Circuits

1. a. In respondents' telling (at 16), the court of appeals *did* apply the presumption against preemption but merely held that its weight "is at a low ebb" in the present context.[1] The decision below belies respondents' tale. "Once a party enters bankruptcy," the court of appeals held without qualification, "the Bankruptcy Code constitutes a wholesale preemption of state laws regarding creditors' rights." Pet. App. 34a. Petitioners' "state law claims," the court continued, "were preempted when the Chapter 11

[1] Elsewhere, respondents assert (Br. in Opp. 9, 16, 18) that the Second Circuit "recognized" the presumption, perhaps as one might "recognize" but then ignore an estranged acquaintance.

proceedings commenced and were not dismissed." *Ibid.* Ignoring the long history of state regulation of creditors' rights, the court declared broadly that "detailed, preemptive federal regulation of creditors' rights has . . . existed for over two centuries." *Ibid.* And, to dispel any ambiguity: "Our bottom line is that the issue before us is one of inferring congressional intent from the Code, without significant countervailing pressures of state law." Pet. App. 36a.

Every word inverts the presumption against preemption. It casts state creditor-rights law as the presumptively unwelcome intruder into the federal bankruptcy domain. Nor was this holding limited, as respondents contend (at 16), to "whether [Section 546(e)] preempts state-law fraudulent-transfer claims to unwind a transaction that occurred in the federally regulated securities markets." The court's words were about federal bankruptcy law and state creditor-rights law writ large.

The Second Circuit's *actions* echoed its words. To forestall a foray into textually unanchored policy, the court required *petitioners* to show that their text-based reading of Section 546(e)—as binding only on the "trustee" (and not creditors)—is "necessarily" correct. Pet. App. 38a. A presumption *against* preemption would do the opposite, imposing on *respondents* the burden to show that Congress meant more than it said.

b. Respondents try to explain away the circuit split (at 18) by focusing on "the different Code provisions at issue in each case." But the decision below was sweeping—it held that the presumption against preemption is inapplicable, "wholesale," to

any state creditor-rights law once the debtor has entered bankruptcy. Pet. App. 34a. Decisions in other Circuits have held the opposite. *E.g.*, *Melikian Enters., LLLP* v. *McCormick*, 863 F.3d 802, 806 (8th Cir. 2017) (rejecting argument that "the Bankruptcy Code broadly preempts Arizona law"); *Rosenberg* v. *DVI Receivables XVII, LLC*, 835 F.3d 414, 419 (3d Cir. 2016).[2]

Respondents further confuse the issue by citing (at 19) three appellate decisions that did not even mention the presumption against preemption. For example, *Trikona Advisers Ltd.* v. *Chugh*, 846 F.3d 22 (2d Cir. 2017), rejected preemption by invoking a *different* presumption: "the strong presumption in favor of granting comity to foreign judgments," *id.* at 35, which the court applied as a matter of state law. No state creditor-rights law was at issue.

The decision below is also irreconcilable with decisions of this Court. Respondents again protest (at 19) that this Court's decisions "concern[] vastly different federal and state interests than those at issue here." But the court below did not tailor its holding to particular federal and state interests. This Court's holding in a fraudulent-transfer case that, "where [congressional] intent to override is doubtful, our federal system demands deference to long-established traditions of state regulation," *BFP* v. *Resolution Trust Corp.*, 511 U.S. 531, 546 (1994),

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[2] Although *Pacific Gas & Electric Co.* v. *California ex rel. California Department of Toxic Substances Control*, 350 F.3d 932 (9th Cir. 2003), ultimately held that state law was expressly preempted, it began with the threshold issue of the presumption against preemption. *Id.* at 942-43.

admits of no "wholesale preemption of state laws regarding creditors' rights," Pet. App. 34a. See also *Midlantic Nat'l Bank* v. *New Jersey Dep't of Envtl. Prot.*, 474 U.S. 494, 505 (1986).

c. As a last resort, respondents contend (at 20) that the Second Circuit's rejection of the presumption is irrelevant because, even without it, state fraudulent-transfer laws are preempted. But that contention assumes that the court of appeals correctly understood the text and purposes of Section 546(e). It did not, as explained below and in the petition and amicus briefs. In any event, courts should determine whether state law is preempted *in light of* the presumption against preemption, not by applying the opposite presumption.

2. The Second Circuit held that state fraudulent-transfer law was preempted based on "the purposes and history" of Section 546(e). Pet. App. 51a. This holding conflicts with holdings of courts in the Third Circuit, home to an outsize share of the Nation's largest bankruptcy cases. Pet. 30. And it cannot be squared with decisions of this Court.

a. The court of appeals' holding contradicts *Merit Management Group, LP* v. *FTI Consulting, Inc.*, 138 S. Ct. 883 (2018). The Second Circuit began with the premise that the purpose of Section 546(e) is to "promote finality . . . and certainty for investors." Pet. App. 56a (quotation marks omitted). But this Court in *Merit* held that this "perceived purpose is actually contradicted by the plain language of the" statute. 138 S. Ct. at 897. Instead, Section 546(e) "protects only certain transactions 'made by or to (or for the benefit of)' certain covered entities" so central to

markets that their failure would threaten domino effects. *Ibid.* (quoting 11 U.S.C. § 546(e)). Even then, Section 546(e) applies only if the debtor is eligible to enter bankruptcy under the Code (rather than other insolvency regimes) *and has done so*, a limitation flatly inconsistent with broad preemption of state fraudulent-transfer law.

It matters not that "*Merit* did not address preemption." Br. in Opp. 21. *Merit* addressed "statutory purpose," 138 S. Ct. at 896, and, by rejecting "finality and certainty" as the purposes of Section 546(e), cuts the legs from under the "purposes and objectives" preemption holding of the court below.

b. The decision below is wrong. Section 546(e) and its context circumscribe its preemptive scope. Its text applies only to "the trustee," which of course means "only the trustee." *Hartford Underwriters Ins. Co.* v. *Union Planters Bank, N.A.*, 530 U.S. 1, 7 (2000). It is an exception to powers given only to the trustee. Pet. 28. And a nearby provision, 11 U.S.C. § 544(b)(2), shows that Congress knows how to preempt creditors' fraudulent-transfer claims when it wants to.[3]

Unable to defend the court of appeals' "freewheeling judicial inquiry" into statutory purpose (see *Kansas* v. *Garcia*, 140 S. Ct. 791, 801 (2020) (quotation marks omitted)), respondents contend (at 23) that there is an "identity in bankruptcy between creditors and the trustee," and thus the express limitation of

[3] The Bankruptcy Code contemplates that certain persons other than trustees may exercise trustee powers on behalf of the bankruptcy estate. See *Merit*, 138 S. Ct. at 888 n.1. Petitioners, acting in their own interests, are not exercising trustee powers.

Section 546(e) to "trustees" extends to creditors as well. The Second Circuit did not adopt this transmogrification of the statutory text, and with good reason. As this Court's *Hartford* decision and Section 544(b)(2) confirm, the word "trustee" means "trustee" and "trustee" only.

Respondents thus are left to assert (at 24) that, but for preemption, Section 546(e) "would be a dead letter." That assertion, however, rests on the dubious assumptions that, "[i]n every case, the trustee [w]ould renounce its authority" to bring claims, Br. in Opp. 24, and the bankruptcy court would relieve creditors from the stay of 11 U.S.C. § 362, as the court did here. Even if those assumptions held, Section 546(e) still would bar federal fraudulent-transfer claims within its scope, leaving available only less consequential claims under state law. See Pet. App. 45a-46a (noting that federal claims, unlike state claims, are funded by the estate, can avoid the entire transfer, and have national long-arm jurisdiction).

3. Respondents finally oppose review of the preemption questions because, they say, the court of appeals is destined to come out the same way on remand even if the present judgment is reversed. According to respondents, the Second Circuit, if given another chance, will hold that petitioners' claims did not "revert" from the trustee, and that, even if they did, those claims are burdened by the Section 546(e) safe harbor that is otherwise applicable only to the trustee.

Every step in that argument is mistaken.

There is no reason to believe that the Second Circuit will adopt the "reverter" argument on remand. The district court rejected it. Pet. App. 149a-150a. And the court of appeals twice declined to reach it. Pet. App. 51a, 113a; C.A. Opp. of Defendants-Appellants to Mot. to Recall Mandate 9-12 (Apr. 20, 2018).

The reverter argument also is wrong. As we have argued throughout this case, the state-law claims have always belonged to petitioners; they never "vested in the trustee," as respondents maintain (at 27), and thus do not need to "revert" to petitioners.[4]

To be sure, in the twilight of Reconstruction, "the Bankrupt Act[] vest[ed] in the assignee" (now called trustee) all "property fraudulently conveyed." *Glenny* v. *Langdon*, 98 U.S. 20, 27-28 (1878); see Bankruptcy Act of 1867, ch. 176, § 14, 14 Stat. 517, 523. But Congress has long since repealed that statute, making irrelevant the cases construing it. The Bankruptcy Code's vesting provision, 11 U.S.C. § 541, does not touch claims like petitioners'. And although Respondents assert that a different provision, 11 U.S.C. § 544(b), somehow handed petitioners' state-law claims to the trustee, that is plainly wrong. Section 544(b) creates a *federal* cause of action that, while borrowing state-law standards, has its own statute of

[4] Inexplicably, respondents attribute this "reverter" argument to petitioners. We have never advanced that argument, as it lacks any textual support in the Code. To the contrary, we have consistently argued that the state-law claims always belonged to petitioners, subject to the stay of 11 U.S.C. § 362. See C.A. Resp. & Reply Br. 18-33 (Apr. 17, 2014).

limitations, *id.* § 546(a), and measure of damages, *id.* § 550, among other things.

Even if the claims did "vest" in the trustee (and they did not), they would not "revert" to petitioners diminished by Section 546(e). Section 546(e) is a restraint personal to "the trustee." It constrains the trustee's assertion of the claims, not anyone else's. Respondents' contrary argument (at 28-29) is like saying that anyone who gives a van to charity and later gets it back could no longer use the van for political campaigns. That would be a peculiar enough holding in its own right. It would be all the stranger for the Second Circuit to adopt the "reverter" hypothesis on remand from a decision of this Court holding that Section 546(e) does not preempt creditor state-law claims.

II. Respondents Do Not Dispute That The Second Circuit's Disposition Of The Third Question Presented Would Deprive This Court's *Merit* Decision Of Any Force

1. In *Merit*, the Court expressly left open "what impact, if any," the Bankruptcy Code's definition of "financial institution" "would have in the application of the § 546(e) safe harbor." 138 S. Ct. at 890 n.2. Respondents agree (at 12) that "the Second Circuit decided . . . that very" question. That alone justifies a grant. Pet. 32.

What is more, the court of appeals answered the open question in a way that would deprive *Merit* of practical significance. Under *Merit*, the fact that a transfer "was executed via [banks or similar entities] as intermediaries" does not suffice to apply Section

546(e). 138 S. Ct. at 888. Yet, under the decision below, Section 546(e) would immunize securities-related transfers in which the transferor "deposit[s]" with a bank or similar entity under the transferor's control a transaction's "purchase price" for the bank "to pay" the transferee. Pet. App. 28a. That is just a roundabout way to say that, contra *Merit*, Section 546(e) applies to securities-related transfers executed via banks or similar entities.

Respondents' main answer (at 12-13) is that there is more money at stake in this case than there was in *Merit*. That's not much of a distinction. Even a professor who otherwise dislikes our lawsuit agrees: "If other courts are to follow *Tribune*, the interpretation of applicability and scope of the safe harbor will be restored to its original, excessively far-reaching, pre-*Merit Management* breadth." Irina Fox, *Back to Square One: How* Tribune *Revived the Settlement Payment Safe Harbor to Trustee Avoidance Powers in the Context of Leveraged Buyouts*, 29 NORTON J. BANKR. L. & PRACTICE (forthcoming Aug. 2020).

2. The court of appeals' holding that Tribune, a media company, was a "financial institution" is as wrong as it is counterintuitive.[5] It neglects the words around "financial institution" and "agent." And it would mean that Congress "alter[ed] the fundamental details of" Section 546(e)'s operation in an "ancillary provision[]," something that this Court presumes

[5] Per that holding, fashion company Nine West was just held to be a "financial institution." *In re Nine West LBO Sec. Litig.*, No. 20-md-2941, 2020 WL 5049621, at *8-*11 (S.D.N.Y. Aug. 27, 2020).

Congress does not do. See *Whitman* v. *Am. Trucking Ass'ns*, 531 U.S. 457, 468 (2001).

Instead of addressing these points, respondents misstate our argument about the term "agent." We never said that "an agent must have 'discretionary authority to manage its customer's investments' or 'bind[] [its principal] in contract.'" Br. in Opp. 13 (quoting Pet. 36). We said only that those are apt *examples* of attributes an agent has. Pet. 36 ("for example"); *ibid.* ("such as").

Respondents are ultimately unable to defend the court of appeals' unconstrained expansion of the term "agent." The court's holding would find agency even in arm's-length services agreements that lack restrictions against aiding the principal's competitors (as any true agent has a fiduciary duty to avoid). It thus violates the tenet that the absence of fiduciary duties weighs against agency. *Hollingsworth* v. *Perry*, 570 U.S. 693, 714 (2013) (holding that petitioners were not agents because, in part, they owed no fiduciary duties). Moreover, the court did not even ask whether the purported agent had "power to affect the legal rights and duties of the" principal, even though that power inheres in agency. Restatement (Third) of Agency § 1.01 cmt. c. Applying such established principles would have changed the result: The bank here (to whatever extent it played a relevant role) expressly disclaimed *both* fiduciary duties not expressly assumed *and* the power to affect Tribune's legal rights in dealings with third parties. Pet. 36 n.7.

III. Respondents' Conflicts Argument Is Baseless And Procedurally Improper

Without deigning to file an actual recusal motion, respondents contend that one or more Members of the Court likely still have a conflict despite petitioners' decision to drop certain defendants. Respondents' transparent effort to evade review is both misleading and misguided.

The dropped defendants do not, as respondents claim (at 30), "remain respondents here." A party to the proceedings below remains a respondent "*unless* the petitioner notifies the Clerk of this Court in writing of the petitioner's belief that [the party has] no interest in the outcome of the petition." Sup. Ct. R. 12.6 (emphasis added). Petitioners gave that required notification on July 6. And, in over nine weeks since, not a single dropped defendant has "notif[ied] the Clerk promptly . . . of an intention to remain a party," which Rule 12.6 requires to remain a respondent. Following the procedure of this Court's Rules yields no "actual or apparent conflict of interest." Br. in Opp. 30.

Respondents nevertheless insist that Members may be conflicted because a decision of this Court on the scope of Section 546(e) might affect dropped entities that are named in a *different* case now pending before the Second Circuit. That is obviously not grounds for recusal. *Every* decision of this Court has potential ramifications for other pending litigation. See, *e.g.*, *Sharp* v. *Murphy*, 140 S. Ct. 2412 (2020) (per curiam) (applying to a pending case an opinion of the Court, issued the same day, written by a Justice who was recused from *Sharp*). Neither the recusal statute

nor this Court's Rules require a sweeping survey to identify all pending cases that might be affected by a decision of this Court. See 28 U.S.C. § 455; Sup. Ct. R. 14.1.[6]

Finally, there is no cognizable "inequity" in the fact that petitioners dropped some but not all of the severally liable defendants, in an effort to improve prospects for a quorum. Petitioners, Tribune's retirees and other creditors, seek to recoup billions of dollars defrauded from them. If anything, it would be inequitable to preclude petitioners from litigating the remaining claims simply because some of the defendants are no longer parties to the case.

If respondents truly thought they had proper grounds to recuse one or more Members of this Court, they should have filed a motion for such relief. Their decision to make such a request through indirection speaks volumes about their confidence in the recusal claim, as well as in the merits of their opposition to certiorari.

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The petition for a writ of certiorari should be granted.

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[6] Petitioners properly excluded the pending Second Circuit case from their list of directly related proceedings, as that case does not "arise[] from the same trial court case as the case in this Court." Sup. Ct. R. 14.1(b)(iii). Respondents apparently agree, as they identified no "directly related cases that were not identified in the petition under Rule 14.1(b)(iii)." Rule 15.2.

Respectfully submitted.

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