

QUESTIONS PRESENTED

- I. Is the power to order substantive consolidation of multiple debtors' estates, a remedy that did not exist in the English courts of chancery at the time of the enactment of the Judiciary Act of 1789 and one that is not expressly authorized in the Bankruptcy Code, within the scope of federal courts' equitable jurisdiction?

- II. Do pending employment discrimination claims against a corporation that is a debtor in bankruptcy constitute "interests in property" as contemplated by Section 363(f) of the Bankruptcy Code, such that the corporation's assets can be sold free and clear of the claims?

TABLE OF CONTENTS

| | |
|---|-----------|
| QUESTIONS PRESENTED | i |
| TABLE OF AUTHORITIES | v |
| OPINIONS BELOW | 1 |
| STATEMENT OF THE CASE | 1 |
| SUMMARY OF THE ARGUMENT | 3 |
| ARGUMENT | |
| I. FEDERAL COURTS DO NOT HAVE THE POWER TO ORDER SUBSTANTIVE CONSOLIDATION OF MULTIPLE DEBTORS’ ESTATES. | 5 |
| A. The Equitable Powers of the District Court Do Not Extend to Authorizing Substantive Consolidation of Bankruptcy Estates. | 6 |
| 1. <u>The Judiciary Act of 1789 limits the equitable jurisdiction of federal courts to remedies and procedures employed by the English Court of Chancery in 1789.</u> | 7 |
| 2. <u>Grupo Mexicano de Desarrollo v. Alliance Bond Fund, Inc. solidified the limitation on federal courts’ equitable powers.</u> | 9 |
| 3. <u>Substantive consolidation was not an equitable remedy available at Chancery in 1789, so federal courts may not employ the remedy under their general equitable powers.</u> | 10 |
| a. English Courts of Chancery did not employ the equitable remedy of substantive consolidation in any bankruptcy proceeding. | 11 |
| b. Substantive consolidation is a twentieth century product of judicial convenience with no substantial legal basis. | 12 |
| B. There Is No Statutory Authorization for the District Court to Order Substantive Consolidation in This Case. | 14 |
| 1. <u>Congress did not make the specific grant of power</u> | |

| | | |
|-----|---|----|
| | <u>required to establish substantive consolidation as a new remedy.</u> | 14 |
| 2. | <u>The courts’ powers under Section 105(a) do not include the use of substantive consolidation.</u> | 15 |
| 3. | <u>The Bankruptcy Code contains no other provision to authorize the order for substantive consolidation in this case.</u> | 18 |
| C. | Even If the Equitable Jurisdiction of the Federal Courts Includes the Authority to Order Substantive Consolidation, That Power Should Not Be Exercised in this Case. | 20 |
| 1. | <u>Courts have authorized substantive consolidation only after conducting a balancing test.</u> | 20 |
| 2. | <u>This case fails to meet the test for substantive consolidation.</u> | 21 |
| II. | THE BANKRUPTCY CODE DOES NOT PERMIT THE SALE OF ASSETS FREE AND CLEAR OF SUCCESSOR LIABILITY CLAIMS UNDER SECTION 363(F). | 23 |
| A. | “Claims” Are Not “Interests” Under Title 11, and Therefore They Are Not Subject to a Free and Clear Asset Sale Under Section 363(f). | 24 |
| 1. | <u>“Claims” are specifically excluded from Section 363(f).</u> | 25 |
| 2. | <u>Equating “claims” with “interests” circumvents the protections that Congress built into the reorganization plan process for creditors.</u> | 26 |
| 3. | <u>Equating “claims” and “interests” in Section 363(f) renders the phrase “in such property” mere surplusage.</u> | 28 |
| B. | Section 363(f)’S “Interests in Property” Does Not Include Unsecured Claims Such as Respondent’s. | 29 |
| 1. | <u>363(f)’s “interest in such property” refers only to in rem interests and does not extinguish in personam claims.</u> | 29 |
| 2. | <u>363(f) cannot encompass Respondent’s claim because such a claim is not afforded the requisite “adequate</u> | |

protection” of Section 363(e).31

**C. Allowing Section 363(f) to Include Claims Like Respondent’s
Directly Undermines Congress’s Underlying Purposes for
Chapter 11 and Successor Liability.32**

**1. The purpose of successor liability is undermined by
allowing Section 363(f) to justify sales free and clear
of claims such as Respondent’s.33**

**2. Misinterpreting Section 363(f) turns Chapter 11 into a
business forum for the buying and selling of assets.33**

**3. Excluding Respondent’s claims from coverage under 363(f)
does not provide her with favored status over other creditors.34**

CONCLUSION35

CERTIFICATE OF SERVICE35

TABLE OF AUTHORITIES

United States Supreme Court Cases:

| | |
|---|--------|
| <i>Atlas Life Ins. Co. v. W.I. S., Inc.</i> , 306 U.S. 563 (1939). | 9 |
| <i>Caminetti v. United States</i> , 242 U.S. 470 (1917). | 23, 25 |
| <i>Conn. Nat’l Bank v. Germain</i> , 503 U.S. 249 (1992). | 16 |
| <i>Desert Palace Inc. v. Costa</i> , 539 U.S. 90 (2003). | 15 |
| <i>Gordon v. Washington</i> , 295 U.S. 30 (1935). | 7 |
| <i>Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc.</i> , 527 U.S. 308 (1999). | passim |
| <i>Guaranty Trust Co. of N.Y. v. York</i> , 326 U.S. 99 (1945). | 7, 8 |
| <i>Hartford Underwriters Ins. Co. v. Union Planters Bank</i> , 530 U.S. 1 (2000). | 15 |
| <i>Louisville Joint Stock Land Bank v. Radford</i> , 295 U.S. 555 (1935). | 31 |
| <i>Norwest Bank Worthington v. Ahlers</i> , 485 U.S. 197 (1988). | 17 |
| <i>Payne v. Hook</i> , 74 U.S. 425 (1868). | 7 |
| <i>Pierce v. Underwood</i> , 487 U.S. 552 (1988). | 6 |
| <i>Robinson v. Campbell</i> , 16 U.S. 212 (1818). | 7 |
| <i>Robinson v. Shell Oil Co.</i> , | |

| | |
|--|--------|
| 519 U.S. 337 (1997). | 15--16 |
| <i>Sampsell v. Imperial Paper Color Corp.</i> , 313 U.S. 215 (1941). | 13 |
| <i>United States v. Nordic Village, Inc.</i> , 503 U.S. 30 (1992). | 16 |
| <i>United States v. Ron Pair Enter. Inc.</i> , 489 U.S. 235 (1989). | 25 |
| <i>Wright v. Union Central Life</i> , 311 U.S. 273 (1940). | 31 |
| <u>Federal Circuit Court Cases:</u> | |
| <i>Chem. Bank N.Y. Trust Co. v. Kheel</i> , 369 F.2d 845 (2d Cir. 1966). | 12, 13 |
| <i>Disch v. Rasmussen</i> , 417 F.3d 769 (7th Cir. 2005). | 17, 18 |
| <i>Eastgroup Properties v. S. Motel Assoc.</i> , 935 F.2d 245 (11th Cir. 1991). | 20 |
| <i>Fed. Deposit Ins. Corp. v. Colonial Realty Co.</i> , 966 F.2d 57 (2d Cir. 1992). | 13, 18 |
| <i>Fish v. East</i> , 114 F.2d 177 (10th Cir. 1940). | 12 |
| <i>Hawes Org. Inc. v. Basic Distribution Corp.</i> , 957 F.2d 239 (6th Cir. 1992). | 26 |
| <i>In re Augie/Restivo Baking Co. Ltd.</i> , 860 F.2d 515 (2d Cir. 1988). | 13, 18 |
| <i>In re Auto-Train Corp.</i> , 810 F.2d 270 (D.C. Cir. 1987). | 20--21 |
| <i>In re Bonham</i> , 229 F.3d 750 (9th Cir. 2000). | 18 |

| | |
|--|--------|
| <i>In re Chicago, Milwaukee, St. Paul & Pac. R.R. Co.</i> , 791 F.2d 524 (7th Cir. 1986). | 8, 18 |
| <i>In re Continental Airlines, Inc.</i> , 780 F.2d 1223 (5th Cir. 1986). | 27 |
| <i>In re Continental Vending Mach. Corp.</i> , 517 F.2d 997 (2d Cir. 1975). | 20, 21 |
| <i>In re Dairy Mart Convenience Stores, Inc.</i> , 351 F.3d 86 (2d Cir. 2003). | 16, 17 |
| <i>In re Fesco Plastics</i> , 996 F.2d 152 (7th Cir. 1993). | 17, 18 |
| <i>In re Flora Mir Candy Corp.</i> , 432 F.2d 1060 (2d Cir. 1970). | 21 |
| <i>In re Haber Oil Co.</i> , 12 F.3d 426 (5th Cir. 1994). | 16-17 |
| <i>Musikiwamba v. Essi, Inc.</i> , 760 F.2d 740 (6th Cir. 1985). | 34 |
| <i>Rojas v. TK Communications</i> , 87 F.3d 745 (5th Cir. 1996). | 23, 33 |
| <i>Soviero v. Franklin Nat'l Bank of Long Island</i> , 328 F.2d 446 (2d Cir. 1964). | 12 |
| <i>Stone v. Eacho</i> , 127 F. 2d 284 (4th Cir. 1942). | 12 |
| <i>United States v. Sutton</i> , 786 F.2d 1305 (5th Cir. 1986). | 17 |

Federal District and Bankruptcy Court Cases:

Berge v. Sweet,

| | |
|--|--------|
| 37 B.R. 705 (Bankr. W.D. Wis. 1983). | 23 |
| <i>Fairchild Aircraft Corp. v. Campbell</i> , 184 B.R. 910 (Bankr. W.D. Tex. 1995). | passim |
| <i>In re Cook</i> , 205 B.R. 437 (Bankr. N.D. Fla. 1997). | 31 |
| <i>In re Ingle</i> , 91 B.R. 27 (Bankr. E.D. Mich. 1988). | 31 |
| <i>In re Wandrey</i> , 334 B.R. 427 (Bankr. N.D. Ind. 2005). | 28 |
| <u>Statutes and Regulations:</u> | |
| 11 U.S.C. § 105(a) (2005). | 16 |
| 11 U.S.C. § 302(b) (2005). | 14, 19 |
| 11 U.S.C. § 362(e) (2005). | 32 |
| 11 U.S.C. § 363 (2005). | 23, 25 |
| 11 U.S.C. § 501 (2005). | 25 |
| 11 U.S.C. § 502 (2005). | 25 |
| 11 U.S.C. § 503 (2005). | 31 |
| 11 U.S.C. § 506 (2005). | 31 |
| 11 U.S.C. § 507 (2005). | 31 |
| 11 U.S.C. § 510 (2005). | 26 |
| 11 U.S.C. § 521 (2005). | 31 |
| 11 U.S.C. § 541 (2005). | 26 |
| 11 U.S.C. § 542 (2005). | 31 |
| 11 U.S.C. § 552 (2005). | 31 |

| | |
|---------------------------------|----------------|
| 11 U.S.C. § 553 (2005). | 31 |
| 11 U.S.C. § 554 (2005). | 31 |
| 11 U.S.C. § 724 (2005). | 31 |
| 11 U.S.C. § 922 (2005). | 31 |
| 11 U.S.C. § 1111 (2005). | 26, 31 |
| 11 U.S.C. § 1112 (2005). | 31 |
| 11 U.S.C. § 1122 (2005). | 26, 31 |
| 11 U.S.C. § 1123 (2005). | passim |
| 11 U.S.C. § 1124 (2005). | 26, 31 |
| 11 U.S.C. § 1125 (2005). | 26 |
| 11 U.S.C. § 1126 (2005). | 26 |
| 11 U.S.C. § 1141 (2005). | 26, 27, 28, 34 |
| 11 U.S.C. § 1145 (2005). | 26 |
| 11 U.S.C. § 1205 (2005). | 31 |
| 11 U.S.C. § 1221 (2005). | 31 |
| 11 U.S.C. § 1225 (2005). | 31 |
| 11 U.S.C. § 1227 (2005). | 26, 28 |
| 11 U.S.C. § 1322 (2005). | 31 |
| 11 U.S.C. § 1325 (2005). | 31 |
| 11 U.S.C. § 1326 (2005). | 31 |
| 11 U.S.C. § 1327 (2005). | 31 |
| Bankr. R. 2002(a) (2005). | 27 |

| | |
|---|----------|
| Bankr. R. 6004(f) (2005). | 27 |
| Fed. R. Bankr. Proc. 1015 (2005). | 19 |
| <u>Secondary Authority:</u> | |
| 1 Story's Commentaries on Equity Jurisprudence § 19 (W.H. Lyon Jr., ed., 14th ed. 1918). | 8 |
| 1 William Blackstone, Commentaries 269 (1st ed. 1765). | 11 |
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| Edward V. Robinson, <i>The Holding Corporation—II</i> , 19 Yale Rev. 13. | 11 |
| H.R. Rep. No. 95—595 (1977). | 33 |
| J. Maxwell Tucker, <i>Grupo Mexicano and the Death of Substantive Consolidation</i> , 8 Am. Bankr. L. Rev. 427. | 10,11,12 |
| Nathan F. Coco, <i>An Examination of Successor Liability in the Post-Bankruptcy Context</i> , 22 J. Corp. L. 345. | 30 |

OPINIONS BELOW

The decision of the United States District Court for the District of Kelly is unreported. The opinion of the United States Court of Appeals for the Thirteenth Circuit has not been published, but is included in its entirety in the Appendix to this brief.

STATEMENT OF THE CASE

Factual Background

Chemical America Product Company, Inc. (“CAPCO”), which produces calcium chloride at its facility in Manistee, Michigan, is the defendant in a class action lawsuit alleging sex and gender discrimination by the company (Record at 3–5). More specifically, CAPCO is accused of violating Title VII of the Civil Rights Act of 1964 by creating a hostile work environment for female employees and failing to pay them “equal pay” for “equal work” (R. at 5). The success of the plaintiffs in the discrimination lawsuit, including the Respondent in this case, will result in a large recovery against CAPCO (R. at 5).

CAPCO is a subsidiary of Acme Chemical Industrial Products, Inc. (“ACME”), which also owns Trona Ash Products Company, Inc. (“TAPCO”) (R. at 2–3). Although the three companies share officers, directors, employees, and a centralized cash management system operated by ACME, they each engage in a distinct business pursuit (R. at 2–3, 4). CAPCO produces calcium chloride, which is used primarily as a de-icing agent for roads and highways, and also helps to prevent surface deterioration of roads (R. at 3). TAPCO produces soda ash, or sodium carbonate, which is used to make glass, soaps, determents, rubber, explosives, and other chemicals (R. at 3). ACME markets and distributes the products of its two subsidiaries (R. at 2–3). While TAPCO and ACME have suffered financially from the increasingly depressed prices of soda ash, CAPCO has enjoyed soaring sales of its calcium chloride during the past several years, due to the development of industry and

infrastructure in countries in Southeast Asia and South America (R. at 4–5).

ACME’s financial difficulties have caused it to default on several lending agreements, and after a failed attempt to restructure out of court, ACME, TAPCO, and CAPCO filed for relief under Chapter 11 of the Bankruptcy Code (R. at 5–6). After determining that the businesses should be sold, ACME received an offer to purchase all three companies from Sousa Industries, Inc. (“SOUSA”), one of TAPCO’s competitors (R. at 6, 8). Concerned about successor liability for the claims of Respondent and the other discrimination plaintiffs, SOUSA insisted that the sale of the businesses be accomplished in such a way that it would be shielded from any liability (R. at 6). SOUSA has made it clear that the sale will not be finalized until this appeal is resolved, although SOUSA’s CEO has conceded that he would purchase the businesses even in light of the outstanding discrimination claims if he could negotiate a reduced purchase price or a payment of the claims from the sales proceeds (R. at 8–9).

Procedural History

ACME filed a motion in the Bankruptcy Court requesting the substantive consolidation of the bankruptcy estates of ACME, TAPCO, and CAPCO, and requested that the court authorize the sale of the assets of all three corporations free and clear of all liens, claims, and encumbrances, pursuant to Section 363(f) of the Bankruptcy Code (R. at 6–7). After a hearing on the matters, and over the objection of Respondent, the District Court granted ACME’s motion, erroneously concluding that the extensive inter-corporate dealings of the three companies demanded the substantive consolidation of their bankruptcy estates, and that a sale of CAPCO’s assets free and clear of Respondent’s discrimination claims was appropriate pursuant to Section 363(f) (R. at 7–8).

Respondent appealed to the Court of Appeals for the Thirteenth Circuit, contesting the authority of the District Court to order the substantive consolidation and to allow the sale of CAPCO

free of her discrimination claims (R. at 9). The Court of Appeals reversed the District Court's decision in its entirety, holding that substantive consolidation was not within the scope of the federal courts' equity powers by virtue of general equitable jurisdiction or authority from the Bankruptcy Code, and also that Respondent's claim was not an "interest in property" that could be stripped away in a sale of assets pursuant to Section 363(f) (R. at 18–19).

This Court granted Petitioner ACME's application for writ of certiorari to consider the issues of substantive consolidation and a sale of assets free and clear of successor liability claims under the Bankruptcy Code (R. at 1).

SUMMARY OF ARGUMENT

I. FEDERAL COURTS DO NOT HAVE THE POWER TO ORDER SUBSTANTIVE CONSOLIDATION OF MULTIPLE DEBTORS' ESTATES

In the exercise of their general equitable powers, federal courts are limited to employing those equitable remedies that were available in the English courts of chancery at the time of the enactment of the Judiciary Act of 1789. Substantive consolidation of the bankruptcy estates of multiple debtors was not a remedy employed by the English courts of chancery. In fact, substantive consolidation did not even come into being until the twentieth century, and then only as an invention of the federal judiciary. Accordingly, the general equitable jurisdiction of the federal courts does not include the power to order substantive consolidation.

Additionally, there exists no statutory basis for the order in this case that the debtors' estates be substantively consolidated. Although the district court pointed to the broad powers granted in Section 105(a) of the Bankruptcy Code, the express terms of that provision limit its application to "the provisions of this title." In other words, courts are granted only those equitable powers necessary to accomplish what is expressly authorized in the Code. Since no substantive provision in

the Bankruptcy Code authorizes the consolidation ordered in this case, Section 105(a) does not supply a basis for the order.

Substantive consolidation, even if determined by this Court to be authorized, is not appropriate in this case. Courts employing substantive consolidation have done so only after conducting a strict balancing test, and only when it is determined that the measure will ensure equitable treatment of all creditors. Where a creditor who relies on the financial viability of a debtor would be prejudiced by substantive consolidation, as would the Respondent in this case, using the remedy would undermine its purpose; namely, effecting an equitable distribution among creditors.

II. THE BANKRUPTCY CODE DOES NOT PERMIT THE SALE OF ASSETS FREE AND CLEAR OF SUCCESSOR LIABILITY CLAIMS UNDER SECTION 363(F).

ACME cannot be permitted to sell its assets free and clear of Respondent's employment discrimination claim under Section 363(f) of the Bankruptcy Code. Section 363(f) permits sales of assets free and clear of "interests in such property." There is no basis in the Bankruptcy Code for interpreting "claims," such as Respondent's, to mean "interests," as used in 363(f); in fact, the Code in numerous provisions distinguishes between "claims" and "interests." The plain meaning of the language of 363(f), in conjunction with this distinction between "claims" and "interests" in other parts of the Code, demonstrates Congress's intentional exclusion of "claims" in 363(f). Congress intended free and clear asset sales to occur only under approved plans of reorganization; allowing debtors to make free and clear asset sales outside of the reorganization context deprives creditors, like Respondent, of the protections that Congress built into the reorganization process. While a few courts have interpreted 363(f) to include "claims" as "interests," this misinterpretation renders an important phrase in the statute, "in such property," inoperative.

Unsecured claimants, such as Respondent, have no in rem "interest in property" that could be

disregarded in a free and clear sale under Section 363(f). “Interest in such property” refers only to in rem interests and is not intended to extinguish such in personam claims as the unsecured claim held by Respondent. Additionally, “interests in such property” that may be stripped in a 363(f) asset sale must receive adequate protection as mandated by Section 363(e); because adequate protection does not apply to unsecured claims, it follows that 363(f) must not apply to unsecured claims.

Using Section 363(f) as a justification for allowing claims like Respondent’s to be discarded in a sale of the assets of a debtor undermines overwhelming policy considerations, while contravening requirements Congress imposed for asset sales of this nature. The important purpose of successor liability is circumvented if sales are allowed free of those claims. In addition, judicial allowance of free and clear asset sales transforms Chapter 11 from a facilitator of reorganization planning to a business forum for buying and selling assets. Finally, excluding Respondent’s claim from the coverage of Section 363(f) will not provide her with any favored status over other unsecured creditors of ACME.

ARGUMENT

I. FEDERAL COURTS DO NOT HAVE THE POWER TO ORDER SUBSTANTIVE CONSOLIDATION OF MULTIPLE DEBTORS’ ESTATES.

This Court should affirm the decision of the court of appeals, because the district court did not have the authority to substantively consolidate the estates of ACME, TAPCO, and CAPCO. There are three reasons this Court should conclude that the District Court decision to issue the order for consolidation of these estates was in error. First, the general equitable powers of the district court do not extend to authorizing substantive consolidation as a remedy in bankruptcy. The Judiciary Act of 1789 and subsequent case law limits the federal courts’ general equitable jurisdiction to those remedies available at the English Court of Chancery in 1789. Because

substantive consolidation did not even exist until the twentieth century, the courts' general equitable powers do not include such a remedy. Second, Congress has not granted the federal courts the power to substantively consolidate debtors' estates. No provision in the Bankruptcy Code confers a general power of substantive consolidation upon the federal courts, and where the Code does mention substantive consolidation, it provides specific prescriptions not applicable to this case. Finally, even if the equitable powers of the court included the authority to order substantive consolidation, that remedy is not appropriate in this case, as the remedy should be used only sparingly and in very specific circumstances which are not present here. In light of these considerations, this Court should not permit substantive consolidation of the estates of these three entities.

Because the issue of whether substantive consolidation is a remedy that may be invoked by federal courts is purely a question of law, this Court should review the decision of the district court *de novo*. *Pierce v. Underwood*, 487 U.S. 552, 558 (1988).

A. The Equitable Powers of the District Court Do Not Extend to Authorizing Substantive Consolidation of Bankruptcy Estates.

The district court did not have the authority to order substantive consolidation of ACME, CAPCO, and TAPCO under its general equitable powers. This Court has repeatedly held that the federal judiciary does not possess the boundless authority to invoke new powers, procedures and remedies not granted by the Constitution, the Judiciary Act, or relevant statute. *Guaranty Trust Co. of N. Y. v. York*, 326 U.S. 99, 104–05 (1945); *Gordon v. Washington*, 295 U.S. 30, 36 (1935). This Court has directly addressed the issue of the scope of the equitable powers of the federal courts in cases dating back to the early nineteenth century, not long after Congress passed the Judiciary Act. *See, e.g., Robinson v. Campbell*, 16 U.S. 212 (1818); *Payne v. Hook*, 74 U.S. 425 (1868). And

recently, the Court reviewed this specific issue in a bankruptcy context in *Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc.* 527 U.S. 308 (1999). Historical context and precedent, along with recent cases concerning related subject matter, clearly demonstrate that this Court's position is one of restraint when considering the scope of the judiciary's equitable powers. Neither history nor recent case law authorizes substantive consolidation in this case.

1. The Judiciary Act of 1789 limits the equitable jurisdiction of federal courts to remedies and procedures employed by the English Court of Chancery in 1789.

Historical analysis refutes the court's authority to order substantive consolidation in this case. Neither the framers of the Constitution nor the Congressional authors of the 1789 Judiciary Act intended for the federal courts to exercise unlimited equitable jurisdiction. The Judiciary Act of 1789 conferred jurisdiction to the lower federal courts in "all suits . . . in equity." *Gordon*, 295 U.S. at 36. From the beginning, this Court has consistently interpreted the intent of Congress in enacting the Judiciary Act of 1789 as limiting the equitable relief available in federal courts to those measures available at the English Court of Chancery. *Id.*; *Robinson*, 16 U.S. at 212 (acknowledging that remedies in the courts of the United States are derived from those "as distinguished and defined in that country from which we derive our knowledge of those principles"); *Payne*, 74 U.S. at 430 (stating that the equity jurisdiction conferred upon the federal court is the same as the High Court of Chancery in England possesses). This Court has narrowly construed the remedial power of federal courts sitting as courts in equity and has prohibited the courts from crafting remedies that did not exist at Chancery in 1789. *Grupo Mexicano*, 527 U.S. at 322; *Guaranty Trust Co. of N. Y. v. York*, 326 U.S. 99, 105 (1945) (stating that this enactment gave the federal courts no power that they would not have possessed in any event when the courts were first given "cognizance of equity" by

the Judiciary Act of 1789).

The work of legal scholars contemporary to the Judiciary Act of 1789 further bolsters that Congress did not intend to vest unlimited jurisdiction in the federal courts. Justice Joseph Story's treatise on Equity Jurisprudence aptly conveys the reasoning behind the limitations on the equitable powers of the United States federal courts. 1 Story's Commentaries on Equity Jurisprudence § 19 (W.H. Lyon Jr., ed., 14th ed. 1918). The underpinnings of these limitations rest in the fundamental principle that one man's opinion of what is fair or equitable should not control the judiciary's application or interpretation of the law to administer justice. *Id.*; *In re Chicago, Milwaukee, St. Paul & Pac. R.R. Co.*, 791 F.2d 524, 528 (7th Cir. 1986). Justice Story states that if a Court of Equity in England truly had boundless equitable jurisdiction, then "it would literally place the whole rights and property of the community under the arbitrary will of the judge." 1 Commentaries on Equity Jurisprudence § 19 at 21. He further emphasizes that personal views of equity should not empower the individual adjudicator in his pursuit of what constitutes a fair result to employ unauthorized procedures or remedies not contemplated by the framers of the Constitution or by Congress in their adoption of a particular statute. Likewise, the District Court in this case should not have the power to order substantive consolidation merely because it appears a fair solution in the interest of equity, absent some statutory or constitutional authorization.

This Court has not departed, in over two hundred years, from the view that courts are limited to those equitable remedies available in 1789 at the English Court of Chancery. Clearly, this case does not merit such a departure. This Court should lend credence to both the legislative intent of the authors of the Judiciary Act of 1789 and the numerous preceding members of this Court who have interpreted the equitable jurisdiction of the federal courts as subject to strict limitations.

Congress intended to vest in the federal courts only those powers that existed at English common law in the Court of Chancery at the time of enactment of the statute. *Grupo Mexicano de Desarrollo*, 527 U.S. at 318; *Atlas Life Ins. Co. v. W.I. S., Inc.*, 306 U.S. 563, 568 (1939). Only Congress is authorized to expand those powers by statute, which they did not elect to do with respect to substantive consolidation in Title 11 of the United States Code. *Grupo Mexicano de Desarrollo*, 527 U.S. at 322. Historical precedent dictates that this Court adhere to the boundaries of the federal courts' equitable power, and those boundaries clearly preclude substantive consolidation of the bankruptcy estates of ACME, TAPCO, and CAPCO.

2. Grupo Mexicano solidified the limitation on federal courts' equitable powers.

Allowing substantive consolidation in this case would render this Court's decision in *Grupo Mexicano* a nullity. This Court directly addressed the limited jurisdiction of the federal courts in a bankruptcy context in that recent case. 527 U.S. 308. In *Grupo Mexicano*, this Court determined that federal courts lacked the jurisdiction to issue a preliminary injunction against the bankrupt petitioner Grupo Mexicano de Desarrollo, a toll road operator, to enjoin the organization from disposing of or transferring any assets. *Id.* In recognizing the long-standing precedent of limiting the equitable powers of federal courts, Justice Scalia wrote, ". . . the equity jurisdiction of the federal courts is the jurisdiction in equity exercised by the High Court of Chancery in England at the time of the adoption of the Constitution and the enactment of the original Judiciary Act, 1789." *Id.* at 318. The *Grupo Mexicano* decision plainly limited the bankruptcy remedial powers of federal courts sitting in equity to those remedies and powers that existed in bankruptcy in the English Court of Chancery in 1789. This Court flatly declined to extend the equitable power of the courts to include ordering a preliminary injunction, a remedy that did not exist until 1975 at the Court of Chancery

and in the United States. *Id.* at 327.

In fact, this Court expressly disclaimed any judicial authority to employ new remedies not available at the Court of Chancery. *Grupo Mexicano* held that where there are new conditions that necessitate a departure from past practice, “Congress is in a much better position than we both to perceive them and to design the appropriate remedy.” *Id.* at 322. The same reasoning applies here.

Because this Court has plainly declared that the powers of the courts in equity are only those available in 1789, the only way federal courts would be authorized to substantively consolidate debtors’ estates is if the English Courts of Chancery possessed the same power, or a functional equivalent, in 1789. However, substantive consolidation did not exist at the English Court of Chancery in 1789, and in fact did not emerge in the American judicial system until the twentieth century. J. Maxwell Tucker, *Grupo Mexicano and the Death of Substantive Consolidation*, 8 Am. Bankr. Inst. L. Rev. 427, 432. Accordingly, the District Court lacked the authority to order substantive consolidation in this case.

3. Substantive consolidation was not an equitable remedy available at Chancery in 1789, so federal courts may not employ the remedy under their general equitable powers.

Substantive consolidation was not a remedy available to the English Courts of Chancery in 1789, and therefore the District Court acted without authority in ordering substantive consolidation of ACME, CAPCO, and TAPCO. *Id.* (citing 1 William Blackstone, Commentaries 269 (1st ed. 1765) and Edward V. Robinson, *The Holding Corporation – I*, 18 Yale Rev. 390, 400-07). Federal courts in the United States developed the remedy nearly 150 years after the passing of the Judiciary Act. Substantive consolidation is simply a judicially created solution endorsed by a few courts in the twentieth century based upon “inherent” equitable powers they did not actually possess.

- a. English Courts of Chancery did not employ the equitable remedy of substantive consolidation in any bankruptcy proceeding.

Substantive consolidation of the debtors' estates in this case does not fall within the court's equitable jurisdiction, as the remedy was not used until over 150 years after the passage of the Judiciary Act. Historical perusal of bankruptcy laws in England shows that substantive consolidation almost certainly was not a remedy at the English Court of Chancery at that time. The first bankruptcy laws passed in England in the sixteenth, seventeenth, and eighteenth centuries were available only to merchant traders, and were decidedly pro-creditor regulations. Charles Jordan Tabb, *The History of the Bankruptcy Laws in the United States*, 3 Am. Bankr. Inst. L. Rev. 5, 8. In fact, only creditors could place a debtor in bankruptcy, a feature which transferred into American bankruptcy law with the passing of the first Bankruptcy Code of 1800. *Id.* at 14.

Furthermore, the corporate structures of parent and subsidiary did not come into existence until the twentieth century. Edward V. Robinson, *The Holding Corporation – II*, 19 Yale Rev. 13, 29. This demonstrates that Courts of Chancery likely did not even contemplate substantive consolidation as an aid to the corporate debtor or in the context of combining corporate assets. The academic research in this area supports the idea that the Courts of Chancery did not employ the remedial power of substantive consolidation. *Id.*; Tabb, *supra* at 5; Tucker, *supra* 427 n. 92. Several contemporary scholars acknowledged that the remedy of substantive consolidation likely was not available at Chancery in 1789, basing their assertions primarily on the corporate structures in existence at the time. Tucker, *supra* at 442-43, n. 89. Since the remedy did not exist at the Court of Chancery, the order in this case to substantively consolidate ACME, TAPCO, and CAPCO has no basis in the general equitable powers of the courts.

- b. Substantive consolidation is a twentieth century product of judicial

convenience with no substantial legal basis.

The District Court's alleged authority to substantively consolidate in this case rests only upon judicial invention. Long after the passing of the Judiciary Act of 1789, federal courts came up with substantive consolidation of multiple entities as a preventive measure to combat fraudulent conveyances once corporate America began evolving into its present, multiple holding structure. Courts of the United States did not use substantive consolidation in bankruptcy until well into the twentieth century, beginning with *Soviero v. Franklin Nat'l Bank of Long Island* and *Chem. Bank N. Y. Trust Co. v. Kheel*. 328 F.2d 446 (2d Cir. 1964); 369 F.2d 845 (2d Cir. 1966). The *Soviero* court justified its use of substantive consolidation by pointing to the common ownership and interests in all of the corporations, because recognizing the entities as separate organizations would result in injustice to the creditors. *Soviero*, 328 F.2d at 448. The court cites no statutory authority or constitutional basis for this power, other than to reference "instrumentality rule" cases such as *Fish v. East* and *Stone v. Eacho*, which address piercing the corporate veil in bankruptcy, not substantive consolidation. 114 F.2d 177 (10th Cir. 1940); 127 F.2d 284 (4th Cir. 1942).

But courts continued to adopt the remedy, relying on baseless language in *Soviero* to substantiate their holdings. The Second Circuit later in *Kheel* relied on *Soviero* and the same cases cited therein, where there was no constitutional or Congressional basis for the authority to substantively consolidate. *Kheel*, 369 F.2d at 847. From that point, nearly 150 years after the Judiciary Act, courts began using substantive consolidation, relying only upon these two cases. Subsequent opinions even recognized that the remedy was merely "a product of judicial gloss." *In Re Augie/Restivo Baking Co. Ltd.*, 860 F.2d 515, 518 (2d Cir. 1988); *Fed. Deposit Ins. Corp. v. Colonial Realty Co.*, 966 F.2d 57, 59 (2d Cir. 1992). These courts fashioned substantive

consolidation as a remedy based upon seemingly relevant principles in the corporate context, citing each other as authority for a power that neither Congress nor the Constitution granted. This practice directly contradicts the purpose of Congress in limiting the power of the courts, and is the type of harm Justice Story predicted would occur if this nation allowed courts to substitute their judgment for that of the legislature.

Even though lower courts have premised many decisions upon this Court's ruling in *Sampsell v. Imperial Paper Color Corp.*, that case did not recognize a general power for federal courts to order substantive consolidation in bankruptcy cases. 313 U.S. 215 (1941). Rather, the *Sampsell* Court merely upheld the power of the bankruptcy court to reclaim for the estate assets that the debtor fraudulently transferred to a corporation he established for the sole purpose of removing those assets from his creditors' reach. *Id.* The decision rejected the argument that creditors of the transferee were entitled to priority against the transferor's assets. *Id.* at 220. *Sampsell* noted that courts have never furnished such protection to unsecured creditors of a transferee under fraudulent transfer law and were disinclined to protect the unsecured creditor who acted with knowledge of the fraudulent character of the corporation. *Id.* The *Sampsell* holding is inapposite to this case, a fact that further supports the idea that courts have no authority to order substantive consolidation under their general equitable powers, and that this power must be specifically assigned to the courts from a source outside common law; namely, an act of Congress.

B. There Is No Statutory Authorization for the District Court to Order Substantive Consolidation in This Case.

The Bankruptcy Code does not authorize federal courts to employ substantive consolidation as an equitable remedy in bankruptcy. The *Grupo Mexicano* decision emphasized that courts employing new remedies that did not exist in 1789 at the English Court of Chancery must have

Congressional authorization. 527 U.S. 308, 322 (1999). The district court in this case had no such authorization, as Congress has set forth only very specific, limited circumstances in which courts can employ substantive consolidation. See 11 U.S.C. §302(b) (2005); 11 U.S.C. §1123 (a)(5) (2005). Standard canons of statutory construction, as well as case law directly on point, indicate that the Bankruptcy Code confers no power on federal courts to exercise substantive consolidation in the manner used by the district court in the instant case.

1. Congress did not make the specific grant of power required to establish substantive consolidation as a new remedy.

No provision in the Bankruptcy Code meets the requirements which this Court proscribed as necessary to confer power to the federal courts to exercise new equitable remedies in bankruptcy. This Court requires Congress make a specific grant of jurisdiction in designing remedies not existing at the Court of Chancery. The *Grupo Mexicano* case stipulates that even where Congress confers a broad grant of power under a statute, if the issue involves an equitable remedy, the general principles of equity still apply. The brief filed by the United States as amicus curiae in the *Grupo Mexicano* case suggested that there was statutory support for the preliminary injunction issued in that case, relying on the broad powers of the Court under the All Writs Act. Brief for United States as Amicus Curiae Supporting Respondents at 18, *Grupo Mexicano de Desarrollo, S.A. v. Alliance Bond Fund, Inc.*, 527 U.S. 308 (1999) (No. 98–231), 1999 WL 86498. But this Court expressly stated that a general grant of power under a statute like the All Writs Act is defined and limited by those traditional principles of equity. 527 U.S. at 326, n. 8.

Even where Congress has expressly conferred broad powers upon the court through statutory language, the general principles of equity limit those powers. Thus, the broadest grant of power within Title 11, that found in Section 105(a), is not without boundaries. Though 105(a) affords the

courts some flexibility and discretion in administering bankruptcy proceedings, *Grupo Mexicano* prevents reading into the provision an implicit, general authorization for substantive consolidation. Rather, according to *Grupo Mexicano*, Congress must expressly and specifically grant the courts authority to substantively consolidate corporate entities. 527 U.S. at 326, n. 8. However, Congress has made no such allotment of power, and the district court in this case operated outside its jurisdictional bounds in ordering substantive consolidation of these estates.

2. The courts' powers under Section 105(a) do not include the use of substantive consolidation.

This Court should not construe Section 105(a) as conferring a general power to substantively consolidate debtors' estates. The rules of statutory interpretation show that Congress did not grant courts unlimited jurisdiction under Title 11. In construing statutes, this Court begins with the language of the statute and asks whether Congress has spoken on the subject. If the intent of Congress is clear, then the analysis is over, for the court must give effect to the unambiguously expressed intent of the legislative body. *Desert Palace Inc. v. Costa*, 539 U.S. 90, 98 (2003); *Hartford Underwriters Ins. Co. v. Union Planters Bank*, 530 U.S. 1, 6 (2000); *Robinson v. Shell Oil Co.*, 519 U.S. 337, 340-41 (1997). Furthermore, the Court should presume that the legislature says in a statute what it means and means in a statute what it says there. *Conn. Nat'l. Bank v. Germain*, 503 U.S. 249, 253-54 (1992). These canons of construction, when applied to Section 105(a) of Title 11, clearly limit its applicability to the confines of the Bankruptcy Code. Therefore, the court may not enter an order such as that sought by Petitioner unless another provision of the Code actually authorizes it.

Section 105(a) reads: "The court may issue any order, process, or judgment that is necessary or appropriate to carry out the provisions of this title." 11 U.S.C. § 105(a) (2005). The statute

confers broad powers to the court in the beginning of the clause, but the end of the sentence plainly confines those actions to a provision within the Code. Congress expressly included “provisions of this title” in the section. Therefore, Section 105(a) only gives broad powers with respect to implementing other specific sections of the Code.

Additionally, courts should interpret a statute in such a manner that every word has operative effect. *United States v. Nordic Village Inc.*, 503 U.S. 30, 36–37 (1992). To read Section 105(a) as a broad grant of unlimited jurisdiction would render “the provisions of this title” clause and other provisions of Title 11 inoperative. Such an interpretation would violate key canons of construction and substitute the judiciary’s reading for the intent of Congress.

Applicable case law restricts application of Section 105(a) to the substantive provisions of the Bankruptcy Code; it is not a free-standing equitable power. When confronted with this very question of interpretation, this Court and numerous lower courts held that no provision of Title 11 confers an independent basis for broad equitable powers upon courts in bankruptcy proceedings. *In re Dairy Mart Convenience Stores, Inc.*, 351 F.3d 86, 92 (2d Cir. 2003); *In re Haber Oil Co.*, 12 F.3d 426, 442-43 (5th Cir. 1994); *Disch v. Rasmussen*, 417 F.3d 769, 777 (2005). In *Norwest Bank Worthington v. Ahlers*, this Court concluded that the bankruptcy proceedings’ status as proceedings in equity did not preclude application of the absolute priority rule to the bankrupt’s case as required by the Code. 485 U.S. 197, 209 (1988). This Court rejected the argument that a “fair and equitable” reorganization plan could be executed without applying the absolute priority rule, and held that the equitable powers of the courts in bankruptcy “must and can only be exercised within the confines of the Bankruptcy Code.” *Id.* at 206. This Court in *Norwest Bank* expressly limited the equity jurisdiction of the courts in bankruptcy proceedings to the provisions of Title 11, which

do not include authority to order substantive consolidation of the type employed in this case. *Id.*

Several lower court opinions followed suit in recognizing that the intent of Section 105(a) was to confine the general powers of the bankruptcy court in issuing orders, processes, and judgments to the parameters of Title 11. Multiple holdings from the Second, Fifth, and Seventh Circuits unmistakably restrict the jurisdiction granted under Section 105(a) to compliance with some specific provision within the Bankruptcy Code. *In re Dairy Mart*, 351 F.3d at 92 (holding that “carrying out the provisions [of this title]” suggests an exercise of Section 105 power must be tied to another Code provision and not “merely to a general bankruptcy concept or objective”); *In re Haber Oil*, 12 F.3d at 442-43 (stating that even the broad powers of the courts to fashion equitable remedies must be exercised only within the confines of Title 11); *In re Fesco Plastics*, 996 F.2d 152 (7th Cir. 1993) (providing that a court may use equitable powers only as a means to fulfill some specific Code provision).

Nor does Section 105(a) constitute a roving commission for courts to do equity in bankruptcy. *United States v. Sutton*, 786 F.2d 1305, 1308 (5th Cir. 1986). The basis for many of these holdings, as explained in *Disch v. Rasmussen*, is avoiding the risk of rendering particularized restrictions in other parts of the Code ineffective by allowing court to fall back on the residual equitable authority under Section 105(a). 417 F.3d 769, 777 (7th Cir. 2005). Courts should not read the statute as affording judges free reign to redistribute rights according to personal views of justice and equity, “however enlightened those views may be.” *Id.* (quoting *In re Chicago, Milwaukee, St. Paul & Pac. R.R. Co.*, 791 F.2d 524, 528 (7th Cir. 1986)). Nor should the courts use the equitable power in Section 105(a) to circumvent the Code. *Id.* Lower courts have interpreted 105(a) as a specific grant of power meant to supplement and further the substantive provisions of Title 11;

accordingly, it does not supply a basis for the district court's order in this case.

3. The Bankruptcy Code contains no other provision to authorize the order for substantive consolidation in this case.

There is no express authority for substantive consolidation anywhere in the Bankruptcy Code, and thus no lawful foundation for the district court's order to substantively consolidate in the present case. *See Fed. Deposit Ins. Corp. v. Colonial Realty Co.*, 966 F.2d 57, 59 (2d Cir. 1992); *In re Bonham*, 229 F.3d 750, 763 (9th Cir. 2000). Courts have explicitly recognized the absence of such statutory authority, deeming substantive consolidation solely a "product of judicial gloss." *Fed. Deposit Ins. Corp.*, 966 F.2d at 59; *In re Augie/Restivo Baking Co.*, 860 F.2d 515, 518 (2d Cir. 1988). Furthermore, when a specific Bankruptcy Code section addresses an issue, a court may not employ its equitable powers to achieve a result not contemplated by the Code. *In re Fesco Plastics Corp.*, 996 F.2d 152, 154 (7th Cir. 1993).

The Bankruptcy Code alludes to substantive consolidation only three times, and in a very limited context in those instances: Bankruptcy Rule 1015, Section 302(b) dealing with married debtors who file joint bankruptcy petitions, and Section 1123(a)(5) regarding substantive consolidation in the context of a reorganization plan. Fed. R. Bankr. Proc. 1015; 11 U.S.C. § 302(b) (2005); 11 U.S.C. §1123 (a)(5) (2005). There is no provision that grants a general power to substantively consolidate corporate debtors' estates in the name of economic or judicial expediency. These specific provisions are evidence that Congress contemplated the use of substantive consolidation only in connection with joint, married debtors or when included in a plan of reorganization.

Congress specifically disclaimed authorization for substantive consolidation in Rule 1015. The note to Bankruptcy Rule 1015 reads, "this rule does not deal with the consolidation of cases

involving two or more separate debtors. . .Consolidation, as distinguished from joint administration, is neither authorized nor prohibited by this rule . . .” Fed. R. Bankr. Proc. 1015. Congress expressly states that this rule should not serve as a license to exercise substantive consolidation, and actually declines to authorize use of the remedy. Therefore, the Court cannot rely upon Rule 1015 to supplement Section 105(a) and permit substantive consolidation in this case.

Section 302(b) provides that “after the commencement of a joint case, the court shall determine the extent, if any, to which the debtors’ estates shall be consolidated.” 11 U.S.C. § 302(b) (2005). Congress contemplated consolidation of individual estates in the limited circumstance of marriage and joint filing—a situation that has no relevance in the case of ACME.

Finally, Section 1123(a)(5) cannot supplement Section 105(a) to authorize substantive consolidation in this case. 1123(a)(5) is the only provision that mentions substantive consolidation in a corporate context; it deals with the remedy exclusively in the framework of a reorganization plan. “Notwithstanding any otherwise applicable non-bankruptcy law, a plan shall—provide adequate means for the plan’s implementation, such as . . . merger or consolidation of the debtor with one or more persons.” 11 U.S.C. § 1123 (a)(5) (2005). In this case, substantive consolidation was not employed as part of a formal plan of reorganization; Section 1123 does not apply.

These provisions demonstrate that Congress did contemplate substantive consolidation in a few circumstances. Since no provision in the Code authorizes substantive consolidation in this case, this Court should determine that the district court operated outside its lawful jurisdiction in issuing the order for substantive consolidation of ACME, TAPCO, and CAPCO.

C. Even If the Equitable Jurisdiction of the Federal Courts Includes the Authority to Order Substantive Consolidation, That Power Should Not Be Exercised in this Case.

Even if this Court determines that federal courts do have the power to order substantive

consolidation, this Court should not allow substantive consolidation in this case. The fundamental purpose of substantive consolidation is to ensure the equitable treatment of all creditors. *Eastgroup Properties v. S. Motel Assoc.*, 935 F.2d 245, 248 (11th Cir. 1991). Even those courts that have employed substantive consolidation have recognized that it is appropriate only in very limited circumstances. Because substantive consolidation is “no mere procedural device, but a measure vitally affecting [the] substantive rights” of the parties involved, it should be used only sparingly. *In re Continental Vending Machine Corp.*, 517 F.2d 997, 1001 (2d Cir. 1975). This case is not a situation in which substantive consolidation is appropriate.

1. Courts have authorized substantive consolidation only after conducting a balancing test.

Substantive consolidation is not appropriate where consolidation would prejudice or defeat the claim of any creditor. Courts have developed a nuanced framework for using substantive consolidation only if the case meets certain conditions. *See generally In re Auto-Train Corp.*, 810 F.2d 270 (D.C. Cir. 1987). Where a party objecting to the consolidation proves it relied on the separate credit of one of the entities to be consolidated, courts have not allowed substantive consolidation where the party would be prejudiced by that consolidation. *See, e.g., In re Flora Mir Candy Corp.*, 432 F.2d 1060, 1062–63 (2d Cir. 1970); *In re Auto-Train Corp.*, 810 F.2d at 276; *In re Continental Vending Mach. Corp.*, 517 F.2d at 1001 (overruling use of substantive consolidation and holding that courts should use the measure sparingly due to the possibility of unfair treatment of creditors who have dealt solely with the corporation operating at a surplus as opposed to those creditors who have dealt with a deficient entity). After applying this framework to the instant case, this Court should determine that substantive consolidation is not appropriate here.

2. This case fails to meet the test for substantive consolidation.

This case fails to meet the test for substantive consolidation for several reasons. Most importantly, allowing substantive consolidation in this case would undercut the sole purpose of the measure: to ensure equitable treatment of all creditors. Courts below have declared substantive consolidation inequitable where it diminishes the claim of even one creditor. *In re Flora Mir Candy Corp.*, 432 F.2d at 1062-63. To allow substantive consolidation in this case would diminish significantly the recovery to which Respondent is legally entitled. Combining the assets of a financially viable entity with significantly weaker organizations will dilute the stronger entity's funds. The record in this case indicates that CAPCO continues to realize strong profits in the production of calcium chloride, while the other entities have suffered financial hardship. (Record at 5). Even more importantly, the dissent in the court of appeals recognized that in the absence of substantive consolidation, general unsecured creditors of CAPCO would receive 65 to 75 cents on the dollar. (R. at 22). Substantive consolidation would surely dilute Respondent's claim, as TAPCO's resources will generate only about seven cents on the dollar for its unsecured creditors. (R. at 22). This could potentially slash CAPCO's payout rate—and Respondent's damages—by over fifty percent. Because consolidating the debtors' assets would prejudice Respondent and the other discrimination plaintiffs, this case is not one of the few where substantive consolidation would be appropriate.

Furthermore, Respondent and the other discrimination plaintiffs, as employees of CAPCO, have relied upon the separate existence and credit of CAPCO in pursuing their claim. As an employee of CAPCO, Respondent is doubtlessly familiar with the financial vitality of CAPCO. TAPCO and CAPCO manufacture two completely different, unrelated products in two different parts of the country; substantive consolidation of these debtors' estates would certainly prejudicially

reduce Respondent's recovery.

Because the circumstances of this case fail to merit the application of substantive consolidation, this Court should not permit substantive consolidation of ACME, TAPCO, and CAPCO in this case. To do so would undermine the sole purpose of substantive consolidation, to ensure equitable distribution among all creditors. Furthermore, the Court in effect would be merely slapping CAPCO's hand, instead of forcing the company to endure the consequences of fostering discriminatory work environments and employment policies. A reversal of the court of appeals' decision would allow corporate debtors to ameliorate or altogether escape the consequences of wrongdoing by invoking the parent/subsidiary relationship as an excuse for consolidating assets.

II. THE BANKRUPTCY CODE DOES NOT PERMIT THE SALE OF ASSETS FREE AND CLEAR OF SUCCESSOR LIABILITY CLAIMS UNDER SECTION 363(F).

Section 363(f) of Title 11 of the United States Code provides that a trustee may sell property that falls within the section free and clear of "any interest in such property" to an entity other than the estate. 11 U.S.C. § 363(f) (2005). ACME seeks to include Respondent's employment discrimination claim as an "interest in property" under Section 363(f), so that it may sell its assets to SOUSA without any successor liability arising from the sale. Authorizing such an interpretation, and allowing businesses to circumvent the Code's requirements under this section, will set a dangerous precedent of depriving successor liability claimants of their chance for an adequate recovery.

When construing a statute, the sole function of courts is to enforce it using the language in

which it is framed. *Caminetti v. United States*, 242 U.S. 470, 485 (1917). Because Congress specifically excludes “claims” from Section 363(f), while intentionally including the term in other sections, the plain meaning of Section 363(f) dictates that “claims” must not come within the section’s scope. *Berge v. Sweet*, 37 B.R. 705, 708 (Bankr. W.D. Wis. 1983). The tendency of some courts to include “claims” unduly punishes unsecured creditors by depriving them of the protections that Congress intended to provide for them. Further, allowing “claims” to be stripped from assets under Section 363(f) contravenes the underlying purpose of successor liability for claims such as Respondent’s, which is to ensure that an employee’s statutory rights are not vitiated by a sudden change in an employer’s business. *Rojas v. TK Communications*, 87 F.3d 745, 750 (5th Cir. 1996).

More specifically, “interests in such property,” as used in Section 363(f), cannot include unsecured, in personam claims such as Respondent’s. Section 363(f) applies only to in rem interests that have already attached to the property. *Fairchild Aircraft Corp. v. Campbell*, 184 B.R. 910, 918 (Bankr. W.D. Tex. 1995). Bankruptcy does not give an unsecured creditor any interest in the particular property of the debtor. *Id.* at 919. Because an unsecured creditor does not have an in rem interest in the property of the debtor, the district court may not allow Respondent’s discrimination claim to be stripped in a free and clear asset sale under Section 363(f). Doing so would directly contradict the “adequate protection” provisions in Sections 363(e) and (b). Adequate protection applies only to secured creditors. Allowing a sale of assets free of a “claim” under 363(f) needlessly blurs the Code’s distinction between secured and unsecured creditors.

ACME may not sell its assets free and clear of Respondent’s employment discrimination claim under Section 363(f) of the Bankruptcy Code for three reasons. First, there is no basis in the Bankruptcy Code for interpreting “claims,” such as Respondent’s, to mean “interests,” as used in

363(f). Additionally, unsecured claimants, such as Respondent, have no in rem “interest in property” that could be disregarded in a free and clear sale under the section. Finally, allowing debtors to strip claims like Respondent’s under 363(f) undermines overwhelming policy considerations, while contravening requirements Congress imposed for asset sales of this nature.

A. “Claims” Are Not “Interests” Under Title 11, and Therefore They Are Not Subject to a Free and Clear Asset Sale Under Section 363(f).

“Claims” such as Respondent’s must not be the “interests” referred to in 363(f) for three reasons. First, the plain meaning of the language of 363(f), as well as the intentional inclusion of the term “claims” in various other provisions of the Code, demonstrate Congress’ intentional exclusion of “claims” in 363(f). Second, Congress intended free and clear asset sales to occur only under approved plans of reorganization; allowing debtors to make free and clear asset sales outside of the reorganization context deprives creditors, like Respondent, of the protections that Congress built into the reorganization process. Finally, while a few courts have interpreted 363(f) to include “claims” as “interests,” this misinterpretation renders an important phrase in the statute inoperative.

1. “Claims” are specifically excluded from Section 363(f).

“Claims” are not the same as “interests” under 363(f). A statute’s plain and ordinary meaning is the proper place to begin in its interpretation. *United States v. Ron Pair Enter. Inc.*, 489 U.S. 235, 249 (1989). If a statute’s meaning is plain, the court’s effort to interpret the statute should end at the plain and ordinary interpretation. *Caminetti v. United States*, 242 U.S. at 485. 363(f) says that a trustee may sell property free and clear of “any interest in such property.” 11 U.S.C. § 363(f) (2005). The language of 363(f) plainly excludes “claims.” The plain meaning of that section demonstrates that pre-petition claims such as Respondent’s are not intended by Congress to be subject to a free and clear asset sale under this section. Further, Congress specifically included the

term “claims” in other code sections where it intended to include them. The significance of the exclusion of “claims” from 363(f) must be recognized as evidence that claims like Respondent’s are not to be stripped in a sale of assets.

However, even beyond a plain reading of 363(f), there is ample evidence of Congressional intent to exclude of “claims” from “interests in such property” under this section. *Berge v. Sweet*, 37 B.R. 705, 708 (Bankr. W.D. Wis. 1983). The exclusion of “claims” from 363(f) is an intentional exclusion by Congress because elsewhere in the Bankruptcy Code, Congress specifically mentions the term “claims” when it wishes to include them in a section. For example, Section 501 mentions “claims and interests” as two separate items that must be filed in a bankruptcy proceeding, while Section 502 also expressly distinguishes “claims” and “interests” when referring to their allowance. 11 U.S.C. §§ 501, 502 (2005).

While the term “and” may suggest similarity, the term “or” suggests disjunction. *Hawes Org. Inc. v. Basic Distribution Corp.*, 957 F.2d 239, 244 (6th Cir. 1992). Section 1111 of the Code refers to “claims or interests.” 11 U.S.C. § 1111 (2005). Similarly, the classification provision, Section 1122, refers to “claims or interests,” as though they are completely separate items 11 U.S.C. § 1122 (2005). Various other Code sections refer to “claims or interests” as two distinct concepts. (See e.g.: 11 U.S.C. §§ 510, 541, 1123, 1124, 1125, 1126, 1227, 1141, 1145 (2005). In each section, Congress specifically differentiates claims and interests by referring to them disjunctively. In addition, Congress uses the term “claims” when seeking to include them.

On the other hand, Section 363(f) includes only the term “interests.” Because “claims” and “interests” have taken on distinct meanings throughout the Bankruptcy Code, a “claim” must not be treated as an “interest” in 363(f). Congress did not intend for a sale of assets to be consummated

free of claims, such as those held by Respondent.

2. Equating “claims” with “interests” circumvents the protections that Congress built into the reorganization plan process for creditors.

“Claims” are not “interests” under Section 363(f) because this interpretation results in a deprivation to Respondent and similarly situated creditors of the protections that Congress built into the reorganization plan process. A narrow reading of 363(f) more accurately reflects Congressional intent in this area. Further, recognizing that Respondent’s claim is not an “interest” under 363(f) does not prevent ACME’s sale of assets to SOUSA from taking place. The sale is still viable under such an interpretation.

First, claims such as Respondent’s are not “interests” under 363(f) because equating “claims” and “interests” deprives Respondent of the protections that Congress built into the reorganization plan process. Debtors must not use Section 363 to sidestep the Congressional protection afforded to creditors under a plan of reorganization. *In re Continental Airlines Inc.*, 780 F.2d 1223, 1227 (5th Cir. 1986). While Congress allows debtors, in other Code provisions, to engage in asset sales that transfer property free and clear of creditor interests and claims, these sales are normally only allowed as part of a process that has already incorporated protections for those creditors who are adversely affected by the sale.

For example, in the confirmation proceeding, Section 1141 allows property to transfer free and clear of “claims and interests.” 11 U.S.C. § 1141 (2005). However, this section also requires extensive disclosure and multiple hearings before allowing a free and clear confirmation of the assets. Under 1141, creditors are thus afforded protection, and given an opportunity to voice objections. Conversely, Section 363 only requires one hearing and minimal notice before allowing assets to transfer free and clear of “interests in property.” A trustee need only give twenty days’

notice and may choose the method of sale. Bankr. R. §§ 2002(a), 6004(f) (2005). Objections to a sale and alternative bidders are rarely heard by a court in a 363(f) proceeding. By allowing “claims” to equate to “interests,” debtors may obtain a free and clear transfer under 363(f), using its less stringent requirements, and circumventing the protections that Congress intended to afford the “claims” of creditors. As a result, allowing “claims” to fall within 363(f)’s scope leaves Respondent and similar creditors with little or no protection.

On the other hand, a narrow interpretation of Section 363, disallowing sales of assets free of “claims,” complies with Congress’s rationale in creating different requirements and procedures for Section 1141 and Section 363. Likewise, because 363 requires only minimal notice and a hearing, it follows that courts should interpret the interests it includes more narrowly than that of other sections such as 1141 and their more substantial requirements. ACME must not be allowed to sell its assets free and clear of Respondent’s claims, and thereby circumvent these mandated protections.

Finally, recognizing that Respondent’s claim does not come within Section 363 does not prevent ACME from carrying out its intended sale to SOUSA. Although SOUSA wants to buy the assets free and clear of any successor liability, it will still purchase the assets if the price is reduced by the amount of the claim, or if a sufficient portion of the sale proceeds are held in escrow to pay those claims as they are resolved (R. at 9). Additionally, ACME may still seek a sale of assets under other provisions of the code, after complying with their requirements under the plan confirmation process. 11 U.S.C. §§ 1123, 1227, 1141 (2005).

3. Equating “claims” and “interests” in Section 363(f) renders the phrase “in such property” mere surplusage.

Judicial misinterpretation of Section 363(f) creates a nullity in part of the statute. In reviewing a statute, every word must be given effect and meaning, and no part of the statute should

be held meaningless. *In re Wandrey*, 334 B.R. 427, 427 (Bankr. N.D. Ind. 2005). While some courts hold that “claims” may be discarded as “interests” under 363(f), this interpretation renders the language “in such property” a nullity. *Fairchild Aircraft Corp. v. Campbell*, 184 B.R. 910, 918 (Bankr. W.D. Tex. 1995). Congress included the phrase “in such property” to limit interests that could transfer in a 363(f) sale of assets. Thus, judicial inclusion of “claims” under 363(f) defies this common canon of statutory construction and in effect, causes the express statutory phrase “in such property,” that further defines and describes the interests contemplated by Section 363, to become inoperative. *Id.* Since Congress sought to limit the interests that can transfer in a free and clear asset sale only to those “in such property,” this Court must not interpret Section 363 to allow assets to be sold free of claims such as Respondents.

In conclusion, Section 363(f)’s plain meaning, as well as other common canons of construction, demonstrate that Congress did not intend for “claims” to be discarded in a free and clear asset sale under Section 363. Further, the court must not strip Respondent and similar creditors of the protections that Congress expressly provided them throughout Title 11. Finally, interpreting 363(f) as contemplating “claims” renders part of 363(f) inoperative, even though every phrase in a statute must be given meaning if possible. This Court must hold that ACME may not sell CAPCO’s assets to SOUSA free and clear of Respondent’s claims.

B. Section 363(f)’s “Interests in Property” Does Not Include Unsecured Claims Such as Respondent’s.

ACME may not sell its assets free and clear of Respondent’s claims because “interests in such property” as used in Section 363(f) does not include unsecured claims. This must be true for two important reasons. First, “interest in such property” refers only to in rem interests and is not intended to extinguish such in personam claims as the unsecured claim held by Respondent. Second,

“interests in such property” that may be stripped in a 363(f) asset sale must receive adequate protection as mandated by Section 363(e). Because adequate protection does not apply to unsecured claims, it follows that 363(f) must not apply to unsecured claims either.

1. 363(f)’s “interest in such property” refers only to in rem interests and does not extinguish in personam claims.

Section 363(f) applies only to in rem interests that have attached to the property to be sold. The section serves to allow a sale of assets free and clear of any interest “in such property” of the debtor. The phrase “in such property” defines the breadth of the interests that Congress sought to include in 363(f). *Id.* at 917. The phrase indicates that in rem interests are the only types of rights affected by this section. *Id.* at 918. Unsecured claimants hold only an in personam claim and not an “interest in such property” that may be stripped in a 363(f) sale of assets. *Id.* Without a bankruptcy action, an unsecured claim, including a successor liability claim, has no relationship to the debtor’s property. *Id.* at 919. As a result, these claims are not in rem claims against the debtor’s property, but merely claims for which the debtor is personally liable. “Bankruptcy gives an unsecured creditor, via the proof of the claim process, the functional equivalent of a judgment against the debtor’s estate, but does not give the creditor an interest in any particular property of the debtor.” *Id.* While claims may convert to secured claims by agreement or through the judgment process of non-bankruptcy law, until this happens, a claim is merely an unsecured claim, and cannot be characterized as an “interest in such property” as referred to in 363(f). Nathan F. Coco, *An Examination of Successor Liability in the Post-Bankruptcy Context*, 22 J. Corp. L. 345, 353.

The court in *Fairchild* rejected an asset purchaser’s argument that 363(f)’s “any interest in such property” encompassed not only in rem but also in personam claims. 184 B.R. at 918. In that case, Fairchild Incorporated purchased the assets of a bankruptcy debtor. Upon being sued under the

doctrine of successor liability, *Fairchild, Inc.* moved for summary judgment on the ground that the free and clear sale precluded its liability as a successor entity. While the court held for *Fairchild, Inc.* on other grounds, it unequivocally stated that these claims were incapable of being stripped in a free and clear asset sale because they were in personam claims, and that a free and clear asset sale can only apply to in rem interests in property. *Id.*

In light of *Fairchild*, ACME must not be permitted to sell CAPCO's assets free and clear of Respondent's claim. The employment discrimination claim is an in personam claim, because outside of the bankruptcy action, her unsecured claim has no relationship to any particular asset. Respondent's claim must follow ACME's sale of assets to SOUSA.

2. 363(f) cannot encompass Respondent's claim because such a claim is not afforded the requisite "adequate protection" of Section 363(e).

Section 363(f) cannot address Respondent's claim because this inclusion does not afford her claim the mandated "adequate protection" of Section 363(e). First, "adequate protection," as contemplated by 363(e), applies only to secured creditors, and not to unsecured creditors like Respondent. *See In re Ingle*, 91 B.R. 27, 28 (Bankr. E.D. Mich. 1988). Additionally, treating Respondent's "claim" as an "interest in such property" ignores the Bankruptcy Code's distinction between secured and unsecured creditors' interests in property.

363(e) entitles secured interests to "adequate protection" before a 363(f) sale. The concept of adequate protection is derived from Fifth Amendment protections of property rights. *Wright v Union Central Life*, 311 U.S. 273 (1940); *Louisville Joint Stock Land Bank v. Radford*, 295 U.S. 555 (1935). Throughout the code, "adequate protection" is ensured for secured creditors, or creditors with an "interest in property," or in rem interest. *See, e.g.*, 11 U.S.C. §§ 1205, 542, 552, 507, 1326, 1225, 1112, 506, 503, 521, 553, 724, 1111, 1124, 1322, 1325, 1221, 1122, 554, 1327, 922 (2005).

“The purpose of adequate protection is to compensate a secured creditor for any depreciation of collateral between the time that they move for relief from the stay and confirmation.” *In re Cook*, 205 B.R. 437, 441 (Bankr. N.D. Fla. 1997). Creditors being subjected to a free and clear asset sale under Section 363(f) are entitled to “adequate protection” under 363(e). It follows that 363(f) can only apply to secured creditors, lest the protections set forth in 363(e) be violated. Because Respondent is an unsecured creditor who will not (and indeed cannot) receive adequate protection, 363(f) cannot apply to her claim.

Further, allowing unsecured creditors to fall within Section 363(f) blurs the distinction made by the Bankruptcy Code between secured and unsecured creditors' interests in the estate. *Fairchild Aircraft Corp. v. Campbell*, 184 B.R. 910, 918 (Bankr. W.D. Tex. 1995). Even though all creditors have an “interest” in the estate, they do not have the “interest in property” that would be cognizable under, for example, Section 506(a). (*Id.*, where creditors are specifically enumerated as having “liens on such property”). Otherwise, the distinction made there between secured and unsecured claims is useless. *Id.* If unsecured creditors had an “interest in property” that could be stripped off under a 363(f) asset sale, then these creditors would be entitled to adequate protection of their interests. Again, such a conclusion ignores the distinctions drawn in the Code. 11 U.S.C. § 362(e) (2005); *Fairchild*, 184 B.R. at 918. Interpretation of Section 363 must recognize the difference in the treatment of secured and unsecured claims; accordingly, Respondent’s claim must not be characterized as an “interest in property.”

C. Allowing Section 363(f) to Include Claims Like Respondent’s Directly Undermines Congress’s Underlying Purposes for Chapter 11 and Successor Liability.

Respondent’s claim must not be subject to Section 363(f) because of the underlying purposes of this section as well as the Bankruptcy Code as a whole. Additionally, important policy

considerations are implicated in free and clear asset sales. First, the purpose of successor liability is circumvented if sales are allowed free of those claims. Additionally, judicial allowance of free and clear asset sales transforms Chapter 11 from a facilitator of reorganization planning to a business forum for buying and selling assets. Finally, excluding Respondent's claim will not provide her with any favored status over other unsecured creditors of ACME.

1. The purpose of successor liability is undermined by allowing Section 363(f) to justify sales free and clear of claims such as Respondent's.

Allowing Section 363(f) to encompass an unsecured discrimination claim like Respondent's contradicts the important purpose of the successor liability doctrine. The doctrine of successor liability extends to claims asserted under Title VII of the Civil Rights Act. *Rojas v. TK Communications*, 87 F.3d 745, 750 (5th Cir. 1996). Successor liability arises in the context of employment discrimination cases where the assets of a defendant employer are transferred to another entity. *Id.* The purpose of the doctrine is to ensure that an employee's statutory rights are not vitiated by a sudden change in the employer's business. *Id.* The doctrine allows the aggrieved employee to enforce against the successor a claim he could have secured against the predecessor, the employer. If Respondent's discrimination claim is discarded pursuant to Section 363(f), her statutory rights under the anti-discrimination statutes and Title VII can in no way be vindicated, and the rationales of both the anti-discrimination statutes and the doctrine of successor liability are ignored. In light of *Rojas*, Respondent's claim against CAPCO is enforceable against SOUSA, as the mere change in ownership cannot serve to eradicate her important Title VII discrimination claim. Consequently, Respondent's claim must not be taken away in a free and clear asset sale under 363(f).

2. Misinterpreting Section 363(f) turns Chapter 11 into a business forum for the

buying and selling of assets.

Judicial misinterpretation of Section 363(f) to include “claims” under “interests in such property” bypasses the original purpose of Chapter 11, reorganization planning, and creates a common forum for businesses to purchase and sell assets. Congress intended filings under Chapter 11 to produce debtor reorganization plans rather than preplan liquidations. H.R. Rep. No. 95-595 (1977). An improper interpretation of Section 363 results in businesses using it for pre-plan asset sales because of the minimal notice and hearing requirements of that section. Both Section 1123 and Section 1141 require more extensive disclosure and multiple hearings in order to carry out a post-plan sale. 11 U.S.C. §§ 1123, 1141 (2005). Objectors and alternative bidders are rarely heard in a 363 sale. As a result, many companies unnecessarily “throw” a case into bankruptcy merely to effect the sale of some asset of a business or division. Kuney, *supra* at 235.

“[The term] ‘[c]laim’ ought not do what is not possible in a [non-bankruptcy] court of law. It may not authorize bankruptcy courts to ride roughshod over due process and notions of fundamental fairness.” *Fairchild Aircraft Corp. v. Campbell*, 184 B.R. 910, 918 (Bankr. W.D. Tex. 1995). Yet, misinterpretation of 363(f) permits a conclusion that the procedural due process Congress intended for creditors faced with a free and clear asset sale is an unnecessary protection. Kuney, *supra* at 264. This Court must not allow Petitioner to sell CAPCO’s assets free and clear of Respondent’s claim, and thus intrude on Respondent’s due process rights and contradict Congressional intent.

3. Excluding Respondent’s claims from coverage under 363(f) does not provide her with favored status over other creditors.

The exclusion of Respondent’s claim from the result of a Section 363 sale does not provide her with any favored status over other unsecured creditors. Most unsecured creditors have already

been compensated in the form of interest payments or higher prices of goods in exchange for the risk that the predecessor might not repay them. *Musikiwamba v. Essi, Inc.*, 760 F.2d 740, 750 (6th Cir. 1985). Employees, on the other hand, are not compensated for the risk that their employer might discriminate against them. *Id.* Beginning from a position of disadvantage, Respondent is not elevated above other creditors when her claims survive a Section 363 sale of assets.

Allowing Respondent's claims to be stripped in a sale of assets directly contravenes the Congressional policy of eradicating the risk of employment discrimination. The risk of employment discrimination is not even decreased if employers who discriminate are permitted to dispose of an employee's source of recovery without compensating the injured employee. In order for Respondent's ability to recover under federal statute to be meaningful, Petitioner must not be allowed to sell its assets free and clear of her claim.

CONCLUSION

For the foregoing reasons, Respondent respectfully requests that this Court affirm the judgment of the Thirteenth Circuit Court of Appeals.

Respectfully submitted,

ATTORNEYS FOR THE RESPONDENT

CERTIFICATE OF SERVICE

I hereby certify that a true and correct copy of the foregoing Brief for the Respondent was mailed by certified mail, return receipt requested, to Counsel for the Petitioner on February 2, 2006.