OFFICIAL TRANSCRIPT

PROCEEDINGS BEFORE

THE SUPREME COURT

OF THE

UNITED STATES

CAPTION: BANK OF AMERICA NATIONAL TRUST AND SAVINGS ASSOCIATION, Petitioner v. 203 NORTH LASALLE STREET PARTNERSHIP.

CASE NO: 97-1418 C-2

PLACE: Washington, D.C.

DATE: Monday, November 2, 1998

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IN THE SUPREME COURT OF THE UNITED STATES

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BANK OF AMERICA NATIONAL TRUST :
AND SAVINGS ASSOCIATION, :
Petitioner :
v. : No. 97-1418
203 NORTH LASALLE STREET :
PARTNERSHIP. :

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Washington, D.C.

Monday, November 2, 1998

The above-entitled matter came on for oral argument before the Supreme Court of the United States at 11:00 a.m.

APPEARANCES:

ROY T. ENGLERT, JR., ESQ., Washington, D.C.; on behalf of the Petitioner.

PATRICIA A. MILLETT, ESQ., Assistant to the Solicitor General, Department of Justice, Washington, D.C.; for United States, as amicus curiae, supporting Petitioner.

RICHARD M. BENDIX, JR., ESQ., Chicago, IL., on behalf of Respondent.

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P R O C E E D I N G S

(11:00 a.m.)

CHIEF JUSTICE REHNQUIST: We'll hear argument next in Number 97-1418, Bank of America National Trust and Savings v. 203 North LaSalle Street.

Mr. Englert.

ORAL ARGUMENT OF ROY T. ENGLERT, JR.

ON BEHALF OF THE PETITIONER

MR. ENGLERT: Mr. Chief Justice, and may it please the Court:

Bank of America lent 203 North LaSalle Street Partnership $92 million. The loan was secured by 15 floors of an office building in the Loop, in Chicago. Outside of bankruptcy, the bank would have been entitled to be repaid $93 million in January of 1995, or to foreclose on the real estate.

In the bankruptcy proceeding that the Court is reviewing today, the bank was denied the right to foreclose. Its right to receive a $93 million repayment in January 1995 was converted into a right to receive $60 million worth, present value, of payments over a period extending to the year 2005. Ownership of the real estate was left in the hands of 203 North LaSalle Street Partnership, despite its default on the loan, in exchange for a promise to contribute $4.1 million net present value

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of new value into the estate over 5 years.

QUESTION: May I ask just a -- I'm a little fuzzy on the facts. It retained the same part -- it was the same owners as before?

MR. ENGLERT: It's the same partnership. It's been reconstituted with the percentage ownerships changing.

QUESTION: It's reconstituted with the -- some partners contributed and some did not; is that right?

MR. ENGLERT: That's correct, Your Honor. Some partners exercised their option; some did not.

QUESTION: So that it's actually a different group of individuals than it was before?

MR. ENGLERT: It is a --

QUESTION: If it's a different partnership, in effect, do they have different partners?

MR. ENGLERT: It is the reorganized debtor. It was not reconstituted as a separate partnership, but as a reorganized debtor.

QUESTION: Are there any individuals in the new partnership that were not in the former one?

MR. ENGLERT: I don't know the answer to that question, Your Honor.

QUESTION: Well, the new partnership still preserved the tax shelter, right? I mean the -- the whole

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problem here was that if there is a default which constitutes a sale, there's -- there's this enormous tax bill to be paid.

MR. ENGLERT: That's correct, Your Honor. Certainly the owners of the equity are mostly old equity owners. They may be all old equity owners. I'm just not sure whether anybody new came in. But the main purpose of this plan was to save the individual partners from suffering tax losses on transfer of ownership.

QUESTION: What if the plan here had let any creditor participate if it wanted to --

MR. ENGLERT: That would be a very different case, Your Honor.

QUESTION: -- in the reorganization?

MR. ENGLERT: That would be a very different case.

QUESTION: Would that have satisfied the claim here and overcome the so-called absolute priority rule?

MR. ENGLERT: It might well have. The key statutory phrase, Your Honor, is that the -- is that the junior interest holders may not receive or retain under the plan, on account of such junior claim or interest, any property.

QUESTION: And what section is that, Mr. Englert?

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MR. ENGLERT: It's section 1129(b)(2)(B)(ii) of the Bankruptcy Code. It's on page 2(a) of the appendix to our brief.

QUESTION: Could I ask you a quick preliminary question just to test my knowledge. Why, in this case, since your clients are owed I guess tens of millions of dollars, isn't it --

MR. ENGLERT: The claim of our client -- of my client?

QUESTION: Yeah. The -- the -- the creditor is owed tens of millions of dollars, the main creditor.

MR. ENGLERT: The creditor is owed $93 million.

QUESTION: Right. And -- and the -- the -- the only other class are a group of people who are owed like $50,000.

MR. ENGLERT: The trade creditors had claims of $90,000.

QUESTION: All right, 90,000. So why wouldn't the major creditor just have paid them their $90,000? Am I right, that if -- if your client had just said, I'll write a check for $90,000, you get the money, at that point you would have been the only one left.

MR. ENGLERT: Correct.

QUESTION: And then there would have been no doubt they couldn't do this.

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MR. ENGLERT: Well, I agree with you, Your Honor. But the Seventh Circuit certainly thought otherwise.

QUESTION: No, no, no. Suppose you -- they would have thought -- if you were the only creditor left, if there was only one class of creditor, because you had paid off the other ones, then is there any doubt that you could have objected to a cram down plan or not?

MR. ENGLERT: Well, Your Honor, if I --

QUESTION: Can they cram down a plan if there is one -- the only creditor is the one who is being sort of crammed down, so to speak?

MR. ENGLERT: We -- we can object. We did object. The -- the provision that makes the unsecured creditors important is Section 1190 -- 1129(a)(10), which requires the assent to the plan of at least one impaired class. And keeping the trade creditors in the plan not to be paid in full in -- in the case -- not paid in full -- was important to the debtor. We can't take them out of the bankruptcy case just --

QUESTION: Why can't you just pay them? If you write a check, don't they disappear?

MR. ENGLERT: We can -- we can purchase their claims.

QUESTION: Yeah. Well, is this a test case, in

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other words? Is this some kind of test case? Or is there some good economic reason why you couldn't have written a check for 90,000, gotten rid of them, and then won?

MR. ENGLERT: We -- the debtor got to them first. The debtor paid them in full.

Justice O'Connor, in response to your question, the key phrase here is -- is "on account of." And if they had not been granted property on account of their pre-petition equity interest, this would be a vastly different case. They were granted two forms of property on account of their pre-petition equity interest. One was the exclusive option to buy equity in the reorganized debtor. An option is itself a property right. Options in publicly traded stocks are bought and sold every day.

Judge Reinhardts opinions in the Ninth Circuit in Bonner Mall, conceded that the --

QUESTION: But that was not under the plan.

MR. ENGLERT: Your Honor, every --

QUESTION: The plan didn't give them the right to buy that option.

MR. ENGLERT: It did, Your Honor.

QUESTION: It did?

MR. ENGLERT: It did. The plan doesn't give anybody anything until a bankruptcy judge confirms it. So, under the plan, has to mean what happens when this

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plan is confirmed. And it was the plan that excluded anyone other than the pre-petition equity holders from having the option to buy equity in the reorganized debtor.

It's also the plan that gives the pre-petition equity holders the equity interest in the reorganized debtor on account of being pre-petition equity holders. In other words, on account of their prior claim or interest.

QUESTION: Are you saying that if an equity owner is ever to be allowed to contribute new value, that that must be made available on the same terms and conditions to all -- to the -- to all persons?

MR. ENGLERT: Not quite, Your Honor. If they're ever to be allowed to contribute new value over the objections of a class of impaired creditors, then yes, we -- our position is that the -- the opportunity to buy the equity for new value must be distributed equally.

But the real-world way that new value plans get confirmed all the time is through creditor consent. And that's what Congress intended. It didn't intend judges to cram down new value plans. It intended negotiation among the parties to allocate any going concern surplus. The legislative history says that explicitly -- page 224 of the House report.

This Court --

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QUESTION: Yes. But if you always had creditor consent, would you ever have a cram-down?

MR. ENGLERT: There are many cram-downs, Your Honor, in many kinds of cases. We're dealing here with a single asset real estate case, where there are, as Justice Breyer's question points out, essentially two real parties in interest. The typical bankruptcy case is not a single asset real estate case. It has multifaceted parties --

QUESTION: Right.

MR. ENGLERT: -- with multifaceted interests, and cram-down is often necessary.

QUESTION: But isn't it -- is it not a given in every cram-down that some senior creditor objected?

MR. ENGLERT: You don't reach 1129(b) unless there is an objection by a class of creditors --

QUESTION: But is it not also true that whenever a cram-down is approved, some objector has been not paid in full?

MR. ENGLERT: That's also correct, Your Honor, yes.

QUESTION: Okay.

MR. ENGLERT: But the absolute priority rule says that you go in absolute priority, that you see if the people who are not being paid in full are more senior than junior people who are receiving or retaining property.

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And if they are, the plan violates the absolute priority rule.

QUESTION: So there could never be a cram-down unless equity owners and non-equity owners are treated on an equal basis so far as new value participation?

MR. ENGLERT: Yes, Your Honor. Because, otherwise, the equity owners are receiving something on account of their junior claim or interest. Which is exactly what 1129(b)(2)(B)(ii) prohibits.

Now, it's our position that the statutory language is dispositive here. But the legislative history is also legislative history is also extremely helpful to the bank.

QUESTION: Before you get to the legislative history, would you just answer -- make sure you've answered one question. Would your position -- is your reading of the statute the same as if the words "on account of" were deleted from the statute?

MR. ENGLERT: Absolutely not, Your Honor.

QUESTION: And tell me what the difference is.

MR. ENGLERT: In a typical bankruptcy case, especially involving a small business, the debtors' pre-petition equity holders will often have lent money to the business in the form of debt and not equity. If we excise the phrase "on account of" from the statute, those

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people could not receive or retain anything on account of their debt, as well as being unable to receive anything on account of their -- on account of their equity interest.

That would be a radically different world than the world we have under Section 1129(b)(2)(B)(ii). In addition, as Justice O'Connor --

QUESTION: But if you -- if you deal only with the cases where everybody is only a member of one class, you say there are some people who are members both debtors and equity holders.

MR. ENGLERT: Yes.

QUESTION: But if everybody just was -- only fit in one class and you don't have membership in more than one class, then would the statute mean exactly the same thing whether the words "on account of" were included or deleted?

MR. ENGLERT: No, it would not, Your Honor. That raises the -- the questions of bidding for the equity. If the words "on account of" were deleted, the debtor could not bid against the bank for the equity. Because the words "on account of" are in there, if someone wanted to hold an open auction for the equity in which the -- the debtor bid, or the debtor's pre-petition equity holders bid, and the bank bid as well, then whoever won that auction would be receiving the equity on account of

having the highest bid and not on account of the pre-petition equity interest.

That's why the words "on account of" have a role to play in addition to their role of allowing people to be paid on their debt claim.

QUESTION: So you're concerned only with cases in which the equity position is not the highest bidder?

MR. ENGLERT: Well, here there was a one-horse bid, a one-horse -- a one --

QUESTION: No. But presumably, if somebody had come in with more money and told -- and somebody advised the bankruptcy judge -- that you can get more money by somebody else is going to put into the operation, presumably the judge wouldn't have approved the plan.

MR. ENGLERT: Oh, no, he would have approved the plan. Because we were prepared to say we'll put in more money, and he approved the plan anyway. He said, I'm not terminating exclusivity. You can't do that. I'm going with the debtor's plan.

QUESTION: Can you elaborate a bit on this open auction, which we don't even know whether this is already the order, but you did answer the one-horse race, to say no, of course there would be a two-horse race, and the bank would always have the stronger horse, because it could pay -- it could -- I forgot what footnote it was in

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which you explained that, but --

MR. ENGLERT: The bank wouldn't always have the stronger horse, but the bank would always be in the race. Because there is a point at which they could outbid us, on the facts of this case. There comes a point at which they could outbid us for the equity in this property. It's in our best interest to maximize the value of the estate. And if their bid for the new equity is so high that we think we're really going to get more money out of their plan than out of foreclosure, then they can win the auction with our blessing.

But we think this property is worth a lot more than what we're going to get under this confirmed plan. And up to the point where they have satisfied us that they're going to make us better off, we will continue to outbid them, bidding our deficiency claim -- or bidding cash, because we get it back on a deficiency claim -- so that -- so that we can win the auction. And -- and in many cases, if banks -- if senior unsecured creditors, or senior secured creditors with unsecured deficiency claims, are allowed to bid, that's how the auction will work.

Now -- now, let me add, to the best of my knowledge, no debtor and no creditor has ever proposed an auction as the way to get around Section 1129(b)(2)(B)(ii). Only bankruptcy judges have ever

proposed that as a creative solution. Debtors don't like it because they want exclusivity. Exclusivity matters a very great deal to them, to be able to keep the property. And creditors don't like it because they don't want to go through the nonsense of an auction. They just want to have the absolute priority rule applied as it's written.

QUESTION: Suppose the court had said that the bank could contribute dollar for dollar with the equity holders and receive a proportionate share of the equity.

MR. ENGLERT: That --

QUESTION: Not, not quite exclusivity. We'll say we'll -- we'll allow the bank to participate on the same terms as the --

MR. ENGLERT: That would clearly violate the statute. No question it would violate the statute.

QUESTION: Because?

MR. ENGLERT: Because they are receiving something - the right to the 50 percent equity interest -- on account of their junior claims of interest.

QUESTION: Well, but you're getting the same -- the same deal, and you're not receiving it on account of your prior equity interest.

MR. ENGLERT: No, but --

QUESTION: So how can that be?

MR. ENGLERT: The statute doesn't ask whether we

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get anything on account of our junior claim or interest because we're the objecting impaired class.

QUESTION: Well, but I -- I -- I'm not so sure. If -- if they have the right and you have the right, then it's not just because of their -- of their position.

MR. ENGLERT: It's -- it's not just because of their position. But it's because of their position. It's on account of their position. And that's the question the statute asks.

QUESTION: Well, that would be the case if you had an auction in which only the -- only the debtors and creditors were allowed to participate in.

MR. ENGLERT: I agree, Justice Scalia.

QUESTION: You -- you have to let John Doe walk in off the street and participate in that.

MR. ENGLERT: I agree. And that would delight the bank, because that's the way we're going to maximize the value of the estate, which is what we want.

QUESTION: Is it -- suppose that -- not this case -- but imagine a case in which a large, under-secured creditor has, let's say, $50 million of unsecured debt. And it's a company that has a lot of employees. And the bankruptcy judge thinks, I wish this company could survive, because it would be good for the community, the employees. But if this unsecured creditor gets it, he's

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going to sell it for scrap, basically. So I think I see new capital coming in here. And I would like, even though that unsecured creditor objects, to make this go forward.

Under your view of the case, would that be possible? Is it ever possible on their view of the case? Is it -- what's the status of that?

MR. ENGLERT: Under our view of the case, it is never possible for him to say for that reason, I'm going to choose to allow the equity holders to retain the equity without some sort of competitive bidding.

QUESTION: Well, he could have a competitive bid but exclude the big creditor from that. I mean that's logically possible. He could say, we're going to have a competitive bid but a competitive bid among people who want to keep the company in business.

MR. ENGLERT: Sure. Sure.

QUESTION: Is that possible legally?

MR. ENGLERT: That's a clear violation of the statutory language. Because, at that point, there's absolutely no secret what's going on. He is trying to favor the prior equity holders as such. He is trying to --

QUESTION: No. No. My -- my theory -- my hypothetical is that there are 500,000 people in the world who will put in $6 million of new capital. And he's

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indifferent, among all those 500,000, but one. The one he doesn't want is your equivalent. Now, can he do that?

MR. ENGLERT: No.

QUESTION: Because?

MR. ENGLERT: He cannot do that because he is still giving equity a preferred position. He is not excluding equity from the auction, whereas he is excluding the debtor -- the creditor, excuse me -- from the auction. And he is still giving the junior interest holders something on account of their claim.

But let me add, Justice Breyer, in response to your -- to your question, that's a very unworldly scenario for this reason. A bank that thinks there is more money to be gained for its claim by letting someone else come in and bid on the equity, but nevertheless can insist on its pound of flesh and says, we're going to sell this for scrap, is acting irrational.

QUESTION: Mr. Englert, you said that -- that your client, the bank, put in a competing plan, but that that was rejected.

MR. ENGLERT: We asked for permission to put in a completing -- a competing plan.

QUESTION: Oh. But you actually didn't file anything?

MR. ENGLERT: We did tender a competing plan,

but it was not -- we were not allowed to file it because of the statutory exclusivity of 1121(c).

QUESTION: How did it compare, the plan that you tendered, with the one that the mortgagee tendered in the Coltex case? Was it similar or you don't know?

MR. ENGLERT: I have forgotten the facts of the alternate plan in the Coltex case. But our plan in this case was a plan of liquidation. Because that is how we believe that the estate -- the value of this estate will be maximized.

I'd like to reserve the balance of my time for rebuttal.

QUESTION: Very well, Mr. Englert.

Ms. Millett.

ORAL ARGUMENT OF PATRICIA A. MILLETT

FOR UNITED STATES, AS AMICUS CURIAE,

SUPPORTING PETITIONER

MS. MILLETT: Mr. Chief Justice, and may it please the Court:

Because Respondents concede that they received property under this reorganization plan, the only question presented under the governing text of the absolute priority rule is whether they received that property, quote, on account of their prior equity interest. We believe they did for two reasons.

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First, the ordinary meaning of the phrase "on account of" requires an inquiry into causation. The absolute priority rule, thus, asks whether there is a causal nexus between the prior junior equity interest and the retentions of property. That causal nexus is clearly present in this case. Under the reorganization plan, the junior partner -- the junior interests, the partners, and only those partners, were allowed to receive interest in the reorganized debtor.

Now, Justice Scalia, you asked about whether that was in fact an option under the plan. And under -- under section 5.2 of the plan, which is at the Joint Appendix, pages 38 through 39, section 4.5(d), which is also at Joint Appendix, page 38, it says clearly that the decision whether or not to make a payment to purchase this new equity interest will be made 2 business days after confirmation of the plan. And then, the default provision of the plan, section 6.1, which is Joint Appendix, page 46, says what will happen if the contributions aren't made.

This previous position -- previous provisions that I cited also address what happens to people who do not exercise the options. So we think that's clearly under the plan.

And, in addition, it's important to understand

what the concept of the under plan means. It's -- it's much like under -- under law, the authority -- there was no authority to have this option or to acquire interest without a plan. So we believe it was clearly under the plan.

Under the plan, no one -- no one else could acquire these ownership interests. Thus, there was a 100 percent certain -- certainty, excuse me -- that partners, because they were partners, because they had junior interests --

QUESTION: But -- but let me just interrupt there. Some partners did acquire an interest. Some did not. Those that acquired it put in some cash. And on account of the fact they put in the cash, they got an interest. Those that did not put in cash did not get an interest. Now, why -- I don't see that it's because they were partners that they got the interest. It's, rather, because they put in the cash.

MS. MILLETT: Well, this Court has recognized that you can have more than one cause for an event. We don't dispute that money was an additional requirement. But money alone was not enough. The bank would have liked to put in money and was ready to put in money, but that was not enough. The status as a junior equity holder, as a partner, was a necessary and indispensable cause to

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acquiring this interest. And --

QUESTION: And does the record show the bank was prepared to put in new money that would not have been just used to retire their own debt in a larger amount than -- than these people were?

MS. MILLETT: I believe -- I believe so. I'm not -- we have not seen the copy of the bank's plan --

QUESTION: I'm just asking whether the record shows whether they would or not. You don't know? If you don't --

MS. MILLETT: I'm sorry, I don't know that.

QUESTION: The bank's plan was a liquidation plan, I thought.

MS. MILLETT: A liquidation plan, that's correct.

QUESTION: Yeah. Right.

QUESTION: Well, at any rate, under this plan, nobody else had the opportunity to put up any money than the people who finally put it up; isn't that correct?

MS. MILLETT: That's absolutely right. And so there was a 100 percent certainty that partners and only partners, because they were partners, would end up in possession of this property. We think that falls within the plain language of --

QUESTION: Well, but -- but let me just -- maybe

it's just that I don't have enough familiarity with reorganization positions -- but what if a stranger came in, not seeking liquidation, as I gather the -- the -- you suggest the bank's plan was, but offering more new money into the plan, and that was known to the bankruptcy judge, and more money available from others. Is there anything to indicate the judge would have thought this plan fair and equitable?

MS. MILLETT: Well, first of all, it's not totally clear --

QUESTION: See, I -- the way I understood the case -- maybe I'm wrong -- I understood the fact that these people have a huge tax loss that makes them willing to put in more new money than anybody else around. And therefore they are, almost by definition, the highest bidder available for this property that would put in new money. Now, is that an incorrect understanding of the facts?

MS. MILLETT: I think we don't know yet, because there was no competition. We don't know.

QUESTION: But if there were -- I mean was there anything to prevent a stranger from coming in with more money and letting the -- you know, making an offer to the creditors and so forth, and that would be known by the judge, and the judge then would say, well, I'm not going

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to approve this plan because there's more money available from outsiders?

MS. MILLETT: Well, a couple -- a couple of things. First of all, there was an exclusive -- we're -- we're -- this all occurred within the period of -- of exclusivity. Which means --

QUESTION: Well, I understand. But in that period --

MS. MILLETT: -- no one else could submit a plan.

QUESTION: -- somebody finds out about this and wants to buy the business and comes in with some money.

MS. MILLETT: Well, under -- under reorganization, you can't just come in off the street and produce a plan. You have to --

QUESTION: No, you have to get a creditor to -- to make your position known to the judge.

MS. MILLETT: You have to have a plan submitted. And then -- and then, as -- as the bank discovered, you have to not only have someone submit a plan, but get the court to agree to lift the period of exclusivity so that that plan can be considered. But had -- I mean the important thing is that -- we have to keep two things in mind on the amount here -- it's conceded that the tax li -- liability that they were trying avoid was up to $20

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million -- and then why a -- a present value of $20 million -- and yet they only had to kick in present value $4 million to preserve that.

Now, I think it's certainly fair to assume that had there been some competition that they would have been willing to go up to 19 or close to $20 million. You have --

QUESTION: But what you're saying is the only thing they would have had to have done to save this would simply have been to open the class beyond the exclusive -- beyond the exclusive condition of prior equity ownership, and then we would have found out whether anybody else would step up to the plate? That's the nub of your argument?

QUESTION: That would have given us some -- some information. But I want to make clear one thing, that even when a number of plans are submitted, the absolute priority rule and the requirements in 1129(b) must be satisfied as to the actual plan that is confirmed. So had 50 different plans been submitted here and the court had still chosen this one, we would still say there was a violation of the absolute priority because this plan is --

QUESTION: Because this one would have had the -- the exclusive condition of prior equity ownership?

MS. MILLETT: Right. Right.

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QUESTION: And -- and so that's why I said, your -- your position, I take it, is that remove that exclusive condition and there's no further problem so far as -- as this provision is concerned?

MS. MILLETT: The exclusive condition on bidding and purchasing?

QUESTION: Yeah. Yeah.

MS. MILLETT: I believe -- I believe -- yes -- in large part, yes. There may be some other circumstances we would need to consider in a particular case, but that is an enormous factor in deciding that this was on account of.

Now, why is this so important, this exclusivity? It's important to understand that --

QUESTION: But before you get on to that, I'm troubled by the fact that this puts this the debtor in -- in a worse position than anybody else. Anybody else could come in and offer, you know, 15 million of new value and be able to proceed with a plan. They could come in and offer 19 million of new value and not be able to proceed with a plan.

MS. MILLETT: Well --

QUESTION: Why does that make sense?

MS. MILLETT: It makes sense, first of all, because the statutory text puts a special restricted

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status on the holders of junior interest. That's the first answer. And -- and there's a good reason for Congress to do that. And it's important to understand that the absolute priority rule is not just about money.

It reflects a historic concern with insider self-dealing at the expense of creditors. And in -- the insiders, the partners here, will have -- will have the, because of the benefits of being debtor in possession and of their position, information that won't be available to others that will allow them to know about the value of the company and take advantage of that.

But in addition, another thing the absolute priority rule does -- remember, we're in a reorganization, where this entity is going to continue, many times in cooperation with its creditors, and the creditors have a right to limit the ability of the equity holders to stay in control of that reorganized debtor. And then to -- especially in a manner that's going to benefit themselves, to set their own price for new equity interests to exclusively and completely take control of the enterprise while forcing a bank, Housing and Urban -- the -- the Department of Housing and Urban Development, or another senior creditor into long-term, unwanted financial relationships solely to benefit the junior interests.

So it's not just a matter of money; it's also --

if -- if -- essentially the absolute priority rule says if you want to stay in control, having presided over the bankruptcy of this entity, you have to either not impair us, pay us in full or make us happy to continue working with you. And that's our view of why they would be uniquely impaired.

QUESTION: Did the government appear in this -- in this proceeding below?

MS. MILLETT: No, we were -- we have not been involved. This is our first appearance --

QUESTION: Could you have -- could the argument have been made that this was for the avoidance of taxes?

MS. MILLETT: There is -- I think you're talking about 1129(c).

QUESTION: Yes.

MS. MILLETT: The argument -- the argument can be made -- it's -- it's admitted that it was to avoid a capital gains tax. The Internal Revenue Service's application of 1129(c) has actually been very, very narrow. And where someone is just avoiding, in a legal and proper manner, a taxable event, then we have not invoked it although the statutory tax arguably might allow that should we change our position. But also it does require that we would have been a party in interest, and we are not a party in interest in this case.

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QUESTION: How does your position differ from the Petitioner's, if it does?

MS. MILLETT: I don't believe in this case that it does -- that -- that it does. I think we are in agreement. Whether in hypotheticals in future cases we would consider something to still be on account of and they wouldn't, I don't really -- it hasn't really been tested by this case. And that's because whatever your definition of causation and whatever your definition of on account of, a 100 percent certainty that junior equities obtains property because they're junior equity will satisfy that.

QUESTION: Thank you, Ms. Millett.

Mr. Bendix, we'll hear from you.

ORAL ARGUMENT OF RICHARD M. BENDIX, JR.

ON BEHALF OF RESPONDENT

MR. BENDIX: Mr. Chief Justice, and may it please the Court:

I want to start by answering a question that -- one or two questions that had been asked earlier in the argument. The bank did propose a plan of reorganization here, or asked to propose a plan of reorganization, which was a plan of liquidation. It's really not correct for the bank to stand up here and say they were proposing to put in money, when their plan was a plan of liquidation

that did not propose to put in $6 million or any lesser sum.

It was a proposed plan of liquidation that was defective on its face because it didn't satisfy the best interest of creditors test. And that's why the court properly denied the bank's motion. The bank could have appealed. It chose not to. And this whole auction argument I think is simply an attempt to --

QUESTION: Whose interest didn't it satisfy, if the only other creditors were the trade -- trade creditors? They got paid in full. The only creditor is the bank, and it gets -- it wants that. So that's one thing that puzzled me. Whose interest could that not have satisfied?

MR. BENDIX: Well, Justice Breyer, if I understand your question, the unsecured class was impaired in this case. Which meant that they were not paid everything that they were entitled to.

QUESTION: Well, who is that?

MR. BENDIX: That was the class of trade creditors.

QUESTION: All right. How much money did they get?

MR. BENDIX: They got the principal amount of their claim. They did not get interest. The correct

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amount is --

QUESTION: So we're talking about like $3,000 or $4,000, is that what that was?

MR. BENDIX: That's correct.

QUESTION: So this is some kind of a test case; is that what -- I take it?

MR. BENDIX: I believe it's a test case, Your Honor.

QUESTION: All right.

MR. BENDIX: And it's important to point out that the amount of claims in a particular class is not relevant to the fair and equitable --

QUESTION: Yes, yes. Your quite right. I just -- then, if we're talking about really not this case but this is a test for many, many other cases --

MR. BENDIX: And I think --

QUESTION: -- what -- what is it wrong with -- with what has been suggested, that the rule simply should be the debtor in possession, when he proposes during that exclusive period his plan, in your kind of a situation, what he should say is we, the past equity holders, will receive equity in return for new value of, let's say, $10 million, provided that anyone but for the principal secured creditor who wants to liquidate -- let's say anyone who doesn't want to liquidate -- puts in more. If

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anyone who doesn't want to liquidate will put in more, then of course we concede; they get the equity, not us.

Now under, what would be -- I'm sure there are things wrong with that, but I -- I ask it because it seems to me that would be consistent with the statute. Whoever ended up with it, including the old holders, wouldn't be getting it because of their prior equity holding. It would keep what you want not to happen not to happen -- liquidation.

MR. BENDIX: The difficulty with that example, Justice Breyer, is that any dilution -- because of the tax laws in this case -- any dilution of the ownership would have basically destroyed the ability to defer the taxation. And it was that ability to defer the taxes, not to avoid taxes, but to defer the capital gain, that ability to defer was the economic incentive for the investors to put money in. If that incentive disappeared, then they would have had no reason or economic motivation to put the money in.

QUESTION: Then you would have lost absolutely nothing by having that condition in, because there would have been no such person to put in more equity.

MR. BENDIX: I don't -- I don't know whether there would be or there would not have been, Your Honor. But it's -- it's important to point out and to understand

what the confirmation process is. Section 1121 of the Bankruptcy Code gives the debtor the exclusive right to file a plan for the first 120 days of a case. That is clearly a valuable right. It's a right to set the agenda, to set the option. It's like -- somewhat like writing the first draft of an opinion.

Congress recognized that's a valuable right. And in fact, the bank, in its amici, recognized it was a valuable right. Because in 1978, when this particular section was being debated, the creditor -- the secured creditor lobby, which is here today, lobbied to do away with debtor exclusivity altogether.

Congress decided not to do that and instead to have a compromise, where the debtor got an exclusive right, for the first 120 days, which could be shortened for cause shown -- if somebody came in and said, I -- here are the following circumstances, and I believe that they -- they demonstrate cause for terminating the exclusive period, the bankruptcy court has discretion.

Once a plan is filed, Section 1123(a)(5) says that the plan must specify the means of implementation. That means a plan has got to say where the money is coming from to make the payments required under the plan. The Code, in various subparagraphs, lists examples of means of implementation. And one of them, in subparagraph (J), is

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the sale of the securities of the debtor for cash or in exchange for claims or other interests.

If Congress had meant to limit the debtor's discretion in what kind of package it was going to put together in an offer to the creditors for a restructuring, it easily could have said so. It could have said you've got to specify means of implementation. You can sell the securities, but if it's the debtor proposing a plan, you must do it by way of auction or you must cut other people in. It simply didn't say that.

What Congress decided was that if creditors or other parties and interests didn't like the plan and, instead of simply objecting to it, wanted to propose a different plan, they had an obligation, under Section 1121(d), I believe, to come in and ask the court to terminate exclusivity. And if the court terminated exclusivity, both plans, if there was a proper disclosure statement, would go out to the creditors. The creditors would vote.

And if both plans were accepted and if both plans met all of the requirements of 1129, then the bankruptcy judge, in 1129(c), is required to decide between those plans, and choose one based on the preferences --

QUESTION: But what, Mr. Bendix, then what is

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your interpretation of the "on account of" language?

MR. BENDIX: My interpretation, Your Honor, is that it means an exchange for or synonyms for that, such as in satisfaction of or in consideration of. And the reason we take this position is that the phrase must be interpreted in the context in which it appears.

We're talking here about corporate reorganizations, companies whose -- unable to meet their obligations and to pay their interest because they don't have enough income, and they make a proposal to creditors to restructure the capital structure. And there are an infinite number of ways that a troubled company can restructure its finances.

You can extend debt. You can turn debt into equity. You can pay a percentage on the dollar. And that's why, because there are so many different ways -- well, let me go back to -- to the "in exchange for." What happens in a --

QUESTION: On account of.

MR. BENDIX: On account of. What happens in a reorganization is that new obligations or property are exchanged. They're given to creditors in satisfaction of their old obligations or in exchange for existing securities. For example, a class of unsecured creditors might get under the plan 50 cents on the dollar. They

receive that not because they are creditors but in satisfaction of their pre-petition claims.

Similarly, a class of equity holders or preferred --

QUESTION: Well, but that really is parsing words rather finely, to say they don't receive it because they're creditors but because of their pre-petition claim. It's their pre-petition claims that makes them creditors.

MR. BENDIX: That's correct, Your Honor. But you also have to consider, first, that we're talking about a -- an economic situation that involves exchange. Second, I think we submit that you have to consider the meaning of "on account of" in relationship to what the absolute priority rule is designed to accomplish.

Everybody -- one of the few things that everybody agrees on in this case is that Section 1129(b)(2)(B)(ii) is the so-called absolute priority rule. This Court has held for more than 100 years that the purpose of that rule is to prevent transfers for less than a fair equivalent value, a transfer, if you will, a fraudulent transfer.

What that means in the context of a reorganization is that a senior class of creditors that has not been paid in full gets first claim on all of the reorganization value of the company. That's all they get.

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That does not mean that somebody can't come in and -- well, let me go back.

If some of that reorganization value is diverted to a junior class of stockholders, for instance, then the senior class of creditors which hasn't been paid in full, hasn't gotten everything that it's entitled to.

QUESTION: I don't -- it seems to me you're going around Robin Hood's barn here. "On account of," you've heard what the -- what the Petitioners argue, that it means -- it means -- it has a causal connection. And do you have a brief response to that?

MR. BENDIX: Yes. Cause has nothing to do with the purpose of the absolute priority rule.

QUESTION: Well, it may not have anything to do with the purpose, but lots of times Congress may have a purpose in mind, but it adopts language that may carry out that purpose, may be broader than the purpose, may be narrower than the purpose. So what do you say "on account of" means?

MR. BENDIX: We say, Your Honor, that it means in exchange for or in satisfaction of. And as a fall-back, as we've said in our briefs, even if you were to take the position that it meant cause -- which I think is irrelevant to the idea of whether you have a fair exchange, which is the purpose of the absolute priority

rule -- even if you said it meant cause, as this Court said 2 years ago in the O'Gilvie case, cause means direct cause.

And it's interesting to note that in the O'Gilvie case, the Solicitor General filed a brief with this Court saying that "on account of," as it appeared in the Internal Revenue Code, did not mean but for a cause, where any sort of remote fact could influence the decision, but meant direct cause. They haven't mentioned that here today.

If you take a causal analysis, then it must mean direct cause. And direct cause is a question of fact, which --

QUESTION: Mr. Bendix, may -- may I ask you a question about the -- the absolute priority rule -- which sounds like, you know, what it says, that the senior creditor has to be paid in full before the next -- and then the case in which -- the case -- case in which Douglas presented this corollary or new value exception. He was talking about necessity to keep a going concern going.

When you think of going concern, a business with goodwill, with employees. Here we have nothing at stake for anybody other than to preserve this leaky tax shelter. So I -- I really don't comprehend how you would even

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satisfy the necessity standard of the new value, if I comprehend Douglas right, that what he had in mind was keeping a going concern going, where there are employees and suppliers and all that.

MR. BENDIX: Chapter 11 encompasses far more than operating businesses. As this Court has held, it encompasses individuals that don't have businesses. It certainly encompasses real estate partnerships. Old Chapter 12, which is real estate partnerships, was intentionally included in Chapter 11.

So the fact that there are no -- there aren't a large number of employees here really is not a reason that you shouldn't apply Chapter 11, and the absolute priority rule in particular.

QUESTION: Yes, but I'm asking, what is that absolute priority rule? And if I think Douglas used the word, in describing it, "necessity," necessity for keeping something going, these are going to be the same tenants, nobody is going to -- I think one of the briefs put it, the only change would be who the managing agent pays the rent to.

MR. BENDIX: The reason why reorganization is good in this case -- if I'm -- if I'm answering your question properly -- is that it allowed creditors to realize on the tax problem that these investors had. The

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creditors got a windfall, got more money, 6 and a half -- or 6 and a quarter million dollars, plus the -- the insiders had $8 million worth of claims, which they waived, and thereby gave up $3 million in cash.

QUESTION: Well, that -- that all depends on how much the property would have sold for. I mean, the reason the bank didn't like it was that they -- they disagreed with that. They thought the property would have sold for a lot more than the 6 million.

MR. BENDIX: They did, Justice Scalia, but they never appealed the bankruptcy court's factual finding that the value of the property was $55.8 million. And it's important to remember in this case that the bankruptcy judge's factual decision was 2.8 percent -- factual valuation -- was 2.8 percent less than the value which the bank's own appraiser gave.

So it really I don't think is proper for the bank to come in here, having not appealed that factual determination, and suggest that the bankruptcy judge made a mistake or to say that because bankruptcy judges may make mistakes that banks should have the right to decide and overrule the vote of other creditors.

QUESTION: In answer to Justice Ginsburg's question, I suppose the going concern value here is postponing the capital gain, really?

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MR. BENDIX: In a real sense, yes, Justice --

QUESTION: Indicated in the economic motivation to keep the business going?

MR. BENDIX: It allowed the creditors to get the benefit of something that the debtor didn't own and didn't have a right to sell. The tax problem was something unique to this group of individuals. It wasn't anything that appeared on the balance sheet of the -- of the company. And -- and because of that, you're correct, that they -- they were able to realize on this thing that the debtor didn't own and couldn't sell.

QUESTION: What would your view be on a case that's similar to this one but with the following difference: You have a plan. You put it forward just like the one you have. What was it, 9 million -- 6 -- I forget -- 6 million you put in?

MR. BENDIX: Six -- $6.125 million.

QUESTION: 6.125. And suppose a creditor says, you know, I -- I have a plausible person over here who will put in 8 million. And he'll put in 8 million if he gets the shares. And the bankruptcy judge says, no, I'm not going to consider that; I'm going to adopt your plan. Suppose those were the facts. Would there be any way to avoid saying, in that case, that the old owners got the equity on account of their prior ownership? Just like

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this case, but we have really someone who comes in and wants the -- wants this --

MR. BENDIX: In that case, the -- the short answer to your question is that the owners are still getting something -- they're getting their interest only on account of the money they put in. The bankruptcy judge -- you're suggesting by your question that perhaps the bankruptcy judge makes a mistake or abuses his discretion in not --

QUESTION: I don't know all those things. I mean there could be complicated cases. But --

MR. BENDIX: But in --

QUESTION: But I'm thinking it's just like this case, but we have a real bidder out there for 8 or 10 million, and he -- and the only reason really the bankruptcy judge is doing it is -- is it then not on account of? And you say no, because --

MR. BENDIX: Well, Justice Breyer, in that case, frankly, if I was a bankruptcy judge, I would terminate the exclusive period and let both plans go out to creditors. The interesting thing about the bank's position is that they say, even if there is competing plans, and even if the debtor's plan, the debtor's new value plan, puts in more money, that somehow the -- the owners have still gotten something on account of their

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prior ownership interest and the debtor's plan couldn't be confirmed without --

QUESTION: But then it seems we're not arguing about very much. Because then all you'd have to do -- even on their theory -- is -- is put a provision in -- maybe not on their theory, but put a provision in and say, we aren't the exclusive ones; we'll let anyone else who wants to keep it going as a going business do it. And -- and it's just a question of that boiler plate. Because if in fact there is such a person, you agree, he should get it?

QUESTION: That would work in all cases except yours, because of the tax problem that -- that you had. You couldn't let other people in. But -- but in the ordinary case, why wouldn't that happen?

MR. BENDIX: I don't know. But the point is that nowhere in the Bankruptcy Code does the word "auction" appear. And it certainly doesn't appear in any of the provisions dealing with what a plan must contain.

QUESTION: No, no. But the virtue of the auction of course is that it gets around this "on account of." Naturally it doesn't appear.

MR. BENDIX: Well --

QUESTION: But where it's an auction, you can't possibly say it's on account of.

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MR. BENDIX: It doesn't appear. And -- and we are trying to interpret the plain language of the statute. It seems anomalous to me to say that, if you're the bank, we're relying on the plain language of 1129(b)(2)(B)(ii), and it clearly says that the only time a plan like this can be confirmed is if you have an auction.

And in fact, in footnote 6, at page 11 of the bank's brief, they concede -- indirectly, but I take it as a concession nevertheless -- that there really isn't a section -- there -- there is nothing in the Bankruptcy Code that permits it. It says it raises many questions about whether you could do it. The fact is there is nothing in the Bankruptcy Code that requires it or --

QUESTION: But, Mr. Bendix, it is -- it is essential, for the preservation of the -- the tax benefit, that you have the -- this exclusivity, that you be the only ones that -- that end up as equity holders.

MR. BENDIX: That is --

QUESTION: You cannot have anybody bidding against you; that would defeat the whole thing?

MR. BENDIX: That is correct.

And if you think about it, who else besides somebody facing a tax liability, would pay $6 million-plus for this interest, which the court has found is worthless because it's completely subordinate to the bank's

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deficiency claim?

QUESTION: Well, but it might be possible, if there were other people who felt that the property had been undervalued, to bid up -- requiring your clients to bid up, so they end up paying, but they end up paying not 6 million, but 10 million, maybe?

MR. BENDIX: Well, that's possible. The interesting fact here is that -- it's important to remember that the bank is here, arguing as an unsecured creditor. 1129(b)(2)(B)(ii) and the absolute priority rule only applies to a dissenting class of unsecured claims. Under this plan, the deficiency claim got all of the future appreciation in the building until its claim was paid in full.

Therefore, what difference does it make to an unsecured creditor who gets that whether the building, for purposes of the bank's separate secured claim -- which they're not here contesting today -- was worth a million dollars more or less? They get everything that's there before the investors got a penny. And that's why it just seems obvious, and it seemed clear to the judge, that this was a -- a fair price to pay for the -- for the equity interest, because the owners get nothing back except this tax deferral until the bank has been paid --

QUESTION: The question is, why should the judge

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be the judge of that rather than what is the only substantial creditor in the picture?

MR. BENDIX: Because that's what Congress has said. What the bank is really doing here is making a policy argument that they don't like bankruptcy judges second-guessing their decisions. That's -- that's a plausible policy statement to make. But Congress said judges decide value and judges decide whether plans are fair.

If they don't like that, they are perfectly free to walk across the street and argue to Congress that the -- the statute should be changed. But --

QUESTION: Mr. Bendix, what about the argument that when this new value corollary came in, in the Case case, that the Bankruptcy Act was structured differently, so that you could have one recalcitrant creditor holding up the whole works and everybody else is willing to go through, now the Bankruptcy Act has taken -- the Bankruptcy Code has taken care of that by having classes of creditors and you can't have just one creditor holding out, so that the problem that that was addressing is now handled in a different way?

MR. BENDIX: Well, the earlier cases really didn't address that problem. The earlier cases addressed the problem of whether the unsecured creditors are getting

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all of the reorganization value of the company or whether something is being diverted to a junior class. The change in the Bankruptcy Code doesn't affect that.

What -- what we have now is, instead of under -- as under old Chapter 10, the right of an individual creditor to object, now it has to be by classes. But as somebody pointed out earlier, the absolute priority rule only comes into effect if you have one class that agrees and one class that disagrees. So the analysis that you go through with respect to the disagreeing party -- whether that party is an individual creditor or class -- is exactly the same under the Code as it was under Chapter 10 and, indeed, under the Federal equity receivership proceedings that existed even before Chapter 10.

The change, quite simply, has no effect on the content of the absolute priority rule.

I want to address for a moment the idea that there was an exclusive option here. Justice Scalia, I think, pointed out correctly there's nothing in the plan in this case that creates an option. An option existed in the case that we cited in our brief, Consolidated Rock. There, the plan said the old owners are getting an option, and they're not paying anything for it.

An option itself is not a bad thing. It's simply a question of whether you pay for it. The language

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of the plan in this case is absolutely clear that the owners had an obligation to put the money in, and the debtor had an obligation to sell the equity to the investors.

QUESTION: Well, even if -- if it wasn't properly described as an option, it included an option, did it not?

MR. BENDIX: No, it didn't, Mr. Chief Justice. Before the plan was confirmed, the debtor had this exclusive right to file a plan. And it had to designate somebody who was going to put the money in. Before a plan is confirmed, it is nothing more than an offer. It's not a contract. It creates no legal rights or obligations unless and until it's been confirmed by the bankruptcy court.

So, yes, of course, there was some -- in some colloquial sense, an opportunity that these people had before confirmation, but they had no legal rights. They couldn't exercise an option and say, now -- now give me my stock.

QUESTION: Well, but the bank -- it was the bankruptcy plan that gave them the legal rights, I take it?

MR. BENDIX: Yes. But once the plan is confirmed, you have a consummated sale. The -- the record

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shows in this case that the money for the -- the new capital was -- the cash -- was put into escrow before confirmation, so that the judge would be satisfied that the plan would be feasible. As soon as the plan was confirmed, simultaneously, the money went out and the -- and the new stock came back.

There was never a moment in time here where there was any discretion in the sense that it exists under an option where --

QUESTION: But are you saying, then, they didn't receive any property within the meaning of (b)(2)(B)(ii)?

MR. BENDIX: No, not at all, Your Honor. They -- they received a very obvious form of property; namely, 100 percent of the equity in the reorganized company.

QUESTION: How does that differ -- how does that make your case any better for purposes of (b)(2)(B)(ii) and the "on account of" language?

MR. BENDIX: Well, the bank is not here arguing that our purchase, the investors' purchase of the equity, violated the statute. They say disregard that. We admit that that's not a problem. What they're saying is that in addition to the actual equity interest that was purchased, there was this so-called option. That's what they hinge their case on, in addition to whether "on account of" --

QUESTION: Well, because of their prior status, they and they alone were entitled to make this purchase.

MR. BENDIX: That's true before the plan was confirmed, and even afterwards. Any time you have a contract -- if I sell you my car, nobody else but you can buy that car. That doesn't mean that you have gotten some option in addition to the car that you've purchased. That's inherent in -- in the nature of a completed contract for the sale of property.

What they're trying to do is create a separate option here, separate and apart from the obvious form of property that was purchased. And that simply doesn't exist.

QUESTION: Well, but there was an option, because all the partners didn't have to participate. I mean each individual partner had an option, did he not?

MR. BENDIX: Not in -- perhaps in a -- a colloquial sense, but not in the sense of my giving you an option to buy 100 shares of my stock at a fixed price for the next 6 months.

There was -- there was a general obligation on the part of the partners to put in $6 million -- a little bit more. Those who didn't put the money in lost their interest. In a true option, if you don't exercise your option, you don't suffer the kinds of legal consequences

that the non-contributing partners suffered in this case.

QUESTION: Did that mean that when some people didn't participate, the shares of the others had to be that much larger?

MR. BENDIX: Effectively, yes.

QUESTION: Okay.

MR. BENDIX: Sixty percent of the ownership interest changed hands under this plan. People received interest in the reorganized firm in direct proportion to the amount of money that they put in. And the amount of money that they put in was not necessarily related in any way to their pre-bankruptcy percentage ownership interest.

QUESTION: Were -- were there any new members of the reorganized firm that hadn't been members of the old one?

MR. BENDIX: No, Mr. Chief Justice. And, again, it's important to remember that if that had happened, that would have basically destroyed the -- the tax benefits that these people were buying.

QUESTION: So it was a very limited universe that you're talking about?

MR. BENDIX: That's correct.

QUESTION: Why are people arguing about option? I didn't understand that part of it. I mean they got -- they got the building. They got the building. And they

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put up the 6 million. And I thought the issue in the case -- they got the building under the plan. It provided that they get the building for the 6 million. And I thought we were arguing about whether they got the building for the 6 million and also because of their prior ownership.

I mean I don't understand why it matters whether we're talking about an op -- why are we looking for an option? They -- we must be. Because I agree with you, they want to. But can you explain it to me?

MR. BENDIX: The bank is trying to say that we got some form of property in addition to the equity that we purchased, that we --

QUESTION: Why -- why isn't enough for the case that you got the equity? You got the equity, you got the building. You got the equity. You put up 6 million. You say, we got it just because of the 6 million. You -- they -- as far as the statute is concerned, they say you got it because of the 6 million and also on account of other prior ownership. So how does it change the case?

MR. BENDIX: Well, they make that argument with respect to the so-called option, Justice Breyer. They don't make the argument with respect to the actual equity interest that was --

QUESTION: If I drop the option out in my mind,

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is it going to make a difference to the decision?

MR. BENDIX: If you accept our interpretation of "on account of" as meaning in exchange for or in satisfaction of, then of course our position is that we received this equity interest in exchange for the new money. And, again, it's important to remember that the interests of non-contributing partners were wiped out. So they received absolutely nothing under the claim. They lost their interests.

There's a number --

QUESTION: In substance, this so-called option is nothing more or less -- as I take it -- than the limited eligibility to put up the 6 million. That's all it means, isn't it?

MR. BENDIX: I think that's what they've tried to characterize it as. And -- and it's -- it's important to remember, as I think Justice Scalia mentioned in the earlier colloquy, that the property -- in order to run afoul of the statute, you have to receive property, you have to receive it on account --

QUESTION: Well, isn't that a valuable right?

MR. BENDIX: The -- the exclusive right to file a plan and to be designated as a potential funder of the plan is certainly valuable. It's not something that was -- it was not property that was distributed under the

plan as confirmed. There is this --

QUESTION: Well, but where does the provision say it has to be property as distributed under the plan?

MR. BENDIX: It's -- it's right in Section 1129(b)(2)(B)(ii).

QUESTION: Yes, but what's -- what's the exact language that you rely on?

MR. BENDIX: Bear with me one second.

QUESTION: The reason I ask the question is that Subsection (2) -- (2)(B)(ii) refers to any property.

MR. BENDIX: But the earlier --

QUESTION: And that -- which sounds pretty broad.

MR. BENDIX: Let me just read -- let me read the language. It says: For purposes of this subsection, the condition that a plan be fair and equitable with res --

QUESTION: Where are you reading from?

MR. BENDIX: I'm reading from --

QUESTION: I guess if we take the bank's brief --

QUESTION: (b)(2)(B)(ii) or --

MR. BENDIX: (b)(2)(B)(ii).

It says: The holder of any claim or interest that is junior to the claims of such class will not receive or retain under -- under the plan, on account of

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such junior claim or interest, any property.

We read that to mean -- that phrase, "under the plan" -- to mean under the plan as confirmed.

QUESTION: So are you saying you didn't receive any property under the plan?

MR. BENDIX: No, Your Honor. We're saying that we received an equity interest under the plan and not any option to purchase equity.

QUESTION: No, but you also received another ben -- or would have received another benefit under the plan. And that was the exclusive opportunity to acquire or retain that equity interest.

MR. BENDIX: But that's really not what -- that's not an opportunity. That is -- once the plan is confirmed, that's what you bought. I guess you could say that --

QUESTION: Well, in the sense that you undertake, by presenting the plan, to exercise that opportunity. So that I suppose, you know, there is a legal instant in time in which all of this occurs. But it's still the case that at the moment the plan becomes operative, you have an opportunity, and nobody else can have one.

MR. BENDIX: Actually, not, Your Honor. Under the plan, there is an obligation -- there's a binding

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obligation to put the money in. It's not an opportunity.

Thank you very much.

QUESTION: Thank you, Mr. Bendix.

Mr. Englert, you have 3 minutes remaining.

REBUTTAL ARGUMENT OF ROY T. ENGLERT, JR.

ON BEHALF OF THE PETITIONER

MR. ENGLERT: Thank you, Mr. Chief Justice.

There are two forms of property that were received or retained under the plan on account of the junior interest, in violation of the statute. One is the option. The second is the equity.

Mr. Bendix says we do not contend that the equity was received on account of the prior junior interest. That's flatly wrong. We do contend that both forms of property were so received.

This is the second time the Court has construed 1129(b)(2)(B)(ii). The first time, the debtor's counsel stood at the lectern in this Court and said the creditors are getting a windfall because we're putting in new value. This Court's response, in a unanimous opinion, was: The Court of Appeals may well have believed that Petitioners or other unsecured creditors would be better off if Respondent's reorganization plan was confirmed. But that determination is for the creditors to make in the manner specified by the Code.

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QUESTION: What case is that?

MR. ENGLERT: Norwest Bank Worthington v. Ahlers, 485 U.S., at 207.

QUESTION: Of course, if we meant that literally, we shouldn't have left the question open.

(Laughter.)

MR. ENGLERT: Your Honor, I do suggest that the Court meant that literally. And I do suggest that that's what the legislative history and text of the Code both say.

In -- in reference to the legislative history, let me say, Mr. Bendix relies heavily on pre-Code practice. The legislative history, at page 414 of the House report, says: The elements of the test are new, departing from both the absolute priority rule and the best interest of creditors test found under the Bankruptcy Act.

QUESTION: Wasn't that with regard to the bill they didn't enact?

MR. ENGLERT: No, absolutely not, Your Honor. H.R. 8200 was passed by the House. Its language was taken into the Code that was enacted, in preference to the Senate report.

And the debtor says, look at what the conferees said. Let me tell you what the conferees said. I'm

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quoting: Except to the extent of the treatment of secured claims under subparagraph (a) of this statement, the House report remains an accurate description of confirmation of Section 1129.

That's from 124 Congressional Record, 32,408, and 34,007. It's quoted in footnote 23 of the Solicitor General's brief.

QUESTION: That may be wrong.

MR. ENGLERT: Justice Scalia, legislative history always could be wrong.

(Laughter.)

MR. ENGLERT: But the legislative history is very one-sided in this case.

"In exchange for" cannot possibly be the meaning of "on account of." Section 1123(a)(5)(J) of the Bankruptcy Code uses "in exchange for" and not "on account of." And you cannot receive or retain property in exchange for something. The fact that "on account of" is used repeatedly in connection with the phrase "receive or retain" shows that it must have a broader meaning than "in exchange for." And, indeed, if -- if Mr. Bendix's argument about "in exchange for" were correct, ours was wrongly decided. It's holding and not just every literal word of it, Justice Stevens.

QUESTION: No, there is no new cash in that

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deal.

MR. ENGLERT: There was no cash. That was a --

QUESTION: In the farmer deal?

MR. ENGLERT: I'm sorry, there was -- there was an exchange. There was sweat equity.

QUESTION: Yeah.

MR. ENGLERT: That's correct.

But the -- the sweat equity was treated as having economic value.

The -- Justice Scalia, there is --

QUESTION: That was precisely the kind of economic value that Justice Douglas said should not count.

MR. ENGLERT: Correct.

QUESTION: Yeah. But -- and he said the other with respect to cash.

MR. ENGLERT: He said the other with respect to cash under the 1898 Bankruptcy Act, yes.

MR. ENGLERT: Thank you.

CHIEF JUSTICE REHNQUIST: Thank you, Mr. Englert. The case is submitted.

(Whereupon, at 12:01 p.m., the case in the above-entitled matter was submitted.)

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CASE NO: 97-1418

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