

OFFICIAL TRANSCRIPT
PROCEEDINGS BEFORE
THE SUPREME COURT
OF THE
UNITED STATES

CAPTION: UNITED STATES, Petitioner v. REORGANIZED CF&I
FABRICATORS OF UTAH, INC., ET AL

CASE NO: 95-325

PLACE: Washington, D.C.

DATE: Monday, March 25, 1996

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IN THE SUPREME COURT OF THE UNITED STATES

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UNITED STATES, :
Petitioner :
v. : No. 95-325
REORGANIZED CF&I FABRICATORS :
OF UTAH, INC., ET AL. :
- - - - -X

Washington, D.C.
Monday, March 25, 1996

The above-entitled matter came on for oral
argument before the Supreme Court of the United States at
11:03 a.m.

APPEARANCES:

KENT L. JONES, ESQ., Assistant to the Solicitor General,
Department of Justice, Washington, D.C.; on behalf of
the Petitioner.
STEVEN JACK McCARDELL, ESQ., Salt Lake City, Utah; on
behalf of the Respondents.

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1 PROCEEDINGS

2 (11:03 a.m.)

3 CHIEF JUSTICE REHNQUIST: We'll hear argument
4 next in Number 95-325, United States v. Reorganized CF&I
5 Fabricators of Utah.

6 Mr. Jones, you're a bear for punishment. You're
7 up again.

8 MR. JONES: And I'm getting it, too, Your Honor.

9 (Laughter.)

10 QUESTION: Either you or we.

11 (Laughter.)

12 MR. JONES: Well, I take comfort in the thought
13 that we're all suffering together here.

14 ORAL ARGUMENT OF KENT L. JONES

15 ON BEHALF OF THE PETITIONER

16 MR. JONES: This case presents two questions.
17 The first question is whether the tax imposed by section
18 4971 of the Internal Revenue Code is within the priority
19 that Congress has established for excise taxes in section
20 507(a)(7)(E) of the Bankruptcy Code.

21 The second question is whether, if this tax is
22 not entitled to that statutory priority, it may then be
23 subordinated to the claims of general unsecured creditors
24 under the principles of equitable subordination that we've
25 been discussing.

1 I would like to briefly discuss the second
2 question first. The case that was just argued could be
3 said to stand, or present the question of whether the
4 principles of equitable subordination on grounds of
5 fairness alone, would permit a court to deviate from what
6 is known as the absolute priority rule. That rule, as
7 discussed by this Court in the Norwest Bank case, is that
8 all claims of a higher priority have to be paid before any
9 claim of a lower priority is paid.

10 In the case that was just argued, the higher
11 priority was the first priority for postpetition tax
12 penalty claims.

13 This case, the second question in this case, if
14 it is reached, could be said to present the question of
15 whether the principles of equitable subordination permit a
16 court, again on grounds of fairness alone, to deviate from
17 what is called the equality of distribution rule. That
18 rule, as discussed by this Court in the Begier case, is
19 that all claims of the same rank must be paid pro rata,
20 without discrimination among them.

21 Now, because, in our view, the principles of
22 equitable subordination are the same in both contexts, and
23 in the absence of creditor misconduct don't permit
24 subordination either of claims of the same or of a
25 different rank, the court of appeals erred in this case in

1 subordinating the innocent claim of the United States.

2 Thus, if the court was right that the claim of
3 the United States didn't have a statutory priority, it was
4 wrong in then saying that the innocent claim of the United
5 States could be subordinated to other general, unsecured
6 claims. That violates the principle of equality of
7 distribution and it also --

8 QUESTION: So you're saying, in effect, even if
9 you lose on the first question, you're entitled to some
10 sort of relief on the second question?

11 MR. JONES: Yes. The relief that we would be
12 entitled to would be to be treated pro rata with other
13 general unsecured claims, if we're not a priority claim.

14 Now, the first question in this case is whether
15 we are a priority claim. Section 4971 of the Internal
16 Revenue Code was enacted in 1974 as part of ERISA. It
17 imposes a tax of 10 percent on underfunded pension plans.
18 Congress expressly designated and described this tax as an
19 excise tax, and it --

20 QUESTION: Well, do you agree that language
21 doesn't always control, that something can be called a tax
22 and, in fact, be a penalty?

23 MR. JONES: I agree that something can be called
24 a tax that isn't, but there are two reasons why we think
25 the designation of this tax as an excise tax is important,

1 which I'll soon address, but I did want to make the point
2 here that this tax does have the two features which are
3 common to excise taxes, and by the way, excise taxes are
4 probably the most common kind of tax there is.

5 QUESTION: This section deals not just with the
6 Federal Government, but with all governmental entities.

7 MR. JONES: That's right, any State, Federal, or
8 local excise tax.

9 Subtitles B through E of the Internal Revenue
10 Code are all excise taxes. There's the estate taxes,
11 employment taxes, miscellaneous excise taxes, alcohol and
12 tobacco taxes -- Congress has a lot of excise taxes, but
13 the common feature, what you can see if you go through
14 them, is there are two common features.

15 They're not universally present, but they're the
16 common characteristics of excises, and those are that it
17 is imposed upon a specific act or event, in this case the
18 act of maintaining an underfunded pension plan, and second
19 is that it's imposed of a portion of the value of that act
20 or event, in this case a portion of the value of the
21 underfunding.

22 Now, 4 years after this tax was enacted,
23 Congress, in restructuring the Bankruptcy Code, enacted
24 507(a)(7)(E), which provides a specific, unqualified
25 priority for any State, Federal, or local excise tax. The

1 court of appeals reasoned in this case that that priority
2 could not reach this tax, because this tax was designed to
3 enforce another law. It was designed to deter the
4 violation of another law, and the court regarded it as a
5 penalty, and as a penalty the court concluded it wouldn't
6 come within the priority for an excise tax.

7 QUESTION: Because it was a nonpecuniary loss --

8 MR. JONES: A nonpecuniary loss penalty, which
9 simply means that it's a penalty that doesn't recover
10 money that would otherwise be owed, I guess.

11 Now, whether you look at the text of the
12 statute, or its structure, or its history, the reasoning
13 of the court of appeals cannot be sustained. The text, of
14 course, which under Ron Pair is what we're supposed to
15 look at, says unqualifiedly that any excise tax, State,
16 Federal, or local, is entitled to this priority. It
17 doesn't contain any suggestion that an excise --

18 QUESTION: Well, Mr. --

19 MR. JONES: -- that has a regulatory purpose is
20 not.

21 QUESTION: Mr. Jones, it does have one
22 qualification, and that is, it uses the word transaction,
23 rather than act or event, and I mean, just in common uses
24 that implies something more, doesn't it, than the passage
25 of the deadline without payment? Would we normally

1 describe that as a transaction?

2 MR. JONES: The transaction language in that
3 code is designed to key off the, if you will, statute of
4 limitations that applies to excise tax claims.

5 Respondents agree --

6 QUESTION: Does it use the word transaction?

7 MR. JONES: Does which?

8 QUESTION: Does the statute of limitations?

9 MR. JONES: No, I didn't -- I was not being
10 precise. I don't mean to say a statute of limitations,
11 but if you look at 507(a)(7) (A), (B), (C), (D), (E), all
12 of which address various kinds of tax claims, each of them
13 has a limitation as to the scope of a claim to fall within
14 the priority.

15 For example, the language in (a)(7)(E), if I'm
16 paraphrasing it properly, is that the tax has to be with
17 respect to a transaction for which a report is due within
18 3 years of the filing of the petition.

19 The word transaction has a broad meaning, and
20 couldn't be reasonably understood to be a narrow meaning.
21 For example, estate taxes are excise taxes. What's the
22 bargained-for exchange if you think of transaction that
23 way? There's no bargained-for exchange there.

24 The transaction language is the act --

25 QUESTION: These taxes you say are excise taxes,

1 that's well-established?

2 MR. JONES: Yes. Estate gift taxes are excises.

3 QUESTION: How is that established?

4 MR. JONES: Well, it's not addressed in the
5 briefs, Your Honor, but I think it's -- it's established
6 in the case law and treatises.

7 QUESTION: Well, what cases?

8 MR. JONES: I'm sorry, I'm not prepared -- I
9 don't have an answer to that question now. I'm just
10 speaking from, if you will, my general knowledge. Excises
11 are taxes that would include estate taxes, just as they
12 include sales taxes.

13 They are at -- this Court talked about the fact
14 that excises, customs duties, and income taxes are really
15 sort of the whole gamut, or as the Court said in the
16 Steadman Machine case, the -- all of the taxes appropriate
17 to sovereignty, and you can track that through the way
18 Congress --

19 QUESTION: Are you saying that all taxes
20 appropriate to sovereignty are excise taxes?

21 MR. JONES: No, sir. I said that income,
22 customs duties, and excises -- the Court used the phrase,
23 appropriate to sovereignty in the Steadman Machine case.

24 If you think about it, customs duties are in
25 title 19, income taxes are in subtitle A of title 26, and

1 as I said, subtitles B through E of title 26 are excises.

2 QUESTION: So your theory is that the Court said
3 customs, income, and excise taxes, and they were covering
4 the waterfront there, and therefore if something isn't a
5 customs duty and isn't an income tax, it is by definition
6 an excise tax?

7 MR. JONES: I think that the point the Court was
8 making was that these are broad and flexible terms. I
9 don't think the Court in the case that I referred to was
10 trying to be specific in the way that you're suggesting.

11 QUESTION: Well, what if a State had structured
12 its tax scheme differently than the Federal Government? I
13 mean, I take it we have to deal with State tax schemes
14 here, too --

15 MR. JONES: Yes.

16 QUESTION: -- and the Federal Government doesn't
17 get any bigger a break than the State does in trying to
18 figure out whether it's an excise tax or not.

19 MR. JONES: Well, I wouldn't say any bigger a
20 break, but I do think that the Mansfield Tire court was
21 probably right in saying that when Congress expressly
22 designates something as an excise tax there's no reason to
23 think it didn't intend to have its excises included within
24 the priority that it adopted for excise taxes.

25 QUESTION: Well, does that really make much

1 sense? I mean, the same committees of Congress don't
2 draft bankruptcy bills as draft tax bills.

3 MR. JONES: It makes sense if you think about it
4 from two perspectives. It makes sense if you think about
5 the fact that Congress is the one -- I mean, if you're
6 trying to decide what is the excise tax, the best evidence
7 of that is -- would be to go through the Internal Revenue
8 Code and to see what Congress has done.

9 I mean, when I suggested that there are two
10 common characteristics for excises, I think that was
11 correct, and that's based on observation of what Congress
12 has done. Congress has probably enacted as many, if not
13 more taxes than anybody.

14 QUESTION: Mr. Jones, the section doesn't
15 purport to include all excise taxes. It includes an
16 excise tax on a specific kind of transaction --

17 MR. JONES: Well, on --

18 QUESTION: -- and what is the transaction we're
19 talking about here?

20 MR. JONES: The transaction that we're talking
21 about here is the act of maintaining an underfunded
22 pension plan.

23 QUESTION: Act of maintaining over a period of
24 time.

25 MR. JONES: That's right.

1 QUESTION: Not a -- it talks about a transaction
2 occurring on a specific date.

3 MR. JONES: Well, the report on that is due on a
4 specific date. It's an end-of-year event. There are
5 other excise --

6 QUESTION: Isn't it the failure to fund on by
7 that date which is the event? It is not the mere
8 maintenance over some period of time, it's the failure to
9 bring it up to the proper level --

10 MR. JONES: It's the maintaining on the
11 reporting date --

12 QUESTION: -- on that reporting date.

13 MR. JONES: Yes. It's the act of, on that date,
14 of maintaining that tax. It is a specific event. There
15 are other excise --

16 QUESTION: It seems to me a more natural term
17 would be to describe that as an omission rather than a
18 transaction.

19 MR. JONES: Well --

20 QUESTION: Or a failure rather than a trans --
21 normally, a transaction is the event of death, or you sell
22 something. I mean --

23 MR. JONES: Well --

24 QUESTION: -- it's an unusual use of the word
25 transaction. Let me put it that way.

1 MR. JONES: It's a broad use of the word
2 transaction, and you can only understand it in a broad
3 context when you understand the broad concept of excises.

4 QUESTION: Of course, maybe the point for your
5 side is that no one has come up with a reason why Congress
6 would want to draw the line between an excise payable,
7 excise tax payable on a failure to do something as
8 distinct from an excise tax payable because of some
9 affirmative action.

10 MR. JONES: Well --

11 QUESTION: At least, I don't have an idea.

12 MR. JONES: I don't think there's any reason to
13 think Congress thought it was drawing such a line. It
14 spoke quite broadly that it's priority would extend to any
15 State, Federal, or local tax expressly treated or
16 generally considered to be an excise.

17 QUESTION: Mr. Jones, there is an additional so-
18 called tax under the ERISA scheme. Where the initial tax
19 isn't corrected within a certain time, then there's
20 imposed a tax equal to 100 percent of the accumulated
21 funding deficiency. Now, what's the transaction there?

22 MR. JONES: The -- there's a lot of issues that
23 I want to talk about in answering that question. The
24 first, of course, is that this Court isn't going to be
25 asked to decide that question, but I will --

1 QUESTION: Well, come on, we have to have that
2 in mind. It's in the very next section --

3 MR. JONES: I understand that.

4 QUESTION: -- and you know we're going to face
5 it.

6 MR. JONES: The United States has never pursued
7 in an appellate court the question of the priority of the
8 subsection (b) tax, and there are reasons to think that
9 the treatment to be accorded to those taxes is different
10 than the treatment to be accorded to the 10-percent
11 priority.

12 There are two differences that I think can be
13 addressed at this point. There are others that may also
14 exist.

15 There is, of course, the facial difference
16 between a 10-percent tax that conforms to the, if you
17 will, ordinary concept of an excise as a tax on the
18 portion of the value, and a 100-percent tax, which is --

19 QUESTION: Which looks something like a penalty.

20 MR. JONES: Which would be, I suppose, a
21 whopping big excise tax.

22 Whether Congress can enact a whopping big excise
23 tax is something that I don't think that there's any
24 reason to think it can't, but I think it's something we'd
25 have to address if we ever argued that case.

1 QUESTION: Well, if an estate tax is an excise
2 tax, certainly estate taxes are whopping big, 65 percent.

3 MR. JONES: That's right, estate taxes can get
4 very high.

5 Now, the other point that I think is a more
6 problematic distinction between those two taxes --

7 QUESTION: More problematic than whopping big?

8 MR. JONES: Yes.

9 (Laughter.)

10 MR. JONES: More problematic even than whopping
11 big is the fact that the (b) tax, unlike the (a) tax, and
12 unlike, if you will, many other excise taxes in the
13 Internal Revenue Code, is expressly subject to waiver by
14 the Secretary of the Treasury on any grounds that he
15 thinks is appropriate.

16 That's a -- that kind of discretionary
17 enforcement would raise a question about whether Congress
18 has treated this as a tax.

19 QUESTION: Is the (b) tax expressly labeled an
20 excise tax?

21 MR. JONES: No, it's labeled -- expressly
22 labeled in the statute a tax.

23 QUESTION: But it doesn't -- the word excise is
24 not in that section, is that right?

25 MR. JONES: No, it's -- nor is it -- nor is it

1 within the (a) --

2 QUESTION: It's not in the other, the
3 10 percent, either.

4 MR. JONES: Nor is it within the section that
5 imposes most congressional excise taxes. Congress
6 designates this as an excise tax both by its location
7 within the code, of course, which Congress is cognizant
8 of --

9 QUESTION: Which also applies to (b).

10 MR. JONES: Which also applies to (b).

11 QUESTION: So if we buy (a), I think we're
12 buying (b).

13 MR. JONES: Well, I'm -- what I'm trying to say
14 is, I think there are reasons why you would certainly want
15 to reserve the question, but even if you were later to
16 address it, there are reasons why you might draw a
17 distinction.

18 QUESTION: Okay. In any event, your point is
19 not that the designation is controlling. The designation
20 is important, but it's not controlling --

21 MR. JONES: It's very important, and it's the --
22 in the words of the legislative history, which I think are
23 useful guides, it says, if Congress has expressly treated
24 it as an excise, or has -- or if it's commonly understood
25 to be one, and so the question that I'm noting about the

1 (b) tax is that, well, it hasn't been expressly treated as
2 an excise when it's subject to waiver on any grounds the
3 Secretary considers proper.

4 QUESTION: Okay, but one thing we can't do is
5 adopt a rule of decision which says (a) has been
6 designated by its location as an excise tax, end of issue.
7 We can't decide on that basis.

8 MR. JONES: You could, if you wished, use the
9 language which the legislative history contains, which is
10 what has been expressly treated as an excise by Congress.

11 QUESTION: Well, depending on how narrowly you
12 read that, this either is or is not --

13 MR. JONES: Yes.

14 QUESTION: -- expressly treated, but we couldn't
15 take the designation rule without picking up (b) as well,
16 is that --

17 MR. JONES: I really don't mean to try to use
18 the word designation as, as the one court said, a label.
19 I think the labeling is important, but it's the treatment
20 of this as an excise tax, and the fact that it shares
21 common --

22 QUESTION: Mr. Jones, could you help me, because
23 I frankly -- I had thought it was -- this was expressly
24 described as an excise tax, but it really is not, is it?
25 What is the closest thing to express language in the

1 Internal Revenue Code -- forget about legislative history
2 for a moment -- that would say the label for this thing is
3 an excise tax?

4 MR. JONES: Well, in terms of labeling, Congress
5 located this within --

6 QUESTION: It just located in the particular
7 section --

8 MR. JONES: In subtitle D, which is called
9 Miscellaneous Excise Taxes. The legislative history
10 describes it as an excise tax.

11 QUESTION: But your textual argument is that
12 it's in a section of the code that's entitled
13 Miscellaneous Excise Taxes.

14 MR. JONES: I'm not sure. Relatively few
15 Federal excise taxes have the word excise in them. I
16 mean, it's just not a legislative draftsmanship thing.

17 QUESTION: But this one doesn't have the word
18 excise in it.

19 MR. JONES: No, it doesn't, and very few do.
20 Most excise taxes are like this. They're taxes, like the
21 estate and gift taxes.

22 QUESTION: Most of them are on a -- you know,
23 you can say you're being taxed on a specific event, like a
24 death or a transaction or something, but this is a
25 nonevent.

1 I mean, if you're right on whether a nonevent is
2 the same as event --

3 MR. JONES: There are --

4 QUESTION: -- of course, you don't --

5 MR. JONES: There are -- there's an excise tax
6 on maintaining a trust with excessive amounts of
7 undistributed income. There are other kinds of excise
8 that follow this pattern.

9 QUESTION: But again -- again, I don't want to
10 just lose this one thought. The only language in the
11 code, other than looking at the tax and trying to decide
12 whether it fits the category, is the title of this section
13 says miscellaneous excise taxes, and it's in that section,
14 is that right?

15 MR. JONES: That would be the only language, if
16 you will, in the code.

17 QUESTION: Yes.

18 MR. JONES: Now, in answering that question, let
19 me point out something that we haven't addressed. We
20 don't think it's relevant, but I do want to point it out.

21 In 7806 of the code, it says that in
22 interpreting statutes you're not to look at captions,
23 basically. I'm summarizing.

24 QUESTION: Right.

25 MR. JONES: We're not suggesting that this is a

1 question of interpreting the statute. It's a question of
2 understanding how Congress has treated this statute to
3 determine whether it's an excise.

4 QUESTION: Yes, but you're not willing to stand
5 by the proposition, which sort of makes doubtful whether
6 the proposition is correct -- you're not willing to stand
7 by the proposition that everything included within that
8 title is an excise tax.

9 MR. JONES: I think everything --

10 QUESTION: It happens to bear that title, but
11 you're -- well, the 100 percent tax you're willing to say
12 is not.

13 MR. JONES: Justice Scalia, what I've said is
14 that to the extent that possible distinctions exist
15 elsewhere, we're not trying to answer those questions,

16 QUESTION: Well, you have answered it --

17 MR. JONES: -- and I've answered --

18 QUESTION: -- if you're going to rely on the
19 fact that this in a title that bears the caption, Excise
20 Tax. If that is going to be the -- you know, the North
21 Star of your argument, the 100 percent is covered.
22 Otherwise, you have to abandon that and say, well, it's
23 not determinative.

24 MR. JONES: We have to look for some evidence to
25 answer the question of what is an excise tax.

1 QUESTION: Okay. I mean, so you say this is
2 just part of the evidence. This alone isn't enough to get
3 you there.

4 MR. JONES: If Congress has expressly treated it
5 as an excise, then it is, and all I'm --

6 QUESTION: No, but that begs the question. It
7 has not expressly treated it. In the section itself, the
8 closest to express treatment, as I understand your
9 argument, is its placement in subsection D, which has an
10 excise tax label, and therefore, if we use the placement
11 in subsection D as the ground of decision, then we're
12 going to pick up the (b) tax as well as the (a), and you
13 don't want us, I take it, to be forced to decide on that
14 ground.

15 If I'm wrong, if you say look, I'll take -- I
16 want the whole hog, and you should decide on the ground of
17 that placement, then I want you to tell me.

18 MR. JONES: Congress has done more than just
19 locating it in this section. It's made it a fixed and
20 determinate excise tax, and to understand why I'm
21 emphasizing that, I want to point out that under the
22 Bankruptcy Act the decision -- our position in this case
23 was endorsed by this Court in the case of United States v.
24 New York.

25 QUESTION: No, but may I just interrupt you,

1 because I want to get clear on one thing. It's the same
2 thing that Justice Scalia and Justice Stevens wants to get
3 clear on.

4 Yes or no. You should decide this case under a
5 rule of decision that says, if it's placed under D, it's
6 an excise tax, end of issue. Is that the position that
7 you take, or is it not the position that you take?

8 MR. JONES: I have two answers to that. One is,
9 you make take that --

10 QUESTION: No, it's yes or no. You can only
11 have one answer.

12 (Laughter.)

13 MR. JONES: The Court could reach that decision.
14 I think that the Court could also have an analysis that
15 also looked to the question of whether the treatment of
16 the tax is --

17 QUESTION: So I guess the answer is no.

18 MR. JONES: -- an excise --

19 QUESTION: I guess the answer is no.

20 QUESTION: But see, Mr. Jones, the court of
21 appeals seemed to think it really is clearly labeled an
22 excise tax, but they said, we apply a four-part test from
23 Cassidy or some earlier case, and you're saying don't
24 apply a four-part test, apply an act or event test.
25 You're just saying they applied the wrong test.

1 MR. JONES: I think that's the test that
2 Congress applies --

3 QUESTION: But it is correct, in your view --

4 MR. JONES: -- in creating excise taxes.

5 QUESTION: -- to apply a test to decide whether
6 we think it's an excise tax.

7 MR. JONES: I think in deciding what's an excise
8 tax, we should apply the test Congress applies, but may I
9 please --

10 QUESTION: Wait, but what test does Congress
11 apply? They have included the 100-percent tax within this
12 section entitled Excise Taxes.

13 MR. JONES: And then they made it waivable. I'm
14 simply saying that in a future case, not in this case, the
15 Court might want to consider whether that's relevant. I
16 don't think the Court has to address it here. I wouldn't
17 expect it to.

18 QUESTION: It seems to me once you abandon --
19 once you're not willing to answer yes to Justice Souter's
20 question, we're just quibbling about what the test ought
21 to be, whether it's the four-part test used here, or we
22 should make up another one.

23 MR. JONES: There's really another point --

24 QUESTION: And there's really no alternative.

25 You --

1 MR. JONES: There's another --

2 QUESTION: Can I ask a question -- at some
3 point, when you can -- a technical question.

4 MR. JONES: May I just make one more point?

5 QUESTION: Yes. You bet.

6 MR. JONES: Thank you. In United States v. New
7 York, the court addressed the same question that it has to
8 address here. It did it under the Bankruptcy Act.

9 The question in that case was whether an excise
10 tax that is designed to enforce some other law is no
11 longer an excise tax. It's no longer qualified to the
12 priority as a tax, it's a penalty, and what the Court said
13 in United States v. New York is that the mere fact that a
14 tax is designed to enforce some other, in this case State
15 law doesn't make it, in the words of the Court, any the
16 less a tax, doesn't remove it from the statutory priority.

17 If this case were being decided under the
18 Bankruptcy Act, that analysis in United States v. New York
19 would prevail here, because --

20 QUESTION: That was a State tax.

21 MR. JONES: No, sir, that was a Federal tax --

22 QUESTION: That was a -- in this same section?

23 MR. JONES: That was a Federal employment tax
24 that was designed to enforce a State unemployment
25 contribution law. The tax did not apply if the State law

1 had been complied with.

2 QUESTION: Was it included in this same section
3 of the code?

4 MR. JONES: I believe the Federal employment
5 taxes are in subtitle C, the immediately preceding
6 section, which is also an excise tax. The Court
7 specifically said this excise tax does not lose its
8 priority. It's not any the less a tax because it's
9 designed to do something else.

10 QUESTION: What's the caption of subsection C,
11 if subsection D is Miscellaneous Excise --

12 MR. JONES: I think it's called Employment
13 Taxes.

14 QUESTION: Not Excise Taxes.

15 MR. JONES: That's not its caption.

16 QUESTION: Mr. Jones, one characteristic of many
17 excise taxes is that they are deductible from income, and
18 then that might be one way you could distinguish an excise
19 tax from a penalty. This is not deductible, this --
20 whatever you want to call the --

21 MR. JONES: It's hard for me to answer that
22 question. This is a tax owed by the pension. No, this is
23 a tax owed by the employer.

24 QUESTION: By the company, because it didn't
25 make the contribution.

1 MR. JONES: This is owed by the employer. I --
2 you're asking me whether it's deductible. I don't know.
3 I have no reason to think it would -- would not be.

4 QUESTION: But how -- is that something that can
5 help us distinguish an excise tax from a penalty, excise
6 taxes or --

7 MR. JONES: Yes, I agree, that would be some
8 evidence.

9 If Congress -- Congress as a general proposition
10 doesn't allow the deduction of penalties, allows the
11 deduction of ordinary necessary business expenses. I
12 don't know how the -- I don't know what the treatment is
13 here.

14 In Mansfield Tire, the Sixth Circuit made the
15 point that many, if not most Federal excises have a
16 punitive or regulatory purpose. If Congress had intended
17 to exclude all of its excises like excises on gambling, on
18 green mail, on unregistered securities dealings, you would
19 reasonably expect to see some evidence of that in the text
20 or the legislative history.

21 But the text and the legislative history contain
22 the unqualified statement that any excise, Federal, State,
23 or local, that has been expressly treated or generally
24 accepted as an excise is entitled to priority, and as the
25 Court said in United States v. New York, the fact that

1 this excise is designed to enforce a penalty doesn't make
2 it any the less a tax.

3 Justice Breyer --

4 QUESTION: Thank you.

5 MR. JONES: -- I'm sorry.

6 QUESTION: Thank you -- that's all right.

7 Suppose, just for the sake of argument that I
8 thought because it's regulatory in nature, it's object is
9 zero dollars, it doesn't want to collect revenue, and
10 because it doesn't seem to be on an activity, though there
11 are things on your side, too, which you very well argued,
12 but suppose for the sake of argument that I were to say it
13 was an excise tax, then we'd get to the next part of the
14 case.

15 Now, the technical question on the next part of
16 the case, assuming that for the sake of argument that we
17 got there, under section 7 priorities, I would have
18 decided that this was a penalty, right?

19 MR. JONES: Under Chapter 7 priorities?

20 QUESTION: Yes. Yes, under Chapter 7 I would
21 have decided this was a penalty.

22 MR. JONES: If you deny the priority on the
23 grounds it was a penalty --

24 QUESTION: Yes, okay.

25 MR. JONES: -- and you're now in a 7 --

1 QUESTION: Then it would have come in the fourth
2 priority after unsecured creditors, is that right?

3 MR. JONES: It's a prepetition claim.

4 QUESTION: Yes.

5 MR. JONES: Yes.

6 QUESTION: All right. So why in this section,
7 in this Chapter 11 case didn't the bankruptcy judge just
8 say, this is a penalty, therefore I put it in a different
9 class. I put it in a class which would be the class it
10 would be in if this were a Chapter 7.

11 I put it in a class below unsecured creditors,
12 and therefore I don't have to worry about equitable
13 subordination or not, and since he could have just as
14 easily done that, which would have come to the identical
15 thing, he just used the wrong words to describe what he
16 did, and therefore that issue drops out of the case.

17 That's my question.

18 MR. JONES: Right. Of course, as you've already
19 pointed out, that question isn't presented here.

20 QUESTION: Yes, but what are we supposed to
21 do --

22 MR. JONES: If it had been presented --

23 QUESTION: Yes.

24 MR. JONES: If it had been presented, what the
25 answer that some courts have given which we think would be

1 correct is that when you cram down, if you will, the
2 priorities from the 7 into the 11, what the courts have
3 pointed out is that you don't do that to the extent that
4 Congress expressly intended that the rules that are
5 applicable to 7 should not apply to 11.

6 QUESTION: But wait, we've assumed in this,
7 we've assumed in this for the sake of my question that
8 this is nothing other than a simple penalty --

9 MR. JONES: Right.

10 QUESTION: -- of a nonpecuniary nature.

11 MR. JONES: Yes, sir, and in -- and my point is
12 that in a Chapter 11, Congress made the express
13 determination that pecuniary -- nonpecuniary loss,
14 prepetition penalties would be treated as general
15 unsecured claims --

16 QUESTION: Oh --

17 MR. JONES: -- and not be treated as --

18 QUESTION: Where does it do that?

19 MR. JONES: We discuss that in our brief. I'm
20 sorry, I don't remember the page, but if you compare the
21 bills as they progressed through Congress --

22 QUESTION: No, but where in the language of the
23 statute does it do that? Anywhere?

24 MR. JONES: It's in the history of the statute.

25 QUESTION: Is there any case -- is there any

1 case which has said that we lack the power in Chapter 11
2 to treat --

3 MR. JONES: Yes. Yes, sir. In two cases that
4 we cite in a footnote addressing this in our reply
5 brief --

6 QUESTION: Thank you.

7 MR. JONES: -- that general point is made, and
8 we also point out the history in our opening brief.

9 I would like to reserve the balance of my time
10 for rebuttal.

11 QUESTION: Yes, Mr. Jones.

12 Mr. McCardell. Is that the correct
13 pronunciation?

14 MR. MCCARDELL: It is, Your Honor.

15 QUESTION: Mr. McCardell.

16 ORAL ARGUMENT OF STEVEN JACK MCCARDELL

17 ON BEHALF OF THE RESPONDENT

18 MR. MCCARDELL: Mr. Chief Justice, and may it
19 please the Court:

20 The IRS claim to tax priority in this case rests
21 on the single assumption identified in the questions of
22 the last argument. That is, that every exaction labeled a
23 tax in section 4971, because of its placement under the
24 heading, Miscellaneous Excise Taxes, is automatically and
25 without further consideration entitled to the tax priority

1 in bankruptcy.

2 The questioning in the last argument I think
3 revealed that the 100-percent exaction imposed under sub
4 (b) of section 4971 is indistinguishable from the exaction
5 under sub (a) on the basis of its labels, and if the IRS
6 can concede that the label alone does not control with
7 regard to sub (b), that concedes the case, if label is the
8 IRS' sole argument, which it must be in this case, because
9 of the concessions that the IRS made in the lower court.

10 QUESTION: Is there anything else that comes
11 under sub (b) and therefore bears the label, Miscellaneous
12 Excise Taxes, which you would assert is obviously not an
13 excise tax, as you do the 100 percent, and as you do the
14 10 percent, for that matter?

15 MR. McCARDELL: If I understand Your Honor's
16 question, the only exaction under sub (b) is the
17 100 percent item designated as a tax.

18 QUESTION: Whatever comes within that section of
19 the code that bears the caption, Miscellaneous Excise
20 Taxes. Now, there are a lot of things embraced within
21 that, are there not?

22 MR. McCARDELL: Yes, there are, Your Honor.

23 QUESTION: What else besides this 10 percent and
24 100 percent strikes you as obviously not an excise tax?

25 MR. McCARDELL: Well, there are other tiered

1 penalties. For example, section 4941 tiered tax on self-
2 dealing. It imposes a first-tier penalty and a second-
3 tier penalty. Both of them are designated as taxes.
4 Those are the exactions that the Fourth Circuit and the
5 Fifth Circuit ruled under the Bankruptcy Act were not
6 entitled to tax priority.

7 QUESTION: Well, do you say that every exaction
8 adopted under 26 U.S. Code section 4971, subtitle D, is a
9 penalty, not a tax?

10 MR. McCARDELL: We do, Your Honor, because both
11 were asserted in this case. The (a) provision which is
12 before the Court today is in the amount of approximately
13 \$1.2 million, the (b) provision for about another \$40
14 million, was in the amount emphasized -- asserted in this
15 case.

16 The reason the IRS must rely on its labels
17 govern argument is that the IRS conceded in the lower
18 court that it would not be able to sustain the position
19 that these exactions are not penalties. That concession
20 is found at pages 48 and 49.

21 QUESTION: To what extent are we bound by a
22 concession like that? We do not accept, for example,
23 concessions on points of law as being conclusive,
24 ordinarily.

25 MR. McCARDELL: Your Honor, the IRS did not come

1 forward with any evidence in the bankruptcy court to
2 satisfy the court's traditional test for the tax priority
3 in bankruptcy. Having failed to meet its burden to prove
4 its entitlement to the priority, I think the IRS is bound
5 by that failure.

6 QUESTION: Well, it's one thing to be bound by a
7 failure to offer proof, another thing to be bound by a
8 concession.

9 MR. McCARDELL: And both occurred in this case.
10 The traditional test for tax priority requires that the
11 exaction have the purpose of supporting the Government.

12 QUESTION: But that can't be the case. Suppose
13 it's a tax on alcohol or cigarettes. It's a tax designed
14 to encourage people not to smoke or not to drink, some
15 kind of a sin tax. Do you say that those aren't excise
16 taxes?

17 MR. McCARDELL: We do not, Your Honor. The rule
18 adopted by the --

19 QUESTION: I mean, aren't there plenty of excise
20 taxes that are designed for the very purpose of
21 encouraging certain behavior, or discouraging certain
22 behavior?

23 MR. McCARDELL: There are, and in the cases of
24 those taxes they have a mixed purpose, both regulatory and
25 to raise revenue.

1 Section 4971 is distinct in that regard, in that
2 it has only a function of coercing and punishing the
3 failure to --

4 QUESTION: Well, it raises revenue for Uncle
5 Sam.

6 MR. MCCARDELL: If it's ever paid, it certainly
7 goes into the Treasury. However, it's not used to fund
8 pensions or to otherwise address the question of retiree
9 claims. Now --

10 QUESTION: But I think what --

11 QUESTION: Well, but we've never required that.
12 That would be constructing some other new --

13 QUESTION: What Justice O'Connor is suggesting
14 is, how can we tell whether the purpose of -- it's easy to
15 say that this tax has a, you know, an encouraging or
16 discouraging function. How can we say that it isn't for
17 the purpose of raising tax revenue? I don't know how to
18 figure out whether it is or isn't. I know that it does
19 raise tax revenue.

20 MR. MCCARDELL: Certainly. First, if I might
21 address the end of Justice O'Connor's question, which I
22 think addresses the question of what the Bankruptcy Code
23 does with regard to penalty claims, subsection (G) of
24 section 507(a)(7) the Court has before it today
25 distinguishes between penalties that have a pecuniary

1 loss, and penalties that are not based on a pecuniary
2 loss.

3 Now, it's clear that if there could never be --
4 if the simple fact that it's paid into the Treasury of the
5 Government always made it a tax simply because the
6 Government receives revenue, then there never could be
7 such a thing as a nonpecuniary loss penalty, but (G)
8 demonstrates that there is such a distinction, and that's
9 why, in looking at section 4971, to answer Your Honor's
10 question, the Court can look at objective characteristics
11 of this tax that demonstrate that it does not satisfy the
12 traditional test for taxes.

13 It was -- first, the United States is not liable
14 for the pensions that are guaranteed. They are guaranteed
15 by the Pension Benefit Guaranty Corporation, which
16 operates on private funds.

17 The penalty, if paid, goes to the IRS, but not
18 to the PBGC or to the plans or to the retirees. If the
19 section 4971 penalty is paid, the underlying obligation to
20 fund the plan remains, and in that regard it's different
21 from the responsible officer penalty addressed in the
22 prior case, which can only be collected once. This one is
23 collected twice.

24 It says to the employer, you fund your pension
25 plan, or if you don't you're still going to have to fund

1 it, or the next year you're going to have to fund it at
2 110 percent, you have to pay 110 percent penalty, or the
3 next year 220 percent, and so on.

4 QUESTION: Well, it doesn't call it a penalty.

5 MR. McCARDELL: That's correct.

6 QUESTION: I mean, you're calling it a penalty.
7 That's what we have to decide, and what's the test?

8 MR. McCARDELL: The test, Your Honor, is whether
9 it qualifies as a tax. The Court has distinguished taxes
10 from penalties by defining it --

11 QUESTION: Well, yes. What is the test for
12 determining that?

13 MR. McCARDELL: The test is that stated in
14 United States v. New York, that a tax is a pecuniary
15 burden laid upon individuals or property for the purpose
16 of supporting the Government, by whatever name it may be
17 called. That's the test.

18 QUESTION: Mr. McCardell, I don't know why the
19 issue isn't -- forgetting these general tests about taxes
20 and penalties, why isn't the issue simply whether it's
21 a -- whether you call it a tax or a penalty, it is imposed
22 on a transaction occurring on a certain date. If that is
23 the test, do you win or lose?

24 MR. McCARDELL: If the Court addresses the
25 question of transaction, which we think it should, because

1 that is encompassed within the question before the Court
2 today, it's an element of qualifying for tax priority, the
3 IRS loses. There was no transaction.

4 QUESTION: Well, they would say -- I think
5 Mr. Jones would say, well, the statute imposed an
6 obligation to file -- make a determination as of the end
7 of the plan year and know exactly what the underfunding
8 was, and I suppose the transaction might be described as
9 making a determination with red figures in it -- bing --
10 and then you pay 10 percent of the red figure.

11 MR. McCARDELL: The IRS's proof of claim in this
12 case identified when this tax arose, and that date was
13 September 15, 1990, at the end of that day, when no
14 payment was made -- at midnight on September 15, 1990. At
15 11:59 p.m. on that day, there was no tax. At 12:01 the
16 next day, there was a tax. What happened in between?

17 QUESTION: I take it that's the end of the plan
18 year, that --

19 MR. McCARDELL: That's the end of the period
20 within which the debtor could have made that final
21 payment, and in between those two --

22 QUESTION: Was that the end of the plan year? I
23 want to be --

24 MR. McCARDELL: Yes.

25 QUESTION: Because they use the term plan year,

1 I think, in the statute.

2 MR. McCARDELL: Yes. Your Honor, the end of the
3 plan year was December 31, 1989, but ERISA allows the
4 funding payments for that year to be made up until
5 September 15 of the following year.

6 QUESTION: So they treated the transaction date
7 as the date the payment was due, rather than the date the
8 determination was made.

9 MR. McCARDELL: That's what their proof of claim
10 says, Your Honor.

11 QUESTION: Why would Congress want to draw that
12 distinction between a tax which becomes payable as a
13 result of nonaction and the expiration of time, and the
14 tax which becomes payable because of an affirmative act,
15 or perhaps even an affirmative agreement, if that's
16 applied by one sense, a transaction. Why draw that kind
17 of line?

18 MR. McCARDELL: I'm not sure, Your Honor, but
19 it's apparent from the language of section 507(a)(7)(E)
20 that that line, indeed, was drawn because of the language,
21 transaction occurring, and perhaps it's based on the
22 distinction the Solicitor General points to that most
23 excise taxes are based on an act or event, or a
24 transaction.

25 QUESTION: Well now, wait, act or event or

1 transaction, you're willing to read transaction to include
2 event?

3 MR. McCARDELL: We are not.

4 QUESTION: You're not willing to include it. Or
5 act? Can it be an act?

6 MR. McCARDELL: Nor --

7 QUESTION: Not an act.

8 MR. McCARDELL: Nor an act, Your Honor.

9 QUESTION: It has to be -- a transaction
10 involves -- you then do not think that estate taxes are
11 excise taxes.

12 MR. McCARDELL: I wondered that as I studied for
13 this case, Your Honor, and although it's not cited in the
14 briefs and I don't have the statute here today, my
15 recollection of the estate tax statute is that it's
16 imposed on the transfer into the estate, which is a
17 transaction.

18 QUESTION: If I impose a tax on the sale of, or
19 the purchase of jewelry, that would be an excise tax, but
20 if I impose a tax on the ownership of jewelry, that would
21 not be an excise tax.

22 MR. McCARDELL: Under the ordinary standard --

23 QUESTION: I mean, above a certain amount. If
24 you own more than a certain amount of jewelry, that
25 would --

1 MR. McCARDELL: Ordinarily, it would be
2 understood as a property tax.

3 QUESTION: A property tax.

4 QUESTION: How about a stamp tax on documents?

5 MR. McCARDELL: I don't know, Your Honor.

6 QUESTION: How is the transfer of property into
7 an estate the result of a transaction? It's the result of
8 a disposition by someone who is now dead, and it's the
9 result of an acceptance, I suppose, by an administrator,
10 but the two in their respective capacities never meet, so
11 there isn't any real transaction in the sense of the
12 characteristically consensual act of two parties.

13 MR. McCARDELL: There is an exchange in the
14 sense of the death creates an estate, and to the estate
15 goes the decedent's property, and that is described in the
16 code as a transfer.

17 QUESTION: But we're getting a little bit
18 attenuated.

19 MR. McCARDELL: Yes, Your Honor, and with regard
20 to the section 4971 imposition, it's made not based on any
21 transaction, simply in this case on the failure to make a
22 payment.

23 QUESTION: Mr. McCardell, do you know the answer
24 to my question about the deductibility of this?

25 MR. McCARDELL: I do, Your Honor. These

1 impositions are not deductible, and the cross-reference in
2 section 4971 is to section 275.

3 QUESTION: There's a whole slew under these
4 miscellaneous excise taxes, and I know one has to do with
5 charitable foundations. It seems to operate the same way
6 this one does. You're supposed to do something that
7 doesn't relate to tax. You do it, and there's what's
8 called an excise tax.

9 MR. McCARDELL: That's true.

10 QUESTION: I'm trying to understand what else,
11 since this is -- there are many, many things that come
12 under this huge title, would be affected by our answer to
13 the question in the context of 4971, what other animals
14 there are like it in this collection.

15 MR. McCARDELL: There are very few just like
16 this one, because this one is imposed only when another
17 statute is violated.

18 Section 302 of ERISA requires that a plan
19 sponsor fund its pension plan, and it's only in violating
20 that statutory obligation that this exaction is imposed,
21 so that many of the other excise taxes imposed under the
22 code which may have a regulatory or a deterrent effect
23 simply wouldn't be covered by this case because they're
24 not based on -- they're not exacted on unlawful conduct.

25 QUESTION: May I ask you this, are all taxes

1 deductible by the person paying the taxes if they're
2 engaged in business?

3 MR. McCARDELL: Section 162 of the Internal
4 Revenue Code, which we have addressed in our brief,
5 generally provides for the deductibility of taxes but not
6 penalties.

7 QUESTION: And penalties are not.

8 MR. McCARDELL: That's correct.

9 QUESTION: And it's your position that neither
10 the 10-percent exaction nor the 100-percent exaction in
11 this ERISA section are deductible.

12 MR. McCARDELL: That's correct. They are
13 expressly made not deductible.

14 QUESTION: The Government suggested that as to
15 the 100-percent tax it has an equitable component within
16 the tax. That is to say, the Government is free to waive
17 the collection of the tax.

18 MR. McCARDELL: That is a distinction --

19 QUESTION: Are there any other taxes that are in
20 the excise subtitle that have this equitable waiver, or
21 equitable feature built into them?

22 MR. McCARDELL: I don't know, Your Honor. It
23 seems to me, however, that the capacity of a creditor to
24 waive its claim always exists with regard to any claim,
25 and that applying that as a distinction really would allow

1 a creditor to determine --

2 QUESTION: Well, I don't -- I think the
3 Government would tell you that it has no discretion to
4 waive its taxes, other than in the one instance we're
5 discussing, the 100-percent tax, and so it would seem to
6 me plausible enough for the bankruptcy court to say, well,
7 there's an equitable component to this tax which can be
8 waived, and I am going to equitably subordinate it.

9 MR. McCARDELL: And that, in fact, did occur in
10 this case. The bankruptcy court --

11 QUESTION: As to the 100 percent.

12 MR. McCARDELL: -- did subordinate under section
13 510(c) both the 100-percent and the 10-percent penalties.

14 QUESTION: But that would at least be an excise
15 tax that has an equitable component, which is not like
16 other excise taxes.

17 MR. McCARDELL: It's true that the -- only the
18 (b) portion of this exaction is waivable by the
19 Government.

20 QUESTION: Can I ask the same question I asked
21 the Solicitor General, because assuming that I agreed with
22 you, assuming for the sake of argument that I agreed it
23 was not a tax, but rather it was a penalty, because it
24 collects zero dollars as its objective. Assume that.

25 Now, on that assumption, I found it very

1 difficult to reach the question of equitable subordination
2 without deciding whether or not the bankruptcy judge would
3 have the power to create a subcategory that would rank
4 this kind of penalty below the unsecured creditors, or you
5 raised that.

6 They replied, I take it, in footnote 14 of their
7 reply brief, and they cite a bunch of cases, but they cite
8 them for the proposition that you cannot set up a
9 subclassification of claims within a class of equal
10 priority. Of course that's true --

11 MR. McCARDELL: It's --

12 QUESTION: -- but I would like to know what you
13 think of that particular argument. Namely, they deny that
14 the bankruptcy judge would have the power in Chapter 11 to
15 create a subclass of the penalties below the unsecured
16 creditor, and I don't know if these cases stand for that
17 specific application of the general proposition, or if
18 they do not, and I don't know enough about bankruptcy law
19 to know how well-settled that kind of question is, and
20 that kind of question seems to me to be prior to a
21 definition of the word equitable.

22 MR. McCARDELL: Those cases do not stand for
23 that proposition, Your Honor, and I should acknowledge
24 that this -- in this case, the IRS's claim was
25 subordinated in two independent ways, not just equitable

1 subordination under 510(c), but also was subordinated
2 under the plan. ~~ground. wouldn't it? Wouldn't we have to~~
3 ~~send it to~~ There was a subordinated class created for
4 nonpecuniary loss penalties. Into that class the IRS's
5 claims were placed, so that the IRS, by never objecting to
6 that class, really left the issue as having been resolved
7 by the -- ~~say, so that by affirming the confirmation order,~~
8 ~~the Court~~ QUESTION: All right. If, in fact, since I'm--
9 I have to -- we have to decide this case, and if you win
10 on the first issue, and then I get to that, and I read the
11 cases, and I think they're indeterminate, what am I, or
12 what would you think this Court should do? ~~exist in the~~
13 ~~plan,~~ and Shouldn't we -- I mean, to answer the question
14 of what's equitable without hanging in the air seems ~~action~~
15 difficult. Should we remand the case? Should we then ~~that~~
16 say, go back and work this out, because we don't need to
17 decide whether it's equitable or not when you have a
18 perfectly good ground for reaching the same result. ~~claims~~
19 ~~may not be~~ What is it, in your opinion, we should do? ~~ally~~
20 ~~similar.~~ MR. MCCARDELL: Your Honor, the Court need not
21 look to equitable grounds if it reaches that question, ~~it~~
22 because two statutes in Chapter 11 both permitted and ~~have~~
23 required the subordination that occurred here.

24 QUESTION: You didn't really argue -- I mean,
25 it's come up here under this other pretense. That is, the

1 question presented was -- so it would be rather hard to
2 affirm on that ground, wouldn't it? Wouldn't we have to
3 send it back? ~~It's difficult to understand why the IRS~~
4 ~~Thus, the~~ MR. McCARDELL: The court of appeals affirmed
5 the confirmation order, which is one of the three orders.
6 The order approving the plan is one of the three orders on
7 appeal today, so that by affirming the confirmation order,
8 the Court will approve the subordination that's provided
9 for in the plan. ~~you are not making the argument that was~~
10 ~~made in~~ It's difficult for us to understand why the IRS
11 doesn't want to address it, but it is an independent
12 ground for subordination that really does exist in the
13 plan, and really was -- really occurred in this case, so
14 that by reaching -- by simply considering the confirmation
15 order as one of the three orders, the Court does have that
16 issue before it. ~~s because Chapter 11 has a specific~~
17 ~~requirement~~ The two statutes which provide for that ~~11 taxes,~~
18 subordination are section 1122, which provides that claims
19 may not be placed in a class unless they're substantially
20 similar. Well, these claims are not substantially similar
21 to the general unsecured claims, first because they don't
22 represent a pecuniary loss, and second, because they have
23 different priorities in the liquidation. ~~explained why~~
24 ~~Congress~~ Further, section 1129(a)(7) of the code gives
25 them -- requires that the Bankruptcy Code consider, in

1 confirming a plan, what the liquidation results would be,
2 and as the IRS has conceded in the Chapter 7 case, penalty
3 claims not entitled to priority would be subordinated.
4 Thus, that result is required in a case of this nature,
5 and those two statutory grounds, rather than any outside
6 equitable factors, would be appropriate grounds for
7 affirmance in this case.

8 QUESTION: Mr. McCardell, do I understand
9 correctly that you are not making the argument that was
10 made in the prior case? That is, if you lose on the first
11 question, if this is characterized in the bankruptcy
12 context as an excise tax and therefore would have
13 priority, you're not saying that even though it has
14 priority status it can be subordinated.

15 MR. MCCARDELL: We're not saying that, Your
16 Honor, and that's because Chapter 11 has a specific
17 requirement that a Chapter 11 plan pay in full all taxes,
18 which this plan says it will do. That's found in section
19 1129(a)(9)(C) of the code, so that we are not making that
20 argument.

21 Our argument, then, simply rests on the Court's
22 traditional longstanding, well-accepted test for the
23 definition of taxes. The IRS has never explained why
24 Congress intended to legislatively overrule the Court's
25 precedents defining taxes.

1 There's no definition for tax in the Bankruptcy
2 Code. Where the Bankruptcy Code intends to incorporate a
3 specific definition from the Internal Revenue Code or any
4 other Federal statute, it does so expressly so that -- and
5 a further significant factor in this case is that the
6 kinds of claims we're dealing with in this case were
7 simply disallowed entirely under the Bankruptcy Act, and
8 to suggest that by saying nothing Congress intended to
9 suddenly elevate those claims to the seventh priority is
10 quite a stretch, as we view the development of the law.

11 The legislative history on which the IRS relies
12 time after time in its brief simply says that exactions
13 that are taxes may -- are covered by this priority if
14 they're excises, but they must be taxes first, and so we
15 ask the Court to consider with regard to this exaction the
16 traditional test, which the IRS conceded in the lower
17 courts it did not satisfy, and did not -- never came
18 forward with any evidence that it satisfied that test,
19 which was its burden as the claimant in this case.

20 QUESTION: You know, Sheppard's Tax Dictionary
21 does have a definition for minimum funding excise tax
22 which, it refers to this particular provision, so the tax
23 community as reflected by the tax dictionary calls it an
24 excise tax.

25 MR. McCARDELL: Your Honor, it certainly has

1 been treated in various ways as an excise tax, but not
2 even the tax practitioners would agree that a tax of this
3 nature is a tax for all purposes under the Internal
4 Revenue Code.

5 We've cited the conflicting line of cases on
6 similar taxes in the Third Circuit and the Eighth Circuit,
7 the Latterman case and the Rockefeller case, where there
8 is disagreement that taxes like this may not even be taxes
9 for purposes of the Internal Revenue Code, so that in view
10 of that kind of a disagreement in a tax of this nature,
11 it's difficult to say that you then import that concept
12 into the Bankruptcy Code when the tax code does not settle
13 bankruptcy priorities. That's settled by the statute and
14 the court's decisions interpreting the meaning of the
15 statute.

16 QUESTION: Mr. McCardell, I understand the big
17 difference it makes in the bankruptcy context whether it's
18 classified as one or the other. In terms of the IRC, does
19 it make any difference whether it's labeled excise or
20 penalty, since, as you have said, there's a specific
21 provision that makes this particular excise tax
22 nondeductible.

23 MR. MCCARDELL: I don't know that it does make a
24 difference, Your Honor, although, as I said in addressing
25 taxes of this -- penalty excise taxes of this nature, the

1 Third and Eighth Circuits have disagreed on the question
2 of whether they are taxes even for purposes of the
3 Internal Revenue Code's provisions calculating interest on
4 those taxes.

5 QUESTION: There's some discussion in the
6 briefs -- I think it's 507(a)(7)(G) -- relating to a
7 penalty related to a claim of a kind specified in this
8 paragraph and in compensation for actual pecuniary loss.

9 MR. McCARDELL: Yes.

10 QUESTION: Can you give me an example --

11 MR. McCARDELL: Yes, I can.

12 QUESTION: -- of a tax to which that would
13 apply?

14 MR. McCARDELL: I can, Your Honor. An example
15 would be the responsible officer penalty exacted under
16 6672. It represents an assessment of 100 percent against
17 the officer, responsible officer, of the taxes that should
18 have been paid by the corporation.

19 The Government gets what it would have received
20 if the law had been obeyed and, indeed, the Senate Finance
21 Committee report, which we've cited in our brief, in
22 describing pecuniary loss penalties, describes them as any
23 fine or penalty, however denominated, which actually
24 represent the collection of a tax. That's the concept we
25 believe is codified in section 50 --

1 QUESTION: Is -- withholding taxes, that's -- is
2 that -- the corporation withholds its employees taxes,
3 then it doesn't pay them, and the person who owes the tax
4 is the employee, and the code refers to the money that the
5 corporation should have withheld, which, of course, is the
6 tax that the employee owed, as a penalty, is that right?

7 MR. McCARDELL: That's correct.

8 QUESTION: And that's the idea of pecuniary
9 penalties?

10 MR. McCARDELL: It's what the Government would
11 have received if the law had been -- the tax that would
12 have been collected if the law had been obeyed.

13 QUESTION: And so the only things that are
14 pecuniary penalties are these instances where a
15 corporation is to withhold a tax that somebody else owes,
16 and the code refers to that as a penalty, or those as
17 penalties?

18 MR. McCARDELL: I can think of another example
19 of possible pecuniary loss penalty, and that is an
20 exaction under the Internal Revenue Code that simply
21 represents interest on a tax that should have been paid
22 and compensates --

23 QUESTION: Yes.

24 MR. McCARDELL: -- for the delay in payment.
25 That would be a -- but this kind of exaction is

1 distinct. -- It doesn't compensate any delay in payment.
2 It doesn't compensate any tax that was not collected.
3 Congress did not enact section 4971(a) with the idea that
4 individuals would not fund their pension plans and that
5 the IRS would then collect revenue.

6 Instead, it passed the statute with the idea
7 that individuals who had sponsored pension plans would
8 fund them, and that that funding would go to pay retirees.

9 QUESTION: They're required to fund them?

10 MR. MCCARDELL: Yes, they are. That's found in
11 section 302 of ERISA.

12 QUESTION: Is there any other penalty for not
13 funding them?

14 MR. MCCARDELL: They -- there's no criminal
15 penalty, Your Honor, but that under section 502 of ERISA
16 the failure to fund may be enforced by a civil action,
17 including injunctive proceedings, so that it is a
18 statutory obligation which, if violated, gives rise to
19 these escalating penalties.

20 Now, in this case, the -- not only did the IRS
21 fail to meet the traditional test for taxes, fail to
22 establish that a transaction had occurred, but in
23 asserting these claims, would have taken funds right out
24 of the pockets of the creditors, and many of those
25 creditors include the very retirees who are intended to be

1 protected by this statute. We don't think, all other
2 things being considered in this case, it makes sense for
3 the Court to adopt a rule which would reach that result.

4 Nothing in the statute requires that the court
5 read section 507 to require that any label in a
6 nonbankruptcy statute governs priority in bankruptcy.

7 The Court's cases, from the Embassy Restaurant
8 case, to the Nathanson case, to the Simonson case, all
9 clearly specify that the Court's mode of analysis over
10 many years has been to say that it's bankruptcy law that
11 establishes bankruptcy priorities, and labels or meanings
12 or understandings in nonbankruptcy statutes while,
13 perhaps, evidence, are not controlling.

14 That was the basis of the court of appeals
15 decisions in this case, and we believe the Court should
16 affirm the court of appeals.

17 QUESTION: Thank you, Mr. McCardell.

18 Mr. Jones, you have 2 minutes remaining.

19 REBUTTAL ARGUMENT OF KENT L. JONES

20 ON BEHALF OF THE PETITIONER

21 MR. JONES: I have two brief points I want to
22 make.

23 The claim that a tax that effects a penalty
24 loses its priority was exactly what this Court rejected in
25 United States v. New York under the Bankruptcy Act. The

1 Bankruptcy Code simply makes it easier to understand that
2 that's the correct answer, because knowing full well that
3 many of its excises are penalty or regulatory in nature,
4 Congress adopted an unqualified priority for excise taxes.
5 ~~this excise~~ We have to establish only that it's an excise
6 tax. ~~Whether it's also regarded as a penalty is not~~
7 relevant for applying the plain language of the statute,
8 and the court held in United States v. New York it was not
9 relevant under the Bankruptcy Act. ~~promise of insurance,~~

10 ~~they get~~ The other point -- ~~is~~

11 QUESTION: Mr. Jones, do you know whether it
12 makes any difference for the IRC purposes alone, ~~employees~~
13 forgetting bankruptcy, whether something is labeled excise
14 or penalty, assuming -- forgetting about the ~~without it.~~
15 deductibility, because this one is not deductible.

16 MR. JONES: You mean, in applying the excise tax
17 priority? ~~is all~~ There are a lot of people who have

18 ~~pensions~~ QUESTION: That -- no. No, not --?

19 MR. JONES: I'm sorry. ~~but for the insurance,~~

20 ~~they would~~ QUESTION: Forget bankruptcy. Just for the
21 purposes of the Internal Revenue Code, does it make any
22 difference whether something is labeled an excise tax or a
23 penalty? QUESTION: That is to say, aren't there ~~some~~

24 ~~people here~~ MR. JONES: Other than what we've already ~~reason~~
25 discussed, I'm not familiar with any circumstances. ~~is he~~

1 hate to make categorical statements, but I'm not familiar
2 with any. MR. JONES: No, sir. They're getting paid the
3 guarantee. And the other point that I want to address very
4 briefly is the suggestion that this -- the priority for
5 this excise tax is unfair because it comes in front of
6 claims of employees for residual retirement benefits. years,
7 on balance. In saying that, the court of appeals looked at
8 only the cost of the tax, and utterly ignored its benefit.
9 These employees not only get the promise of insurance,
10 they get the fact of insurance.

11 The Pension Benefit Guaranty Corporation comes
12 in and pays benefits, guaranteed benefits. The employees
13 are much better off with this guarantee system in effect,
14 including the priority tax, than they would be without it.
15 No one doubts --

16 QUESTION: They don't insure all of them. They
17 don't insure all. There are a lot of people who have
18 pensions whose pensions won't be paid, right?

19 MR. JONES: That's -- but for the insurance,
20 they wouldn't be paid at all.

21 QUESTION: Without insurance.

22 MR. JONES: Oh, without --

23 QUESTION: That is to say, aren't there some
24 people here, employees, who won't get paid, and the reason
25 they won't get paid their promised benefit is because the

1 IRS is going to collect this tax?

2 MR. JONES: No, sir. They're getting paid the
3 guaranteed benefits under the pension benefit system. The
4 IRS tax, which is designed to enforce the ability of the
5 United States to honor the promise to ensure benefits,
6 only comes in in front of residual claims. The employees,
7 on balance, are better off. They're going to get millions
8 of dollars in benefits by the insurance function.

9 CHIEF JUSTICE REHNQUIST: Thank you, Mr. Jones.

10 MR. JONES: Thank you.

11 CHIEF JUSTICE REHNQUIST: The case is submitted.

12 (Whereupon, at 12:02 p.m., the case in the
13 above-entitled matter was submitted.)

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CERTIFICATION

Alderson Reporting Company, Inc., hereby certifies that the attached pages represents an accurate transcription of electronic sound recording of the oral argument before the Supreme Court of The United States in the Matter of:

UNITED STATES, Petitioner v. REORGANIZED CF&I FABRICATORS OF UTAH, INC., ET AL

CASE NO: 95-325

and that these attached pages constitutes the original transcript of the proceedings for the records of the court.

BY Ann Marie Federico

(REPORTER)