

ORIGINAL

OFFICIAL TRANSCRIPT  
PROCEEDINGS BEFORE  
**THE SUPREME COURT**  
**OF THE**  
**UNITED STATES**

CAPTION: ASSOCIATES COMMERCIAL CORPORATION, Petitioner  
v. ELRAY RASH, ET UX. Respondents.

CASE NO: 96-454

PLACE: Washington, D.C.

DATE: Wednesday, April 16, 1997

PAGES: 1-58

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IN THE SUPREME COURT OF THE UNITED STATES

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ASSOCIATES COMMERCIAL	:
CORPORATION,	:
Petitioner	:
v.	: No. 96-454
ELRAY RASH, ET UX.	:
Respondents.	:

-----X

Washington, D.C.

Wednesday, April 16, 1997

The above-entitled matter came on for oral argument  
before the Supreme Court of the United States at 11:04 a.m.

APPEARANCES:

CARTER G. PHILLIPS, ESQ., Washington, D.C.; on behalf of  
Petitioner.

KENT L. JONES, ESQ., Assistant to the Solicitor General,  
Department of Justice, Washington, D.C.; on behalf of the  
United States, as amicus curiae, supporting Petitioner.

JOHN J. DURKAY, ESQ., Beaumont, Texas; on behalf of  
the Respondents.

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## P R O C E E D I N G S

(11:04 a.m.)

CHIEF JUSTICE REHNQUIST: We'll hear argument next in  
No. 96-454, Associates Commercial Corporation v. Elray Rash.

Spectators are admonished not to speak until you get  
outside of the courtroom. The Court remains in session.

Mr. Phillips.

ORAL ARGUMENT OF CARTER G. PHILLIPS

ON BEHALF OF THE PETITIONER

MR. PHILLIPS: Thank you, Mr. Chief Justice, and may it  
please the Court:

The issue in this case is whether the value of  
collateral that a Chapter 13 debtor proposes to retain and use  
should be determined by what the secured creditor could obtain  
if it foreclosed on that property and sold it, or by what the  
debtor would have to pay in order to acquire a comparable  
property.

Our argument is that Section 506(a) of the Bankruptcy  
Code declares that the value of the property should vary,  
depending on whether it is proposed to be used or proposed to  
be disposed of, and that a hypothetical disclosure value is  
insufficient and ignores the language of the statute.  
Accordingly, the Court of Appeals erred when it undervalued  
the secured interest of the Petitioner in this case.

This is a Chapter 13 case in which the Respondents

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1 proposed a plan that would permit them to keep a tractor  
2 trailer truck, which served as collateral for a debt owed to  
3 the Petitioner. At the time of the bankruptcy, the Petitioner  
4 was owed approximately -- well, not approximately -- was owed  
5 \$41,171, and it had perfected a lien on the -- under State  
6 law.

7 Petitioner sought, under Section 362, to lift the  
8 automatic stay and to repossess the truck. Respondents  
9 objected, sought to keep the truck as necessary for their  
10 reorganization, and asked the court to value the truck at  
11 \$28,500. They proposed to pay that amount, plus interest, and  
12 then to strip the lien from the -- from the Petitioner.

13 Both sides offered expert testimony on the value of the  
14 truck. The Respondents' expert valued it at retail, at  
15 \$42,500. Our expert valued it at \$41,000. And the -- the  
16 Respondents' expert also valued it at wholesale, at \$31,875,  
17 which he got to by discounting by 25 percent the retail value.  
18 And all of these numbers were derived, essentially, from  
19 standard industry bluebooks.

20 The Bankruptcy Court, the District Court and the Court  
21 of Appeals all concluded that, under these circumstances, they  
22 had to decide the question as a matter of law, which is the  
23 proper method of valuation, wholesale or retail. In doing so,  
24 they quite properly turned to Section 506(a) of the Code.  
25 Unfortunately, they misconstrued that provision.

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1           506(a) has two sentences. The first sentence tells you  
2 what you value. And as this Court held in Timbers, that  
3 phrase simply tells you that you value the creditor's  
4 collateral. The first sentence says nothing about how you  
5 value the collateral.

6           The second sentence, which is reproduced on page 3 of  
7 the Petitioner's brief, says that the way you value collateral  
8 is that you -- is that you value -- shall be determined in  
9 light of the proposed disposition or use of such property.

10          Now, the Court is fond of observing, generally speaking,  
11 that --

12          QUESTION: You left out part of the sentence, though, I  
13 think, didn't you, Mr. Phillips?

14          MR. PHILLIPS: I'm sorry, Your Honor?

15          QUESTION: You left out part of the sentence.

16          MR. PHILLIPS: That's true. You're supposed to do it in  
17 light of the purposes of the valuation and --

18          QUESTION: Is it -- or of the -- or, and of the proposed  
19 disposition.

20          MR. PHILLIPS: Right.

21          QUESTION: Right.

22          MR. PHILLIPS: Right. I'm sorry.

23          QUESTION: Yes.

24          MR. PHILLIPS: I will reread it: shall be determined in  
25 light of the proposed disposition or use of the property.

1 Suggesting, as we -- as we say --

2 QUESTION: No, in light of the purpose of the valuation  
3 and of proposed disposition.

4 MR. PHILLIPS: That's correct, Your Honor. Although  
5 there is no dispute between the parties about the purpose of  
6 the valuation, so I -- I skipped over that.

7 QUESTION: What was the purpose of the valuation?

8 MR. PHILLIPS: Well, the purpose of the valuation here  
9 was to decide the full extent of our -- of our collateral, for  
10 purposes of deciding how much money should be paid as part of  
11 -- as part of the Chapter 13 reorganization. And there's no  
12 dispute over that.

13 QUESTION: Now, I suppose, if the higher value had been  
14 placed on it, that the reorganization might not have occurred  
15 -- at least that's what Respondents say. They couldn't have  
16 made the payments. And then your client would have had to  
17 take a truck back and sell it, presumably at wholesale value.

18 MR. PHILLIPS: That -- that is correct, Your Honor. But  
19 we would have been perfectly happy with that, because that's  
20 what we proposed in the first instance. But it's not at all  
21 clear, and it's simply speculation as to whether or not this  
22 Chapter 13 reorganization would have succeeded or not.

23 QUESTION: Well, in any event, the thing proceeded, and  
24 Respondents made payments for 5 years, and presumably have  
25 completed this thing. Now, if you prevail, what's going to

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1     happen on remand?

2             MR. PHILLIPS: Well, what the Respondent said in  
3     opposition to the stay in the Bankruptcy Court was that they  
4     remain on the hook to pay back Associates for the amount of  
5     money that's owed. And it's approximately \$7,000 -- is the  
6     difference between what they paid and what we think they  
7     should have paid. So --

8             QUESTION: Now, there are no warranties, I guess, left  
9     on the truck as far as the debtor is concerned at this point  
10    -- I mean at the point they kept the truck. Does that have to  
11    be taken into consideration in setting a value?

12            MR. PHILLIPS: Well, the appraiser can -- ordinarily, I  
13    think the appraiser would take into consideration what is on  
14    the truck. I mean what you're being asked to do is to replace  
15    the truck that that particular --

16            QUESTION: Yeah, and it might -- it might not be  
17    straight blue book wholesale value.

18            MR. PHILLIPS: Right. But then the appraiser could --  
19    could adjust it, to take into account precisely what's on the  
20    truck. Just as if, for some reason, there was something very  
21    special that he put on the truck that he paid for that wasn't  
22    part of the secured interest. I don't think that we would get  
23    the higher value of that, as we say in the brief. You know,  
24    you would look at it as a truck to replace, essentially, what  
25    the secured interest is, what is the collateral.

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1 QUESTION: Well, just on this preliminary point, there  
2 was some payment to be made to the unsecured creditors I think  
3 a few years down the line, was there not?

4 MR. PHILLIPS: Yes, there was money paid to unsecured  
5 creditors.

6 QUESTION: All right. So -- so if the replacement value  
7 had been granted, maybe this is just a question between the  
8 secured and unsecured creditors, not between the debtor and  
9 the secured creditors?

10 MR. PHILLIPS: Generally speaking, that is going to be  
11 the case. Is this -- the question is whether or not the  
12 unsecureds get anything --

13 QUESTION: Well, then --

14 QUESTION: Sorry.

15 QUESTION: No, that's okay.

16 QUESTION: Were you finished?

17 QUESTION: Or if it would be the case, and I think it  
18 would be.

19 The words "wholesale" and "retail" don't appear in this  
20 statute. So I take it Congress wanted to leave it up to the  
21 bankruptcy judge, pretty much. And why wouldn't the  
22 bankruptcy judge be sensible in saying, well, the value  
23 includes whatever will be disputed between the unsecured and  
24 secured creditors?

25 But, as in this case, if you value it at 41,000, and

1 then he can't even go into the -- Chapter 13 because he just  
2 doesn't have that money, that couldn't possibly be the value.  
3 There's no theory on which that would be the value, because if  
4 you value it at that, there won't be a Chapter 13  
5 reorganization.

6 MR. PHILLIPS: Well, but --

7 QUESTION: So we cut back the value in order to make  
8 certain he gets into the reorganization, he puts in his  
9 disposable income that you get the amount insofar as it's in  
10 dispute between the creditors.

11 Now, that kind of result seems fair. And it would be  
12 very case specific.

13 MR. PHILLIPS: Well, no, that kind of result seems to  
14 undo the statute. Chapter 13 is not --

15 QUESTION: It doesn't say.

16 MR. PHILLIPS: -- essentially, a right that all debtors  
17 have. They have a choice between Chapter 7 and Chapter 13.  
18 And if their debts are -- are too great to allow them to  
19 reorganize under Chapter 13, then they have to put up with --  
20 under -- with Chapter 7.

21 QUESTION: But how could the -- the value for purposes  
22 of a Chapter 13 reorganization, insofar as that exceeds what  
23 your client would get in a liquidation, couldn't -- it's  
24 nonexistent if there isn't going to be a Chapter 13  
25 reorganization.

1 MR. PHILLIPS: But -- but it seems to me that you -- you  
2 -- you have to look at the language of the statute. And  
3 Section 506(a) says look at the proposed disposition or the  
4 proposed use. Now, if -- if he cannot use it and successfully  
5 come out of Chapter 13, then he is required to go under  
6 Chapter 7. And you don't avoid the Chapter 7 problem by --

7 QUESTION: In other words, you -- you don't agree that  
8 -- that a secured interest is not a secured interest if -- if  
9 its existence would prevent Chapter 13?

10 MR. PHILLIPS: Exactly. Exactly.

11 QUESTION: That sounds reasonable to me, too.

12 MR. PHILLIPS: Thank you, Your Honor.

13 QUESTION: Isn't it also relevant, Mr. Phillips, that --  
14 and -- the Chapter 13 proposal was not that your client get  
15 the security back at whatever value, but that the security  
16 remain in the hands of the debtor and continue to depreciate?

17 MR. PHILLIPS: That's -- that's -- that's exactly right,  
18 Mr. Chief Justice. And -- and the point I was starting to  
19 move toward, which is the rule of construction, that the Fifth  
20 Circuit relied upon and that I think, really, is where they  
21 made the fundamental error in this case, is by saying that the  
22 State law rights that are implicated here favor requiring us  
23 to show by clear and unambiguous language that our  
24 interpretation of the statute is the correct one --

25 QUESTION: Mr. Phillips, may I -- may I ask you about



1 the Fifth Circuit, because I thought that the main point for  
2 Judge King was based on the Federal statute as much -- well,  
3 more than the State law point that you were about to deal  
4 with. She looked to 1325, and she said, now there are two  
5 things the debtor can do in this situation. And one is  
6 surrender the collateral. Give it back to the creditor. And  
7 then it would have what's been called wholesale value.

8 The other thing is leave it with the debtor and value  
9 it. The question that she put was, why should there be  
10 different results whether which of those two routes the  
11 creditor who doesn't want to go along with the reorganization  
12 -- which -- which route that is -- is picked by the debtor.

13 MR. PHILLIPS: Right. And the answer to that is  
14 twofold. One is that the language suggests -- proposed  
15 disposition or proposed use -- which suggests that there are  
16 different methods of valuation. And second of all, there's no  
17 reason to assume equivalence between what you do if you give  
18 up the property and what you do when you retain the property  
19 and use it as part of a successful reorganization.

20 There's clearly a difference in the valuation. Both  
21 parties agree on that. And the only question is who should  
22 get the benefit of the difference in the valuation. If you  
23 use always a hypothetical foreclosure value, then -- then --  
24 then there's -- you never have any advantages.

25 QUESTION: But I thought the question was putting --

1     what -- what rationale would the legislature have for having  
2     two different -- one much more favorable to the secured  
3     creditor? And I thought that that was the point. Wouldn't  
4     one logically expect, in the balance between the secured and  
5     unsecured, either of those routes to yield the same end  
6     result?

7             MR. PHILLIPS: Well, again, I don't think so. And the  
8     reason is, in part, the Congress envisioned that there would  
9     be negotiations between the parties on these kinds of issues.  
10    And you can only negotiate if you have some kind of  
11    differential in the valuations. And if you use the same  
12    hypothetical foreclosure valuation, you'll always end up with  
13    the same number. Which means there is no basis for  
14    negotiation between the debtor and the creditor in any  
15    particular case.

16            And it seems clearly -- and there's nothing in anything  
17    that supports the notion that going along on the disposed use  
18    -- I mean going along with the proposed use, as opposed to  
19    proposed disposition, is meant to get you to the same value.  
20    It doesn't. The assumption is, is that it will create more  
21    value, because it's going to be used.

22            QUESTION: If -- if that is your -- your theory, if we  
23    adopt that theory, then would it be an abuse of discretion or  
24    a violation of the statute for a judge -- a bankruptcy judge  
25    to adopt Judge Posner's solution, which is just split the

1 difference?

2 MR. PHILLIPS: Yeah, it would be a violation of the  
3 statute, because, again, the statute tells you to look at the  
4 proposed use or proposed disposition, and -- and Judge  
5 Posner's analysis does neither of those things. It does an  
6 amalgam of the two. And so, therefore, it has no statutory  
7 basis. It's much like the rule that the Court condemned in  
8 BFP, the 70 percent rule, that said if you deviate by 70  
9 percent. I mean it's a good rule and it might make good  
10 policy and Congress might want to adopt it, but there's  
11 nothing in the statute that -- that remotely supports it.

12 QUESTION: But, in particular --

13 QUESTION: Go on.

14 QUESTION: No, please.

15 QUESTION: Go.

16 QUESTION: In particular cases that might be a sensible  
17 thing for -- for the -- for the judge to do, I take it. The  
18 judge might very well say, well, you know, I don't know  
19 whether they buy it for a dollar more than the foreclosure  
20 value or a dollar less than retail. And the evidence is  
21 unclear. So the only fair thing for me to do in this  
22 particular case is to split the difference.

23 I -- I take it you're not ruling out that possibility in  
24 individual cases, or are you?

25 MR. PHILLIPS: Well, I'd have to see the particular

1 case. It seems to me that if the evidence in the record is  
2 that there are two very distinct appraisal values and they are  
3 supported by solid testimony, it seems to me you'd probably be  
4 obliged to take one rather than the other, rather than split  
5 the difference.

6 QUESTION: Well, one party says, well -- we -- we can  
7 reasonably hypothesize three bidders at the foreclosure for  
8 the -- for the disposal of the -- of the property, and there's  
9 a fight about that. There might be cases in which the court  
10 could say, look, I -- I -- I can't calibrate these  
11 probabilities, and the only sensible thing to do is to say  
12 it's somewhere in the middle. You don't rule out that?

13 MR. PHILLIPS: I don't rule that out. The important  
14 part about that, though, to keep in mind is, is that's not the  
15 difference between the hypothetical foreclosure value and the  
16 use value. What I'm looking at -- what you're talking about  
17 are two different use values and trying to resolve those by  
18 splitting the difference.

19 QUESTION: But your argument is you simply cannot  
20 construe the statute, as a matter of law, to require that  
21 median figure?

22 MR. PHILLIPS: That's correct.

23 QUESTION: That's your understanding?

24 MR. PHILLIPS: Yes.

25 QUESTION: Mr. Phillips, let me ask, while I do not



1 agree with Justice Breyer's suggestion that the valuation  
2 should be whatever it takes to enable the 13 to proceed, there  
3 is some textual basis for -- for saying that. What meaning do  
4 you give to the -- to the other portion? You say both parties  
5 agree as to what the purpose of the valuation was. But -- but  
6 what -- what is the meaning of that: Such value shall be  
7 determined -- we're discussing here -- in light of the  
8 proposed disposition or use? But it also says: in light of  
9 the purpose of the valuation.

10 What -- what does that mean?

11 MR. PHILLIPS: Well, there are lots of different  
12 situations which --

13 QUESTION: And a lot of different purposes. Why would  
14 its valuation be different for one purpose rather than  
15 another? I'm not sure.

16 MR. PHILLIPS: Well, it depends on --

17 QUESTION: Give me an example of -- of --

18 MR. PHILLIPS: Of a situation where that --

19 QUESTION: -- in which the purpose would -- would --  
20 would produce a different valuation.

21 MR. PHILLIPS: Well, my guess is it might make a  
22 difference whether or not you are trying to decide whether the  
23 outstanding debt puts you into Chapter 13 in the first place,  
24 because there are limits on how much debt you can carry into  
25 Chapter 13. So you might value that differently.

1 QUESTION: Now, why -- why should that affect the  
2 valuation you give?

3 MR. PHILLIPS: Well, if Congress had made clear -- and  
4 -- and I'm speculating here, because I don't know the answer  
5 to this -- but if Congress indicated a preference at the edges  
6 to have more cases into Chapter 13, where it's close, you  
7 might, under those circumstances, attempt to value the  
8 outstanding debt in a way that would make it, you know, less  
9 in order to bring them into Chapter 13.

10 QUESTION: Okay. But you don't think Congress has  
11 indicated any preference for Section -- for Chapter 13?

12 MR. PHILLIPS: Not -- not with the language "proposed  
13 disposition or use." I think what Congress has clearly  
14 indicated is that if you have a proposed use, then you should  
15 value it from the perspective of what the debtor would pay in  
16 order to be able to acquire that exact same property and to  
17 use it. And -- and I think it's important -- I want to go  
18 back to the rule of construction, because I think it's vital  
19 to the -- the proper outcome of this case.

20 We're dealing with a situation here where the Court of  
21 Appeals said that the problem is -- is that your rights under  
22 State law are measured by foreclosure value. Now, our rights  
23 are not measured by the foreclosure value. Our rights are  
24 measured by the lien. And the lien, it protects us all the  
25 way through to the actual payment. It's supposed to protect

1 the stream of payments. That's the vital element of what our  
2 State rights are. And to come in here --

3 QUESTION: Yes, but it only gives that protection to the  
4 extent that there -- the value of the lien can be realized  
5 through sale of the collateral.

6 MR. PHILLIPS: No, that's not true, Your Honor. I mean  
7 it is true that you have a remedy to sell the collateral, but  
8 that's not the end of your right. You're still entitled to a  
9 judgment for the amount of the debt that's outstanding. And  
10 that's how your State law right is defined. And that really  
11 is the mistake that the Court of Appeals made.

12 We have a much broader State law right, which ought to  
13 be valued here. And this Court said both Radford and in --

14 QUESTION: I'm really puzzled by that. Because if you  
15 proceeded under State law, you'd get what the other side says  
16 you should have.

17 MR. PHILLIPS: No, no. I --

18 QUESTION: You would foreclosure, you'd sell the it and  
19 you would get the wholesale value.

20 MR. PHILLIPS: And I'd still be entitled to the  
21 difference between what the -- the --

22 QUESTION: The deficiency.

23 MR. PHILLIPS: -- the under amount and the amount of the  
24 actual debt.

25 QUESTION: Yeah, but you still are here as a general

1 creditor, aren't you?

2 MR. PHILLIPS: Well, I understand that. But we're not  
3 -- we're not --

4 QUESTION: Which is all you'd be under State law.

5 MR. PHILLIPS: But we're not distributing it under those  
6 circumstances. That's the point.

7 QUESTION: No. But under State law, if you had a  
8 \$50,000 debt, secured by collateral worth 40,000, you'd  
9 foreclose, you'd get your 40,000, and you'd be a general  
10 creditor for the 10,000.

11 MR. PHILLIPS: No -- but that's if I'm in bankruptcy.  
12 Under State law, I'd -- I'd foreclose and I'd go and ask him  
13 --

14 QUESTION: You would be under State law, too.

15 MR. PHILLIPS: -- ask him for the extra money --

16 QUESTION: Yeah, but here --

17 MR. PHILLIPS: -- and I'd go against the other assets.

18 QUESTION: Here you don't -- you don't get to have your  
19 security back. It's still in the hands of the debtor.

20 MR. PHILLIPS: Exactly.

21 QUESTION: And all you're getting is -- is periodic  
22 payments.

23 MR. PHILLIPS: Exactly. And that is precisely what the  
24 Court said in Radford. You don't expect Congress to do --  
25 unless it does it expressly. And Congress clearly didn't do



1 it expressly here.

2 QUESTION: Yeah, but you're getting the periodic  
3 payment. Is it not true, though, that you do have the status  
4 of a general creditor as to the difference?

5 MR. PHILLIPS: As to the difference, that's correct.

6 QUESTION: Yeah, okay.

7 MR. PHILLIPS: I'd like to reserve the balance of my  
8 time.

9 QUESTION: Very well, Mr. Phillips.

10 Mr. Jones.

11 ORAL ARGUMENT OF KENT L. JONES

12 ON BEHALF OF THE RESPONDENTS

13 MR. JONES: Mr. Chief Justice, and may it please the  
14 Court:

15 The common sense -- the history of the statute, in this  
16 Court's opinion in Whiting Pools, all reflect that when  
17 collateral is retained for the use of the debtor, it has a  
18 going concern or fair market value that exceeds its  
19 liquidation value and that enhances the value of the secured  
20 claim. This additional value --

21 QUESTION: Mr. Kent, could you -- could you explain to  
22 me, then, what Judge Easterbrook meant, because you just made  
23 this common sense proposition. This is quoted in the appendix  
24 to the petition for cert at 30-31 -- it's something the Fifth  
25 Circuit seemed to rely on -- that there was no real difference

1 between these two values when you take out of the so-called  
2 retail value the things that don't relate to the object  
3 itself.

4 MR. JONES: Well, Judge Easterbrook, in that part of his  
5 opinion, in the, what, Hansen case, I believe, was -- was  
6 thinking --

7 QUESTION: Samson against Alton Bank.

8 MR. JONES: Ah, okay. Judge -- that's a different  
9 opinion than the one I was referring to. What Judge  
10 Easterbrook may have been referring to is the difference  
11 between cost, replacement cost, and value. Replacement cost  
12 could include items that would not need to be spent if the  
13 item were to be replaced from the own inventory, if you will,  
14 of the debtor. But that doesn't have -- that cost doesn't  
15 relate to the value of the asset.

16 The value of the asset is dependent upon what -- is  
17 dependent upon what the use -- what use can be made of it.  
18 And a debtor can't reasonably say that the value of the asset  
19 in his possession has a different value than it would in the  
20 possession of anyone else who used the same sort of property.  
21 Congress used an objective term, "value." And value in that  
22 sense is what --

23 QUESTION: May I, just before -- you're talking about  
24 replacement -- market value rather than replacement cost?

25 MR. JONES: Replacement cost is -- is a term that can be

1 used to describe value in the sense that value is what a  
2 willing buyer would pay a willing seller to -- for the right  
3 to use the same property. That's the way the Court defined it  
4 in the BFP case.

5 And there's something important in BFP that really is --

6 QUESTION: In your submission, is that the same or  
7 different from replacement cost?

8 MR. JONES: Well, replacement cost is normally what a  
9 willing buyer would pay a willing --

10 QUESTION: You can't answer it yes or no, our favorite  
11 thing to lawyers?

12 MR. JONES: Well, I would say it's the same, but I --

13 QUESTION: It's the same, okay.

14 MR. JONES: But I -- but -- but it depends on who is  
15 paying it. I mean if you use the objective concept of the  
16 willing buyer and the willing seller, it's the same. Yes.

17 BFP makes the point that the difference between a  
18 liquidation value and a fair market value is that fair market  
19 value is realized if an ample opportunity is given to realize  
20 the full value of the collateral. That's exactly what a  
21 Chapter 11 and Chapter 13 reorganization do. They give the  
22 debtor the opportunity, the ample opportunities, the Court  
23 said in BFP, to realize the full value of the collateral.

24 Now, that is the value -- the difference between the  
25 fair market value and the liquidation value, that premium or

1 surplus, whatever you want to call it, is the heart of the  
2 reorganization concept.

3 QUESTION: But, in a sense, the security owner ought to  
4 be able to get the same amount of money, if -- if it took its  
5 time and sold the property.

6 MR. JONES: Congress didn't -- didn't write the statute  
7 that way. And -- and -- and nor does --

8 QUESTION: In theory --

9 MR. JONES: -- as a practical matter --

10 QUESTION: As a practical matter, it seems to me they  
11 might be pretty close together.

12 MR. JONES: What -- what Section 506(a) does, by  
13 distinguishing between disposition and use, distinguishes  
14 between a liquidation and a reorganization. And in a  
15 reorganization, what Congress had in mind was that there would  
16 be this surplus value created. It's -- it's like Pareto  
17 optimality. Everyone, debtor and creditor alike, are going to  
18 be made better off. And no one is going to be made worse off  
19 than they would be in a liquidation.

20 The provisions of Sections 1325 and 1129 that -- that  
21 invoke this valuation process make clear that Congress didn't  
22 intend a liquidation value to apply when collateral is  
23 retained by the debtor. There is a little bit of text here,  
24 but I've got to go through it. 1325(a)(5) and 1129(b)(2) both  
25 provide that the debtor can retain the collateral in a

1 reorganization if it pays the allowed amount of the secured  
2 claim as determined under Section 506.

3 Sections 1325(a)(4) and 1129(a)(7), by contrast, say  
4 that an unsecured creditor is only guaranteed to get, in a  
5 reorganization, what he would get if the property had been  
6 liquidated. So Congress clearly distinguished between the  
7 treatment of a security -- secured claim and an unsecured  
8 claim in reorganizations.

9 What the Court of Appeals did in this case was to say,  
10 we're going to give them exactly the same train, we're going  
11 to -- treatment -- we're going to abolish the distinction,  
12 because a secured creditor, like an unsecured creditor, will  
13 only receive the liquidation value of the asset -- what he  
14 would have gotten if there had been a liquidation. That  
15 result plainly violates a fundamental principle of statutory  
16 interpretation, because it nullifies the careful distinctions  
17 that Congress made between secured and unsecured claims in  
18 these reorganization cases.

19 Section 506(a) itself, of course, specifies that this  
20 value is to be determined based upon the proposed disposition  
21 and use of the property.

22 QUESTION: Yes. And what -- do you have any notion as  
23 to what the other thing, in -- in light of the purpose of the  
24 valuation -- do you have any notion --

25 MR. JONES: Well, an example of a -- of a different



1 purpose for the valuation would be to -- when a creditor wants  
2 adequate protection for the use -- for the temporary use of  
3 the asset during the period before -- during -- for example,  
4 before a liquidation or at some point during the process of  
5 the reorganization. 361 --

6 QUESTION: Well, why would you give it a different  
7 valuation for that purpose than you would for --

8 MR. JONES: Well, it's not some -- it's not necessarily  
9 the -- I'm no -- I can't answer, in the abstract, that there  
10 would be a different valuation for that. It's just that you  
11 would want to know what the purpose of the valuation was.  
12 Because, in 361, when you're determining whether -- what  
13 you're supposed to decide is whether the collateral is  
14 diminishing in value by its use during the reorganization  
15 procedures. And so, in deciding how much it's diminishing in  
16 value, I suppose you -- the purpose would be to focus on that.

17 Whereas here, the purpose is to determine what is the  
18 value to be realized from the use of the collateral -- what  
19 would a willing buyer pay a willing seller for the right.

20 QUESTION: You're always going to have a possible  
21 difference in valuation. If you simply take something out and  
22 sell it at forced sale as opposed to, say, renting it for a  
23 couple of years and -- with an assured tenant, there is going  
24 to be a difference in valuation.

25 MR. JONES: Absolutely. And -- and in Whiting Pools,

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1 this Court noted that Congress fully understood that you --  
2 that -- that the -- in a reorganization, when the debtor is  
3 allowed to retain the collateral, that the -- the value would  
4 be greater than what I think the Court said it would be if  
5 they scrapped it, if they sold it at a foreclosure sale.

6 And in BFP, as I've already mentioned, the Court  
7 explained that the difference -- well, I didn't mention this  
8 -- I meant to -- that in BFP --

9 QUESTION: You were about to.

10 (Laughter.)

11 QUESTION: Somebody interrupted you --

12 MR. JONES: In 10 minutes --

13 QUESTION: -- just as I'm doing now, right?

14 (Laughter.)

15 MR. JONES: It's just kind of all blends together.

16 That in BFP, the Court explained the difference between  
17 a liquidation value and a fair market value -- well, I did say  
18 this -- is the -- is that you have an ample opportunity to  
19 make the -- to make -- to realize the full value of the  
20 collateral. That is what reorganizations give you. They give  
21 you that ample opportunity to get that value. And the value  
22 that you've gotten is the value that is referred to in 506(a).

23 QUESTION: Is -- is it possible that -- accepting for  
24 argument's sake all your arguments -- that it's better to give  
25 this money to the secured creditor, basically, than the

1     unsecured? Still, doesn't what he's argued in his red brief  
2     at least set a ceiling on what you can -- I mean, in other  
3     words, if it's impossible for the person to go into  
4     reorganization --

5             MR. JONES: Right.

6             QUESTION: -- unless you lop off some of this surplus --  
7     well, then, I don't see how you could value the secured  
8     interest at an amount that includes what we've just seen is  
9     lopped off?

10            MR. JONES: The only reason we're -- the only purpose of  
11     the valuation involved in this case is if he does qualify for  
12     a 13, if there is a surplus that will be realized. Sometimes  
13     debtors can't --

14            QUESTION: But he said, I think, that he couldn't  
15     qualify if he had to -- if he had to --

16            MR. JONES: Sometimes debtors' business situation is  
17     such that they cannot -- they cannot generate the surplus.  
18     They cannot -- don't forget, 1325(a)(5)(B) will require that  
19     debtor to pay the value of this collateral if he's going to  
20     use it. And Chapter 13 is only available if a debtor can meet  
21     that requirement. And a debtor who can't meet that  
22     requirement, because, for example, his business roots might --  
23     might -- might not recognize the income available from such an  
24     asset, is a -- is a debtor who may not qualify under Chapter  
25     13.

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1 Congress did not mean to let anyone qualify. They were  
2 very severe about the requirements.

3 QUESTION: Of course, they would not open-end that  
4 valuation based on anything that will let the man qualify.  
5 But what if the condition is that he would qualify as long as  
6 he provides the creditor with as much as the creditor would  
7 realize if the creditor foreclosed?

8 MR. JONES: Well, that's exactly what he has to give  
9 unsecured creditors. That's what he has to make sure  
10 unsecured creditors get. And that was the point I was making  
11 earlier. 1325(a)(5) says that for a secured creditor, he's  
12 got to give them the allowed amount of the allowed secured  
13 claim as determined under Section 506.

14 By doing that, Congress meant clearly to provide a  
15 different result for the secured creditor than the unsecured  
16 creditor. But what the Court did here was to treat them  
17 identically. And that deprived the words of the statute of  
18 any plausible meaning.

19 QUESTION: Thank you, Mr. Jones.

20 MR. JONES: Thank you.

21 QUESTION: Mr. Durkay, we'll hear from you.

22 ORAL ARGUMENT OF JOHN J. DURKAY

23 ON BEHALF OF RESPONDENTS

24 MR. DURKAY: Mr. Chief Justice, and may it please the  
25 Court:

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1           The issue before the Court today is the value of a  
2   truck. And the context is this: Instead of allowing the  
3   secured creditor to take back the truck and put it on the  
4   market to sell, the debtor is going to be allowed to retain  
5   the truck and use it in his business.

6           If I can make one comment, Chief Justice Rehnquist,  
7   about that that came up in one of your statements of concern  
8   earlier. Remember, the secured -- the debtor is not just  
9   going to retain the collateral. He's going to do a lot more  
10   than that. He's going to be required, under the system to pay  
11   interest. He's going to be required to answer to the  
12   strongest collection agent in the country, the Chapter 13  
13   trustee. The minute he's late there's going to be a motion to  
14   dismiss the bankruptcy. He's got to maintain full insurance  
15   at all times.

16           QUESTION: But he does run the risk of seeing the  
17   collateral depreciate in value very sharply, does he not?

18           MR. DURKAY: The secured creditor can insist that that  
19   depreciation never be faster than the amount of payments.  
20   That's not 506. That's 362. And adequate protection would  
21   apply in a Chapter 13 plan.

22           QUESTION: Well --

23           MR. DURKAY: This was, remember, not only a 502 hearing,  
24   but it was also a motion to stay.

25           QUESTION: Yeah, but none of the parties can fully



1 anticipate what the bluebook on this particular truck is going  
2 to say 5 years from now.

3 MR. DURKAY: Correct. Correct.

4 Finally, of course, he has to promise to preserve and  
5 maintain the collateral. You know, your point is well taken  
6 in this sense. But, remember, nobody knows what property is  
7 going to be worth in the future. That's part of what we're  
8 doing. We're trying to find out. Now, one of the things we  
9 do to try and find out is we go to people that know.

10 I'd like to raise another question, I think, that's been  
11 raised already in argument, that there were two experts here.  
12 If you read in the transcript on page 90, at the end of the  
13 hearing, the bankruptcy judge said there's only been one  
14 expert in this case.

15 One of the problems with the whole posturing of the case  
16 to this point in time, from the point of view of understanding  
17 where it's coming from, is in order to make sure that the  
18 Rashes were going to win their hearing and get a good  
19 confirmal plan, Mr. Baron and I made a tactical decision that  
20 we weren't going to come in and try to prove a forced sale or  
21 foreclosure sale or any of that. We brought an appraiser in,  
22 who testified as to fair market value. The fair market value  
23 of this truck is \$31,875. And the judge, listening to the  
24 testimony, totally rejected the so-called testimony of --  
25 brought by the Associates.

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1           The witness from the Associates had never seen the  
2   truck. He admitted it. He didn't even know what color it  
3   was.

4           QUESTION: Never seen any truck or he hadn't seen this  
5   truck?

6           MR. DURKAY: That truck.

7           Well, you know, the Uniform Standards of Professional  
8   Appraiser Practice is a guide here. It's --

9           QUESTION: Well, but you're indicating by your tactical  
10   -- your strategic decision that you made that you could have  
11   asked for foreclosure value?

12          MR. DURKAY: The Fifth Circuit says we could have.

13          QUESTION: Well, that --

14          MR. DURKAY: That's their opinion. We didn't --

15          QUESTION: But you didn't -- in other words, you didn't  
16   even try that in the -- in the -- in the trial court. That  
17   would have been your right under this theory of the case?

18          MR. DURKAY: Right. And -- and the reason was tactical.  
19   We wanted to win. We -- we took a -- we gave the number,  
20   31,875 --

21          QUESTION: Well, was it -- was it error, then, for the  
22   judge to find the value that he did?

23          MR. DURKAY: No, the judge --

24          QUESTION: I mean, your view of the case, he should have  
25   said, no, no, it's foreclosure value.

1 MR. DURKAY: No -- well, it -- it's at least foreclosure  
2 value. That was the issue.

3 QUESTION: Well, so far as it's more than that -- let's  
4 suppose it's -- suppose, in the hands of your client, this is  
5 going to earn enough money so that he has plenty of money to  
6 -- to pay what he owes, or much of it, why should the extra  
7 amount, up to the retail value or the replacement value, go to  
8 unsecured creditors rather than the person who had the  
9 foresight to take a secured interest in the truck?

10 MR. DURKAY: I think --

11 QUESTION: That's the part that's worrying me the most.

12 MR. DURKAY: I think what 506 says, if I can get  
13 directly to that, is that the Associates is entitled to be as  
14 well off as if they had taken the truck back and sold it.  
15 They're not entitled to be better off.

16 QUESTION: Well, they're -- if they took the truck back,  
17 it just says that's one of their options -- C, I think.

18 MR. DURKAY: Correct.

19 QUESTION: Well, they might use it themselves. They  
20 might look around for a long time. They might -- who knows  
21 what they might do. And these things are always -- all we  
22 know is they want to take it back.

23 MR. DURKAY: Correct.

24 QUESTION: And so if they want to take it back, they  
25 must think they're better off. And -- otherwise they wouldn't

1 want to.

2 MR. DURKAY: And that's the argument they used about Mr.  
3 Rash, saying, if I want to keep the truck, the truck has to be  
4 worth more value. That -- that truck is still the same truck.  
5 It doesn't increase or decrease in value because somebody does  
6 or doesn't want to retain it or not retain. It's the same  
7 truck.

8 QUESTION: Well, I didn't mean to get sidetracked.  
9 Because my question really was, why not -- why not give the  
10 extra amount, above the 31 -- suppose it turns out to be 38 or  
11 whatever it is -- why shouldn't that go to the truck owner  
12 rather than the unsecured creditors? I understand that maybe  
13 your client should be -- shouldn't -- if the money isn't there  
14 for him to go into 13, that seems like a separate argument.  
15 But the unsecured versus the secured?

16 MR. DURKAY: Because that additional money isn't just  
17 being generated by the truck. It's also being generated by  
18 Mr. Rash driving the truck. You know, I heard a --

19 QUESTION: Well, but --

20 MR. DURKAY: I'm sorry.

21 QUESTION: -- it -- it sets up a -- a queer scheme for  
22 -- for Chapter 13. You -- you -- you're telling the unsecured  
23 creditors -- you -- you don't -- you don't tell them, you're  
24 not going to get any more out of Chapter 13 than what you get  
25 if you -- if you demanded all of your money right now. We're

1 going to give you an incentive to let the guy continue to do  
2 business. You -- you may get more.

3 But you're not telling that to the secured creditors.  
4 You're insisting that the court-secured creditors get nothing  
5 more, as secured creditors, than they would have gotten by  
6 foreclosing immediately and taking the truck away. Leaving  
7 them no incentive, no benefit from the Chapter 13, although  
8 you give the benefit to the unsecured creditors.

9 MR. DURKAY: We -- we guaranteed to them in the process  
10 that they're at least going to get their liquidation value.  
11 And then we allow them to participate as an unsecured  
12 creditors.

13 QUESTION: But you --

14 MR. DURKAY: And that's a fair balancing.

15 QUESTION: But you don't say that to the unsecured  
16 creditors. You don't tell them, you're not going to get any  
17 more out of this than what -- what you would have gotten if  
18 you -- if you closed down the business today. Why should you  
19 -- why should you say that to the secured creditor?

20 MR. DURKAY: I think, in the bottom line, what  
21 reorganization is all about is trying to create value, as  
22 opposed to Chapter 7, which is liquidation, close the door,  
23 let's see what we've got. The way you measure whether or not  
24 a reorganization is a good reorganization is you measure it  
25 against the standard of what would happen in a 7. If we're



1 going to have a 7, what are the results? That's what is the  
2 so-called liquidation analysis, the Chapter 7 analysis. All  
3 right.

4 Now, if its reorganization is able to do better than  
5 that, okay, it probably should go forward. That's the goal,  
6 to do better than the straight liquidation.

7 In this case, there are a lot of parties that are then  
8 going to look to that additional amount of money. The Rashes  
9 get to live on some of the money that they make, within the  
10 bounds of the disposable income test. The Chapter 13 trustee  
11 in the system gets some compensation. At the point in time  
12 when you begin to distribute this extra value, this extra  
13 value is almost totally attributable to the fact that an  
14 individual made a commitment to go to work in this context, in  
15 this system.

16 He did that because he wanted to pay his bills. That  
17 should be shared among the creditors on a fair basis.

18 QUESTION: So is the unsecured creditors' additional  
19 income that they -- that they derive from letting this person  
20 stay in business. And you say, you know, that's the deal, by  
21 letting him stay in business, you get more than you otherwise  
22 would.

23 MR. DURKAY: Correct.

24 QUESTION: That's the whole purpose of it. Now, why do  
25 you give that incentive to the unsecured creditors but not

1 give it to the secured creditor?

2 MR. DURKAY: I think Congress said this is how it's  
3 going to work.

4 QUESTION: It would seem to me Congress wants to  
5 preserve the security and -- and wanted to give the secured  
6 creditor a benefit in Chapter 13, just as it gives to  
7 unsecured creditors a benefit. But you're not giving him any  
8 -- any benefit as a secured creditor. You're -- you're  
9 treating him as though the whole thing came to an end, then,  
10 although -- although you don't treat the unsecured creditors  
11 that way.

12 MR. DURKAY: Well, I guess my simple answer, Justice  
13 Scalia, is I don't -- I understand that, but I don't find any  
14 -- anything in 506 that says that one of the things you take a  
15 look at is a -- a premium or a kicker to the secured, for the  
16 privilege of allowing this to happen. The secured has to  
17 allow it to happen.

18 QUESTION: Mr. Durkay, can I interrupt, just to be sure?  
19 I may not understand it right. But I thought that the -- to  
20 the extent that the secured creditor does not realize on the  
21 collateral, he's an unsecured creditor.

22 MR. DURKAY: Correct.

23 QUESTION: So doesn't he get the same participation in  
24 whatever the surplus available for general creditors is as any  
25 other general creditor?

1 MR. DURKAY: Exactly.

2 QUESTION: So he has the same motivation as the general  
3 creditors?

4 MR. DURKAY: And -- and this creditor did a couple of  
5 thousand dollars better than if they had taken the truck and  
6 sold it. I mean that's -- that's the fair principle.

7 Let -- let me advance this one step further, in  
8 connection with the split --

9 QUESTION: But -- but his -- but his secured status is  
10 not at all recognized as giving -- as being given any  
11 preference.

12 MR. DURKAY: It doesn't have a preference, but it has  
13 its own source of payment stream. It has the payment to --

14 QUESTION: Well, I meant -- I meant preference in the  
15 sense of in -- of incentive to go forward with reorganization.

16 MR. DURKAY: I guess --

17 QUESTION: It's rather odd that the secured creditors  
18 are the one class that -- that are not treated any better.

19 MR. DURKAY: As a creditor, they are treated better.  
20 Their collateral isn't treated better. They get the same good  
21 deal that any unsecured creditor gets to participate in the  
22 fruits of the successful reorganization. And, frankly, a  
23 secured creditor's incentive is exactly that. Now, a secured  
24 creditor can still say, even though I made \$2,000 more, I  
25 don't want to do this, because I don't want to have to fool

1 with this, among all these cases. But that's what Congress  
2 said, no, you do have to. That's the difference --

3 QUESTION: Are -- are there other cases which are not  
4 maybe quite so close as the one involving a truck? Suppose  
5 there's a business where the secured property is all -- is all  
6 fixed, is machinery, a small business like a laundromat or  
7 something.

8 MR. DURKAY: Correct.

9 QUESTION: And the -- the foreclosure value of this --  
10 of this is -- when it's taken out is very, very low, because  
11 the machinery is ripped out and sold for almost scrap. It  
12 doesn't seem fair that -- that that should be the sole value,  
13 if the option -- the alternative is to keep this business as a  
14 going business, where the -- where, in place, the machinery is  
15 worth much, much more.

16 I think this case is a little distorted because we have  
17 a truck and we're all used to the idea of bluebook values and  
18 so forth.

19 MR. DURKAY: Well, in -- in the case you give, again, if  
20 the laundromat operates, it's going to raise revenue for the  
21 -- the secureds, generally, including the unsecured. That's  
22 why, really, part of the scheme is the bifurcation of claim.  
23 The secured creditor comes in, it's undersecured, and they get  
24 two claims. They have the status as secured creditor --  
25 that's defined one way -- then --

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1           QUESTION: My point was that the range of values is much  
2 more dramatic.

3           MR. DURKAY: Correct.

4           Let me -- let me address that issue specifically, and  
5 Justice Breyer's comments about the discretion of the  
6 bankruptcy judge. There are three key words in 506 that you  
7 can't lose sight of. Those three key words are "in light of."

8           What 506 requires the -- the judge to do is to put the  
9 valuation in a context. It used to be -- this was a very  
10 common practice in the Southern District -- when you first  
11 file a bankruptcy, you'd go in and you'd value everything,  
12 sight unseen, to see what kind of hand you got dealt. Then  
13 you'd start to work your reorganization theory based on the  
14 fixed values that were set down.

15          That's not how you do it. What 506 says, when you  
16 conduct a valuation, put it in context. Why are you getting  
17 this valuation? What do you plan to do with the property?  
18 What are you contemplating? What are the res judicata  
19 effects? What are the collateral estoppel effects? What's  
20 this going to mean in the real world of this bankruptcy?

21          But it says "in light of." It says put it in a context.  
22 There's no mandatory language there. There's -- the judge has  
23 -- has eminent discretion in connection with this factfinding  
24 process to come up with what you're really asking him to do,  
25 which is the common sense answer, in context.

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1 QUESTION: Well, but the -- the judge surely doesn't  
2 just pick a number out of the air.

3 MR. DURKAY: No.

4 QUESTION: Doesn't he listen to witnesses as to --

5 MR. DURKAY: Correct.

6 QUESTION: -- let's -- supposing this -- this weren't a  
7 truck, which is perhaps something we all figure we might have  
8 an idea of what it's worth. Suppose it's a big apartment  
9 building or something like that.

10 MR. DURKAY: Correct. Yeah.

11 QUESTION: Certainly the judge would listen to  
12 witnesses, would he not?

13 MR. DURKAY: Absolutely. And he -- one of the things he  
14 would do is he'd make sure that those witnesses, those  
15 appraisers, knew why the valuation was being conducted --

16 QUESTION: And --

17 MR. DURKAY: -- what was the hearing all about.

18 QUESTION: And don't you think all of the appraisers  
19 would agree that if there had to be a forced sale in 30 days,  
20 the value would be less than if they were allowed a year to  
21 find a buyer?

22 MR. DURKAY: Absolutely. Justice Rehnquist, the  
23 formulation I propose, which is the net proceeds to the  
24 secured creditor on repossession and liquidation of  
25 collateral, doesn't require that you have to consider a forced

1 sale. I -- I don't see why you can't allow the secured  
2 creditor the luxury of coming in and saying, I would do better  
3 than that.

4 In fact, at the trial, that was exactly the Associates'  
5 position. They said, you shouldn't hang us with wholesale  
6 because we can get retail when we sell our collateral. The  
7 only problem was their witness said they couldn't. He said he  
8 saw 15 sales and nobody showed up at 12 at -- of them and he  
9 just said that was company policy.

10 A secured creditor ought to be able to come in and say,  
11 if I hold this property. In fact, there's a very simple way  
12 to do this. I mean what the secured creditor does is he comes  
13 in with a buyer with a commitment. That's good -- that's how  
14 a trustee would do it. He wouldn't say, I think it's worth  
15 this, I think it's worth that. He'd go find a buyer that's  
16 willing to sign up to that.

17 To -- to take a good example -- and the reason why the  
18 United States is here -- and there's some real problems, I  
19 think, with the presence of the United States in this case and  
20 the posture they're taking. Of course, they're here because  
21 of the Taffi case. The Taffi case --

22 QUESTION: The -- the what case?

23 MR. DURKAY: The Taffi case. In -- in the Taffi case,  
24 In re Taffi, which is the Ninth Circuit case that -- that has  
25 come here in connection with this, there was a stipulation

1 presented that the home had a fair market value of 300 and a  
2 forced sale value of 250. And the -- and the first and second  
3 liens were 233,000, and the question then was, what was the  
4 value of the IRS claim.

5 Well, in the first place, as a practical matter, you're  
6 not going to find an appraiser -- you're not going to find an  
7 appraiser willing to give any value to that third lien.  
8 That's so far back in the train, that caboose just doesn't  
9 have value. To give, in the stipulation, any value at all to  
10 the IRS was very generous.

11 But, secondly, and more importantly, in the real world  
12 of bankruptcy, the general way that would be handled is if  
13 you're a third lien and you really think there is equity in  
14 that collateral, you write a check to the first and second and  
15 take the first position. This isn't a -- a formula or a  
16 mathematics. This is real business in the real world.

17 QUESTION: But in -- in that context, assuming, which I  
18 do think this statute is really opaque on this question, you  
19 can make excellent arguments on both sides. So -- so if you  
20 think what Justice Kennedy said, which is that in many  
21 businesses, perhaps small businesses, the creditor doesn't  
22 really expect to repossess and sell?

23 MR. DURKAY: Correct.

24 QUESTION: He -- this repossession is a threat?

25 MR. DURKAY: Correct.

1 QUESTION: And -- and he wants to get the money out of  
2 the person?

3 MR. DURKAY: Correct.

4 QUESTION: And that's -- that's the whole thing. You're  
5 going to lose your refrigerator or whatever. That's a threat.  
6 It's not because it -- so -- so if that's what -- how he's  
7 thinking, then I come back to the possible interpretation that  
8 -- that he should be able to get the money out of the debtor  
9 if there is the money to be gotten and it would otherwise go  
10 to a different creditor. That's where I keep coming up  
11 against -- I don't know why -- what would be wrong with that  
12 part.

13 MR. DURKAY: Justice Breyer, otherwise what you do is  
14 you create a waste.

15 QUESTION: Where is the waste?

16 MR. DURKAY: If you hypothesize an asset, that's the  
17 extra value from reorganizing. And under the Petitioner's  
18 theory, you have to give that extra value to the Petitioner,  
19 which means the 13 never happens, which means that value --

20 QUESTION: Well, you see, that's why I say, at that part  
21 -- at that part, if it's a question between you and the -- you  
22 and the creditor. That's a different question.

23 MR. DURKAY: Correct.

24 QUESTION: And -- and that's why I raise what may be the  
25 dead horse, but -- but I don't want to keep flogging it, but

1 --

2 MR. DURKAY: No, I -- I totally agree with --

3 QUESTION: -- that -- that it would set a ceiling -- it  
4 would set a ceiling on the ground that there is no -- you  
5 know, that the value would be what you would have gotten in  
6 the liquidation, plus any amount that would otherwise go to  
7 the unsecured creditors, up to the retail value.

8 MR. DURKAY: If --

9 QUESTION: It seems to me, Mr. Durkay, that in agreeing  
10 with all of this, you understate the position of the -- of the  
11 secured creditor. It isn't just that he has the -- the power  
12 to get back the distress value of -- of what he's able to  
13 yank, but he is able to say to the -- to the businessman, you  
14 pay me what you owe me or I'm going to close your business  
15 down by taking away the washing machines or whatever you have  
16 that's essential for your business. So the businessman says,  
17 well, I'll pay you first, because you can close me down  
18 entirely.

19 Now, you're setting up a Chapter 13, which deprives him  
20 of that benefit of being able to close the -- the business  
21 down. And yet, at the same time, you're telling this -- this  
22 debtor that he doesn't have to pay him what he would have been  
23 able to -- to extract from him had there not been a Chapter  
24 13.

25 MR. DURKAY: Justice Scalia, I totally agree with you in



1 the way you frame your hypothetical. What puzzles me is what  
2 you've said is what I've said all along, which is the only  
3 reason that the Associates wants this extra value is to have  
4 leverage and power in the transaction. And the one thing the  
5 United States Congress said was, we're not going to play a  
6 power game. The bankruptcy court is going to hand out assets  
7 fairly. And we're not going to accommodate the leverage, the  
8 power, the authority, or the transaction. That's gone.

9 QUESTION: Well, they say -- they say they're not going  
10 to let the -- they're not going to let the -- the secured  
11 party prevent the Chapter 13. But it -- it's the whole  
12 purpose of -- of this discussion to -- to determine whether  
13 they have said, we're going to, moreover, deprive the -- the  
14 secured creditor of -- of the value that he has of -- of  
15 keeping the business a going concern, so that he can get his  
16 money out.

17 MR. DURKAY: That isn't value in an appraisal sense.  
18 That's power and it's leverage. Right off the bat, when a  
19 bankruptcy is filed, that secured creditor is told, hands off,  
20 you're stayed. That power and leverage is gone until the  
21 court says otherwise. And as long as you can extract the  
22 economic value of your loss, your depreciation, over time,  
23 adequate protection, that stay is going to stay in effect.  
24 This is a -- this is a debtor remedial statute.

25 QUESTION: May I ask you a question that was prompted by

1 the example you gave earlier. Supposing in this case, just as  
2 the bankruptcy judge was about to rule, the creditor, the  
3 secured creditor, got a buyer, somebody who was interested in  
4 antique Kenworth trucks or something.

5 MR. DURKAY: Correct.

6 QUESTION: Came in with a buyer, who made him a 40 --  
7 \$48,000 offer, higher than any of the appraisals. Could he  
8 have insisted on that valuation?

9 MR. DURKAY: Oh, if he brought that evidence before the  
10 judge, I think a judge would be hard pressed not to give that  
11 evidence -- hard, fast, factual evidence -- full value. You  
12 know, really, what we're talking about --

13 QUESTION: So that if the -- if the creditor could  
14 establish that he could get a premium value for the truck, and  
15 if he -- if they actually repossessed and sold it, you'd say  
16 they'd be entitled to that?

17 MR. DURKAY: If you want to take that position, you  
18 better bring in some good evidence, though. That's the --  
19 that's the only point.

20 QUESTION: Yeah, I understand.

21 MR. DURKAY: Now --

22 QUESTION: You -- you can't have a phony --

23 QUESTION: -- it flips the other way around. Suppose  
24 you've got a -- a pharmacy and they're -- they're going to be  
25 delivering pharmaceuticals. And the owner of the pharmacy

1 insists on using a 1954 antique Mustang instead of a Hyundai.  
2 And -- and he says, well, according to the standard advanced  
3 by the Associates, I'm entitled to value that collateral at  
4 what it would cost me to replace that car, which is a Hyundai.  
5 That doesn't make any sense. A '54 Mustang is worth real  
6 money. A judge is not going to pay any attention to that.

7 Now, this isn't mechanical. I mean it's --

8 QUESTION: They didn't make Mustangs till '63.

9 MR. DURKAY: Sorry, Justice.

10 (Laughter.)

11 MR. DURKAY: Well, Justice Rehnquist, now you have to  
12 admit, under those circumstances, that '54 Mustang is now  
13 mighty valuable.

14 (Laughter.)

15 QUESTION: Mr. Durkay, what is your explanation -- I  
16 think this -- to my mind, the strongest argument for  
17 Petitioners here is -- is the language "in light of the  
18 proposed disposition or use of such property." What is your  
19 explanation of that language? If it does not mean in light of  
20 the fact that this property is going to be continued to be  
21 used in this case by the debtor and therefore has a going -- a  
22 going concern value?

23 MR. DURKAY: The strong position I took with the Fifth  
24 Circuit that's embodied in the King opinion is that it is a  
25 genuine non sequitur to say that simply because the debtor

1 proposes to retain the value -- the property -- in and of  
2 itself, it suddenly has an inherently enhanced value. You  
3 have to think about those issues, but it doesn't automatically  
4 follow that that means that number changes.

5 But let -- let me add this point if I can.

6 QUESTION: May I ask you about --

7 MR. DURKAY: Yes.

8 QUESTION: Well, wait. That isn't the question I asked.  
9 You haven't answered my question. You're -- you're arguing it  
10 on the merit. What is your -- what is your -- you say it  
11 doesn't mean that -- that language doesn't mean that. What  
12 does it mean, "in light of the proposed disposition or use"?  
13 What does it refer to --

14 MR. DURKAY: In this --

15 QUESTION: -- if it doesn't refer to precisely this?

16 MR. DURKAY: In connection with a 1989 Kenworth in a  
17 Chapter 13, those words may not give you a lot of answers. In  
18 some bankruptcies involving some kinds of properties and some  
19 kinds of proceedings, they may be totally dispositive of the  
20 issue.

21 QUESTION: Give me an example.

22 MR. DURKAY: The trustee comes in and says, I want to  
23 sell the Kenworth. It's a Chapter 7 now. And the reason I  
24 want to sell it is I think I can get \$50,000 for it at  
25 auction. And that's equity above and beyond what the

1 Associates claims their first lien is. And for my first  
2 witness I'm going to call a fellow and he's going to come in  
3 and he's going to give an income valuation of that truck that  
4 says it's worth \$50,000.

5 The judge would say, wait a minute, you're proposing to  
6 auction this property. What are you going to get at auction?  
7 I don't want to hear about what somebody says it's worth on an  
8 income approach. You're saying, I'm going to auction it;  
9 what's the auction value? That's the proposed user  
10 disposition.

11 And under those circumstances, that language gives you a  
12 little bit of information. Remember how much ground 506 has  
13 to cover. I mean it has to cover every imaginable type of  
14 property and every proceeding and bankruptcy, and that's a lot  
15 of ground.

16 You know, if you read 506, and you sit it next to the  
17 Canons of Ethics of the Uniform Standards of Professional  
18 Appraisal Practice that tell you what an appraiser needs to  
19 know before conducting an appraisal, the language is  
20 remarkably similar. It's remarkably similar.

21 What both are saying is, do this in the real world, in  
22 context. No hypotheticals, no theoreticals. Let the  
23 appraisers know everything there is to know. Give accurate,  
24 honest answers. Judge, take all the proper context into  
25 consideration before you make your determination. Don't do



1 any blind appraisals. And if you do that, and when you do  
2 that, we will generally leave that alone.

3 QUESTION: Well, are you suggesting that in the  
4 hypothetical that Justice Kennedy gave, where you've got a  
5 laundromat and the forced sale would be almost zero, but the  
6 income-generating value of the property would be significant,  
7 that there you would use some kind of a -- a cash flow  
8 valuation?

9 MR. DURKAY: You might be able to do that. Correct. If  
10 -- if an appraiser were able to provide that kind of analysis,  
11 that may well be acceptable. But under this scenario --

12 QUESTION: But why not here?

13 MR. DURKAY: -- if I can --

14 QUESTION: Why not here? If there, why not here?

15 MR. DURKAY: Well, because in the scenario that Justice  
16 Kennedy gave, what could happen is that secured creditor could  
17 find somebody to come in and buy the laundromat, lock, stock  
18 and barrel -- buy the business. And he would get the cash  
19 flow. He'd come in and start operating it.

20 I mean you're going to have to have some good evidence  
21 on this, but that's at least theoretically possible. In the  
22 case of a truck, there's no going-concern value for a truck.  
23 The truck is a truck is a truck.

24 QUESTION: And that's the only -- the only situation in  
25 which you would -- you would answer Justice Kennedy's

1     hypothetical by saying, we would give it going-concern value  
2     -- only if you could show that -- that he could sell it to  
3     somebody else -- the whole concern?

4             MR. DURKAY: Yes. I can't say it's the only -- but,  
5     yes. I mean that's really the likely alternative scenario.

6             QUESTION: But --

7             MR. DURKAY: Some -- somebody would come in and buy the  
8     laundromat.

9             QUESTION: If he's willing to stay there and operate it  
10    himself, but there's nobody else in this little town willing  
11    to buy it, then all the secured creditor gets is the scrap  
12    value of these machines?

13            MR. DURKAY: And the secured creditor gets all the cash  
14    flow from the operation of the laundromat, because he's  
15    probably the major unsecured. Remember, he's got that backup  
16    position.

17            Now, one thing, also, to do with 506 that I think is  
18    important, don't use 506 to judge the quality of the  
19    bankruptcy. There are a lot of other provisions in the  
20    Bankruptcy Code the judge can use, such as the good-faith  
21    provisions, the liquidation analysis, et cetera, that are  
22    going to make sure that these are good bankruptcies, that  
23    they're not bad deals, they're not bad outcomes. They don't  
24    really harm creditors unnecessarily.

25            506 is one component. If you get a scenario that says,

1 well, I really don't like the way this spins down, in terms of  
2 what the bankruptcy looks like -- I mean remember that you've  
3 got a common sense judge watching that and saying, well, that  
4 still doesn't mean you're going to get your bankruptcy. Even  
5 if you get your 506 evidence proved, you don't automatically  
6 have a confirmation of your plan.

7 QUESTION: Mr. Durkay, could you explain to me, since  
8 you put it to Judge King, why she thought that it was  
9 irrational to make a distinction about the result that you get  
10 -- now, looking to 1325 -- whether you use (b) or (c) -- that  
11 the value should be the same?

12 MR. DURKAY: 1325 (b) and (c) handle the dynamics of the  
13 bankruptcy. They don't really answer the question of what the  
14 property is worth.

15 QUESTION: But she thought --

16 MR. DURKAY: In order to --

17 QUESTION: -- that it would be an unseemly difference to  
18 have, when the debtor surrenders the property, one value --

19 MR. DURKAY: Correct.

20 QUESTION: -- and when the -- the debtor keeps the  
21 property, a much higher value.

22 MR. DURKAY: The simple formula I used here is I just  
23 don't think you can say that when Mr. Rash told the Associates  
24 he wanted to keep the truck, poof, it was suddenly now more  
25 valuable. I -- I just think it's as simple as that. It's the

1 same truck.

2 You know, the comment that was made in en banc was,  
3 well, what about the going-concern value? Trucks don't have  
4 going-concern value. The -- trucks have a ready market. You  
5 know what they're worth. You can find the market. It's very  
6 easy to determine what that truck is worth, what it can be  
7 bought and sold for.

8 You know, if you look, for example, at the Petitioner's  
9 reply brief, in discussing BFP and this issue, they toggle  
10 back and forth -- here -- what I'm talking about is -- is page  
11 14, 15 and 16. They say that the value should be based on  
12 what the debtor would have to pay -- quoting BFP -- which is  
13 if offered for sale. Then they say at the top of 15 that it  
14 has to be sold within the time and manner. Then they go on  
15 down and say, to determine the price it's paid for.

16 In other words, they're toggling back and forth between  
17 paid and -- and bought. Get on -- get in the boat or get on  
18 the shore. I mean you can't flip back and forth between what  
19 the buy price is and what the sale price is in the retail  
20 context.

21 QUESTION: You -- you say that a truck doesn't have a  
22 going-concern value, but that really wasn't what was at issue  
23 here, was it? It was a truck by an owner who had a long-term  
24 contractual relationship with -- what, was it Lane, the -- the  
25 -- the --

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1 MR. DURKAY: Correct.

2 QUESTION: -- the trucking concern. So that we -- we  
3 have something more than a truck here. And why, therefore,  
4 isn't it fair, even on your premise, to say there -- there  
5 would be a going-concern value here?

6 MR. DURKAY: He -- he wasn't renting his truck on a  
7 long-term basis. Every day he showed up and hauled, he got  
8 paid. If he didn't, he didn't. And a part of that activity  
9 --

10 QUESTION: Yeah, but I -- I -- I'm --

11 MR. DURKAY: It wasn't --

12 QUESTION: -- maybe -- maybe I'm making an assumption,  
13 in fact, that is wrong, but I assume that if I were to go out  
14 in the market and buy a truck, and show up in Lane's driveway  
15 tomorrow morning, I would not get the same kind of preference  
16 for business that this individual would.

17 MR. DURKAY: No, you would.

18 QUESTION: Okay. So he's got something that I, as a  
19 buyer on the open market, wouldn't have, and therefore there  
20 at least is a sense in which --

21 MR. DURKAY: No. You -- you would get --

22 QUESTION: -- there's a going concern.

23 MR. DURKAY: You would get the Lane deal.

24 QUESTION: Pardon me?

25 MR. DURKAY: You would get the Lane deal. If you showed



1 up at Lane, you would be able to haul for Lane on the same  
2 basis as Mr. Rash.

3 QUESTION: But Lane believes in equal protection no  
4 matter who shows up?

5 MR. DURKAY: If you can drive --

6 QUESTION: I can't even shift the truck, and he's going  
7 to give me the business?

8 (Laughter.)

9 MR. DURKAY: But, see, that's the point. The value here  
10 is two components. There's the truck and there's the truck  
11 driver.

12 QUESTION: Yeah. And the truck driver is part of the  
13 deal.

14 MR. DURKAY: No, the truck driver wasn't pledged to the  
15 Associates.

16 (Laughter.)

17 MR. DURKAY: That's -- that's a 13th amendment problem.

18 QUESTION: No, but the -- the truck -- the truck driver  
19 is the one who is going to use the truck if he retains it.  
20 And that makes a difference, doesn't it, economically?

21 MR. DURKAY: I don't think it does.

22 QUESTION: Thank you, Mr. Durkay.

23 MR. DURKAY: Thank you, sir.

24 QUESTION: Mr. Phillips, you have 3 minutes remaining.

25 REBUTTAL ARGUMENT OF CARTER G. PHILLIPS

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## ON BEHALF OF THE PETITIONER

MR. PHILLIPS: Thank you, Mr. Chief Justice. I'll try to be short or briefer than that.

I think, ultimately, the case could be disposed of based on, essentially, Justice Scalia's question, which is, you have language that says "proposed disposition or proposed use." And we -- every example he gave talked about auctions, talked about sales. He's got lots of use for the language "proposed disposition," but he has no use for the language "proposed use" in Section 506(a).

And -- and, in fact, if you look in his brief, he doesn't offer up an explanation of what that language is designed to mean. And the only brief on their side is the one amicus brief says that "proposed use" means that you're supposed to use it for farmland in a Chapter 12 proceeding. And it's reasonably clear to me that, to have to stretch that far to find some meaning in this particular language, tells you that their interpretation really eliminates the "proposed use" term.

QUESTION: Of course, "proposed use" doesn't really lead you to "retail value" necessarily. I mean I -- I can see how it doesn't lead you to "wholesale value," but why does it lead you to "retail value"?

MR. PHILLIPS: Well, what -- what it leads you to, ultimately -- and the value we're looking for and the rule we

1 ask for is what it would cost the debtor to purchase the same  
2 property in the open market. And that's the fair market  
3 value.

4 QUESTION: But why isn't that the same as the fair  
5 market value of this truck, as appraised?

6 MR. PHILLIPS: Because the --

7 QUESTION: Or is it? I'm not sure whether or not --

8 MR. PHILLIPS: Well, it -- it is. It's the -- I mean if  
9 he had to go out and buy this truck today, it would have cost  
10 him either 41,000 or --

11 QUESTION: But why is that different from what it can be  
12 sold for if you have fair opportunity to offer it in the  
13 market? Why is there -- I -- I must confess, I should have  
14 asked this in the very beginning -- but why is the fair market  
15 diff -- value -- different, depending on whether you're the  
16 buyer or the seller?

17 MR. PHILLIPS: Because of the differences of what you  
18 can get for it. I mean I realize that's tautological, but I  
19 mean --

20 QUESTION: But you're saying there are two different  
21 markets.

22 MR. PHILLIPS: Yes, exactly.

23 QUESTION: Yeah.

24 MR. PHILLIPS: It's the market that -- that determines  
25 it.

1           QUESTION: Well, I would have thought the difference  
2 might be what you have to pay somebody, by way of a  
3 commission, to sell it for you. I mean if the debtor is going  
4 to keep it, it isn't going to be sold. But if the creditor is  
5 going to take it back and sell it, they're going to have to  
6 pay something to somebody to do that, in effect --

7           MR. PHILLIPS: That's true. And --

8           QUESTION: -- typically. And I thought that was the  
9 real difference.

10          MR. PHILLIPS: Right.

11          QUESTION: Maybe I'm wrong.

12          MR. PHILLIPS: No, I think that's right. And that --  
13 that plays out particularly in the hypothetical foreclosure  
14 cases, where you have a foreclosure on the house and you --  
15 and you --

16          QUESTION: Yeah, but that -- that assumption means if  
17 you keep the truck, you save the commission.

18          QUESTION: Yeah.

19          QUESTION: So that would be the cheaper value.

20          MR. PHILLIPS: Well, except if -- if you keep the truck,  
21 he wouldn't save the commission, because he -- they would ask  
22 you to deduct the hypothetical cost of the commission. And  
23 that's -- and that -- and there are some decisions to that  
24 effect. But I -- as -- for reasons I think I've made clear, I  
25 think those decisions are wrong.

1           If there are no other questions, I would urge the Court  
2   to --

3           CHIEF JUSTICE REHNQUIST: Thank you, Mr. Phillips.

4           The case is submitted.

5           (Whereupon, at 12:03 p.m., the case in the  
6   above-entitled matter was submitted.)



## CERTIFICATION

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BY Don Neri Federico

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