

Pension Benefit Guaranty Corporation's Termination Premiums Constitute Dischargeable Pre-Petition Contingent Claims

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A. Introduction

In *Oneida Ltd. v. Pension Benefit Guaranty Corp.*, the U.S. Bankruptcy Court for the Southern District of New York addressed the issue of whether a debtor's liability for pension termination premiums ("DRA Premiums") constituted a pre-petition contingent "claim" and was, therefore, dischargeable pursuant to the debtor's reorganization plan confirmation. 383 B.R. 29, 32 (Bankr. S.D.N.Y. 2008). The Bankruptcy Court held that the debtor's liability for DRA premiums was a dischargeable pre-petition "claim" even though the pension termination occurs during the debtor's chapter 11 case. *Id.* at 32, 43.

The Bankruptcy Court based its holding on three determinations: (1) that DRA Premiums fell within Bankruptcy Code section 101(5)(A)'s definition of the term "claim"; (2) that the resulting "claim" arose pre-petition despite 29 U.S.C. § 1341(c)(2)(B), which provides that DRA Premiums shall not arise "until the date of discharge"; and (3) that the Deficit Reduction Act of 2005 ("DRA Amendment"), an amendment of the Employee Retirement Income Security Act ("ERISA"), did not present a "clear and manifest" intent of Congress to amend the Bankruptcy Code, a threshold issue that must be met before the Bankruptcy Court could consider the DRA Amendment's underlying policies. *Id.* at 36–38, 40–41.

The Bankruptcy Court dismissed the Pension Benefit Guaranty Corporation's ("PBGC") argument that DRA Premiums were not "claims." The PBGC had argued that DRA Premiums are not "claims" because, by statute, the PBGC's right to payment was not enforceable until Oneida's chapter 11 discharge or case dismissal. Dismissing this argument, the Bankruptcy Court held that DRA Premiums constituted pre-petition "classic contingent claim[s]." *Id.* at 38.

The decision is currently under appeal to the Second Circuit Court of Appeals. As of now, the Bankruptcy Court's *Oneida* decision is the first reported and only decision to consider whether DRA Premiums are "claims" under section 101(5)(A). However, case precedent provides guidance in assessing whether the Bankruptcy Court correctly decided *Oneida*.

Case precedent addresses whether a section 101(5)(A) "claim" exists and, if so, whether the "claim" arises pre- or post-petition. First, precedent instructs that whether a "claim" exists should be determined according to 101(5)(A)'s "text, history, and purpose." Next, precedent establishes three distinct tests to determine when a "claim" arises: (1) when a cause of action for a right to payment exists under non-bankruptcy law; (2) when events creating an eventual right to payment under non-bankruptcy law first begin; and (3) when events creating an eventual right to payment under non-bankruptcy law first begin, but only if the creditor-claimant "had some type of specific relationship with the debtor at that time." *Lemelle v. Universal Mfg. Corp.*, 18 F.3d 1268, 1275-76 (5th Cir. 1994). Last, precedent establishes that a court must determine whether a pre-petition "claim" exists before the court can consider non-bankruptcy law policies that may weigh against discharging liability.

Second Circuit precedent supports the Bankruptcy Court's *Oneida* decision. Under both the Second Circuit's variation of the third test as well as other circuits' variations, DRA Premiums would most likely face discharge. Additionally, the first test, the most generous of the

three to creditors, has been either rejected or narrowed. Thus, DRA Premiums will most likely remain dischargeable under chapter 11 pension terminations unless Congress amends the Bankruptcy Code.

B. DRA Premiums

DRA Premiums were added to the law by the DRA Amendment, which became effective only weeks before Oneida, a leading flatware manufacturer, filed chapter 11. *In re Oneida Ltd.*, 351 B.R. 79, 81 (Bankr. S.D.N.Y. 2006). DRA Premiums permit the PBGC to impose upon companies terminating defined-benefit pension plans a \$1,250 premium for each person who was a plan participant at the time of termination. 29 U.S.C. § 1341(c)(2)(A). Under subsection (B) of the DRA Amendment, DRA Premiums “shall not apply to [a termination] plan [that occurs during a bankruptcy reorganization] until the date of the discharge.” 29 U.S.C. 1341(c)(2)(B) (2006). However, Congress did not explicitly state in subsection (B) that DRA Premiums *cannot* be discharged in a chapter 11 proceeding. Thus, courts must consider whether DRA Premiums are dischargeable claims under the Bankruptcy Code.

1. Section 101(5)(A) Claims

In general, the term “claim” is considered broad in scope, evidenced by Bankruptcy Code section 101(5)(A)’s “text, history, and purpose.” *Johnson v. Home State Bank*, 501 U.S. 78, 83 (1991). First, section 101(5)(A)’s plain meaning dictates that all rights to payment contingent on the occurrence of a later event constitute “claims.” The section defines what constitutes a “claim.” A “claim” is defined as a “right to payment, whether or not such right is reduced to judgment, liquidated, unliquidated, fixed, *contingent*, matured, unmatured, disputed, undisputed, legal, equitable, secured, or unsecured.” 11 U.S.C. § 101(5)(A) (2006) (emphasis added).

Second, the section’s legislative history supports a broad interpretation: “Congress intended by [the section’s] language to adopt the broadest available definition of ‘claim.’” *Id.* See H.R. Rep. No. 95–595, at 309 (1977), U.S. Code Cong. & Admin. News at 6266 (1978) (“[The Code] contemplates that all legal obligations of the debtor . . . will be able to be dealt with in [a] bankruptcy case.”). Third, a broad reading of the term “claim” promotes bankruptcy law’s “fresh start” policy to leave debtors free from creditors’ interests, which supports a broad interpretation of “claim.” See *In re Quigley*, 383 B.R. 19, 25 (Bankr. S.D.N.Y. 2008).

Despite section 101(5)(A)’s broad scope, what constitutes a “claim” is “not infinite.” *LTV Steel v. Shalala (In re Chateaugay Corp.)*, 53 F.3d 478, 497 (2d Cir. 1995) (hereinafter, “*Chateaugay II*”). See *Bennett v. Bennett (In re Bennett)*, 175 B.R. 181, 183 (Bankr. E.D. Pa. 1994) (holding that an interest in a pension plan was not a claim without a secured court order determining the interest’s extent). For example, an interest is not a claim where the debtor does not withdraw from the pension, and thereby trigger liability, until after its plan confirmation. *CPT Holdings v. Indus. and Allied Union Employees Pension Plan*, 162 F.3d 405, 408–09 (6th Cir. 1998) (distinguishing not only cases where claims arose due to pre-petition termination but also claims that arose due to termination during bankruptcy proceedings). Further, section 101(5)(A)’s legislative history contains nothing to “suggest[] that Congress intended to discharge a creditor’s rights before the creditor knew or should have known that its rights existed.” *Jensen v. Jensen (In re Jensen)*, 995 F.2d 925, 930 (9th Cir. 1993).

2. Three Tests To Determine When A “Claim” Arises

“Claims” must arise pre-petition to be dischargeable pursuant to Bankruptcy Code section 1141. 11 U.S.C. § 1141(d)(1) (2006) (“Except as otherwise provided . . . , the confirmation of a plan discharges the debtor from any debt . . . that arose before the date of such

confirmation . . .”). *See Johnson*, 501 U.S. at 84 n.5 (clarifying that, under the Bankruptcy Code, the term “claim” is considered coextensive with the term “debt”). While section 523(a) of the Bankruptcy Code contains exceptions to the discharge of claims that arise pre-petition, these exceptions do not include DRA Premiums. Notably, section 523(a) was amended only a short while prior to the DRA Amendment’s enactment, evidence that the omission was intentional. *See Oneida*, 383 B.R. at 41 n.14.

Courts use three tests to determine when a section 101(5)(A) “claim” arises. *See Lemelle*, 18 F.3d at 1275–77. Under the first test, a “claim” arises when a cause of action for a right to payment exists under non-bankruptcy law. *Id.* at 1275. For example, in *Avellino & Bienes v. M. Frenville Co. (In re M. Frenville Co.)*, the claim at issue, an accounting firm’s non-contractual right to indemnity from a debtor, did not accrue until the indemnity-creating party filed suit. 744 F.2d 332, 337 (3d Cir. 1984). Thus, because the suit was filed post-petition, the “claim” was not dischargeable. *Id.* This first test is widely rejected for contravening the Supreme Court’s broad interpretation of section 101(5). *See, e.g., Watson v. Parker (In re Parker)*, 313 F.3d 1267, 1269–70 (10th Cir. 2002) (declining to follow *Frenville*’s “limiting definition of claim”).

Under the second test, a “claim” arises when events creating an eventual right to payment under non-bankruptcy law first begin. *Lemelle*, 18 F.3d at 1275. Here, unlike the first test, a “claim” can arise pre-petition even when some liability-creating elements are not satisfied until post-petition. *See Grady v. A.H. Robins Co., Inc.*, 839 F.2d 198, 202–03 (4th Cir. 1988). Thus, a “claim” can arise pre-petition when the creditor holds pre-petition rights “contingent” on a future event’s occurrence. *See Id.*

Courts implementing the second test rely on section 101(5)(A)’s express language, which includes “contingent” rights to payment. *See, e.g., In re Manville Forest Products Corp.*, 225

B.R. 862, 866 (Bankr. S.D.N.Y. 1998). These courts narrowly interpret the Supreme Court's statement in *Pennsylvania Department of Public Welfare v. Davenport* that a right to payment is "nothing more nor less than an enforceable obligation." 495 U.S. 552, 559 (1990), superseded on other grounds by Criminal Victims Protection Act of 1990, Pub. L. No. 101-581, § 3. These courts hold that *Davenport* does not require a *presently* enforceable obligation. See, e.g., *Pearl-Phil GMT (Far East) Ltd. v. Caldor Corp.*, 266 B.R. 575, 581 (Bankr. S.D.N.Y. 2001).

While the first and second tests differ, circuit courts employing both tests recognize that a "claim" may arise pre-petition even when jurisdictional prerequisites to filing a claim were not fulfilled until after the debtor's plan confirmation. See, e.g., *Kilbarr Corp. v. Gen. Servs. Admin. (In re Remington Rand Corp.)*, 836 F.2d 825, 826 (3d Cir. 1988). For example, in *McSherry v. Trans World Airlines, Inc.*, a discriminatory termination claim, a "claim" was dischargeable because it was based on actions that occurred before the former employee's company's plan confirmation. 81 F.3d 739, 740 (8th Cir. 1996). The "claim" did not arise later because the employee's "right to sue letter," which he received post-confirmation, was distinguished as a jurisdictional prerequisite. *Id.* at 741.

Under the third test, a "claim" arises when events creating an eventual right to payment under non-bankruptcy law first begin, but only if the creditor-claimant "had some type of specific relationship with the debtor at that time." *Lemelle*, 18 F.3d at 1276. This third, middle ground test's requisite "specific relationship" must begin pre-petition. *Id.* In a Second Circuit variation of the third test, a "specific relationship" may be proven when the relationship at issue "provides sufficient contemplation of contingencies based on pre-petition conduct." *United States v. LTV Corp. (In re Chateaugay Corp.)*, 944 F.2d 997, 1005 (2d Cir. 1991) (hereinafter, "*Chateaugay I*"). In another variation, a "specific relationship" may be proven through certain

factors: “contact, exposure, impact, or privity” between the debtor and the creditor. *In re Piper Aircraft Corp.*, 162 B.R. 619, 627 (Bankr. S.D. Fla. 1994). Comparatively, in *Lemelle v. Universal Manufacturing Corp.*, no “specific relationship” and, thus, no “claim” existed because the injured parties were “completely unknown and unidentified” when the debtor filed for chapter 11. 18 F.3d at 1277.

3. Policy-Based Interpretation of the Bankruptcy Code

If the bankruptcy court determines that a dischargeable pre-petition, contingent “claim” exists, the creditor might argue that the non-bankruptcy statute’s underlying policies support interpreting the Bankruptcy Code to uphold the liability’s enforceability. Second Circuit precedent instructs that courts should interpret the Bankruptcy Code pursuant to Congress’s “clear and manifest” intent before considering DRA Amendment’s underlying policies. *Oneida*, 383 B.R. at 41.

In *Oneida*, the Bankruptcy Court distinguished statutory interpretation in the bankruptcy context from statutory interpretation generally. In the bankruptcy context, “there is a strong presumption that a later law does not repeal or amend an established law such as the Bankruptcy Code.” *Id.* at 40. In *Oneida*, this presumption conflicted with statutory interpretation generally where “a statute must, if reasonably possible, be construed in a way that will give force and effect to each of its provisions rather than render some of them meaningless.” *Allen Oil Co. v. Comm’r of Internal Revenue*, 614 F.2d 335, 339 (2d Cir. 1980). Therefore, following the first maxim, courts that interpret DRA Premiums as “claims” under Bankruptcy Code section 101(5) might not consider the DRA Premium’s underlying policies because the DRA Amendment presents an irreconcilable conflict with the Bankruptcy Code. While the “claims” would be dischargeable under Bankruptcy Code section 101(5), DRA Amendment subsection (B) would

require that DRA Premiums would not be dischargeable because subsection (B) requires that DRA Premiums do not arise until post-petition. 29 U.S.C. 1341(c)(2)(B). Contrastingly, following the second maxim, courts that interpret DRA Premiums as “claims” might consider the DRA Premium’s underlying policies because the effect of holding DRA Premiums dischargeable would be to render them largely irrelevant when termination occurs in bankruptcy.

C. Arguments Made by Oneida and the PBGC

1. On Whether DRA Premiums Constitute “Claims”

In *Oneida*, the Bankruptcy Court agreed with Oneida’s arguments and held that DRA Premiums constituted pre-petition, contingent “claims” under section 101(5)(A). Arguing that DRA Premiums constituted “claims,” Oneida relied on section 101(5)(A)’s broad scope and Oneida’s certain post-petition DRA Premium liability. Oneida argued that DRA Premiums constituted contingent “claims” because DRA Premiums “arose from Oneida’s prepetition pension plan” and because the claim “became fixed as a result of an event occurring prior to confirmation – the termination, in bankruptcy, of the Oneida Pension Plan.” Memorandum of Law in Support of Plaintiff Oneida Ltd.’s Motion for Summary Judgment at 14, *Oneida Ltd. v. Pension Benefit Guaranty Corp.*, No. 06–10489 (Bankr. S.D.N.Y. 2007). Agreeing with Oneida, the Bankruptcy Court found that DRA Premium liability was contingent in name only because the contingency rested upon two alternatives, one of which was guaranteed to occur. *Oneida*, 383 B.R. at 38 (“[DRA Premiums] will arise at the time the debtor obtains a discharge or at the time the case is dismissed.”).

The Bankruptcy Court rejected the PBGC’s contrary position that the DRA Premiums were not contingent “claims.” The Bankruptcy Court distinguished *CPT Holdings*, upon which

the PBGC relied, from *Oneida*, noting that the debtor in *CPT Holdings* terminated its pension obligations post-confirmation, 162 F.3d at 408–09, while the debtor in *Oneida* terminated its pension obligations pre-confirmation. 383 B.R. at 39. To support this distinction, the court noted that the decision in *CPT Holdings* implied that pre-confirmation termination would have created a contingent “claim.” *See* 162 F.3d at 408–09.

2. Whether the “Claims” Arose Pre-Petition

After recognizing DRA Premiums as “claims,” the Bankruptcy Court considered whether the “claims” arose pre-petition. The Bankruptcy Court could not rely solely on statutory language because “[t]he Bankruptcy Code does not specify when a contingent claim arises.” *Oneida*, 383 B.R. at 42. Thus, the Court relied on the *Chateaugay I* variation of the third test. *Id.* at 43. The Court stated, “[T]he critical factor is whether, at the time of the petition, the parties contemplated that the contingent obligation would exist if the contingency occurred.” *Id.* *See In re Chateaugay*, 944 at 1005 (finding that a sufficient relationship existed in a statutory context between the regulating agency and those subject to regulation); *see also In re Jensen*, 995 F.2d at 931 (discharging a statute-based claim under a variation of the third test, which required “sufficient [pre-petition] knowledge . . . of potential liability”). The Bankruptcy Court determined that, for statutory rights to payment, “claims” arise upon “commencement of the relationship between the parties, not the date when the right to payment becomes enforceable.” *Oneida*, 383 B.R. at 43. The Bankruptcy Court found that a sufficient relationship existed because (1) the parties’ DRA Amendment relationship formed pre-petition; and (2) the parties met pre-petition to discuss *Oneida*’s potential pension termination. *Id.* at 43–44.

While the Bankruptcy Court agreed with *Oneida*’s main pre-petition argument, the Court rejected two secondary arguments. First, the Bankruptcy Court distinguished the *Chateaugay I*

variation of the third test from a “conduct”-related variation. The Court determined that the “conduct” variation applies to tort settings and “conduct-related statutory obligation[s]” only, not contract-based statutory obligations such as DRA Premiums. *Id.* at 44. Therefore, the Bankruptcy Court rejected Oneida’s argument that DRA Premiums arose pre-petition because the pension plans were “based on the prepetition labor of the participants.” Memorandum of Law in Support of Plaintiff Oneida Ltd.’s Motion for Summary Judgment at 2, *Oneida Ltd. v. Pension Benefit Guaranty Corp.*, No. 06–10489. Second, the Court rejected Oneida’s reliance on *Pension Benefit Guaranty Corporation v. Skeen (In re Bayley Corp.)*. While *In re Bayley* stated that “withdrawal liability [is] based on benefits earned as a result of employees' pre-petition labor, even if incurred post-petition”, the Tenth Circuit determined that a pre-petition “claim” existed because of plan funding deficiencies that occurred pre-petition. 163 F.3d 1205, 1206–09 (10th Cir. 1998). In *Oneida*, no plan funding deficiencies existed.

The Bankruptcy Court rejected the PBGC’s argument under the first test that DRA Premium “claims” arose post-petition. The Bankruptcy Court rejected the PBGC’s argument that, because the DRA Amendment states that DRA Premiums “shall not apply . . . until the date of the discharge,” 29 U.S.C. § 1341(c)(2)(B), DRA Premium “claims” arose post-petition and, therefore, did not become enforceable under non-bankruptcy law until discharge. Memorandum of Law in Support of PBGC’s Motion for Summary Judgment at 10–11, *Oneida Ltd. v. Pension Benefit Guaranty Corp.*, No. 06–10489 (Bankr. S.D.N.Y. 2007). The PBGC argued that, under *Worldcom, Inc. v. MCI, Inc., (In re Worldcom, Inc.)*, 546 F.3d 211, 221 (2d Cir. 2008), no right to payment exists until all the elements of the claim exist. Memorandum of Law in Support of PBGC’s Motion for Summary Judgment at 11, *Oneida Ltd. v. Pension Benefit Guaranty Corp.*, No. 06–10489. *See Vanston Bondholders Protective Comm. v. Green*, 329 U.S. 156, 170 (1946)

(Frankfurter, J. concurring) (“If there was no valid claim before bankruptcy, there is no claim for a bankruptcy court either to recognize or to reject.”).

The Bankruptcy Court rejected the PBGC’s first test argument. *Oneida*, 383 B.R. at 39. While the Bankruptcy Court stated that “[t]he PBGC is correct that non-bankruptcy law . . . governs issues such as the . . . enforceability of . . . the right to payment,” the Court continued that “[b]ankruptcy law governs . . . whether such claim arose pre- or post-petition.” *Id.* Additionally, while the Bankruptcy Court did not argue this point, even if the widely criticized first test survives in other contexts, where federal law applies as it does here, the first test most likely does not apply. *See Frenville*, 744 F.2d at 337 (“[T]he threshold question of when a right to payment arises, absent overriding federal law, ‘is to be determined by reference to state law.’” (quoting *Vanston Bondholders Protective Comm.*, 329 U.S. at 161)).

3. Whether the DRA Amendment’s Policy Intervenes

The Bankruptcy Court rejected the PBGC’s argument to consider the DRA Amendment’s underlying policies and Congress’s intent “to put the PBGC on a more secure financial foundation.” H.R. Rep. 109-276, 109th Cong. (1st Sess. 2005). The Court decided that, even though the DRA Amendment states that DRA Premiums “shall not apply . . . until the date of the discharge,” Congress did not explicitly state that DRA Premiums arise post-petition. When a statute would rearrange the hierarchy of creditors, bankruptcy courts require more definitive statutory language. *See, e.g., Int’l Brotherhood of Teamsters v. Kitty Hawk Int’l, Inc.*, 255 B.R. 428, 438–39 (Bankr. N.D. Tex. 2000).

The Bankruptcy Court agreed with *Oneida*’s argument that “if Congress wishes to alter any fundamental principles of bankruptcy law – such as the dischargeability of claims – to accommodate non-bankruptcy policies, the appropriate way to do so is to amend the Bankruptcy

Code itself.” Memorandum of Law in Support of Plaintiff Oneida Ltd.’s Motion for Summary Judgment at 3, *Oneida Ltd. v. Pension Benefit Guaranty Corp.*, No. 06–10489. As Oneida argued, “Under the governing law . . . , this Court must implement the terms of the Bankruptcy Code without regard to any policy concerns that may be embodied in the ERISA Amendment.” Memorandum of Law in Support of Plaintiff Oneida Ltd.’s Motion for Summary Judgment at 4, *Oneida Ltd. v. Pension Benefit Guaranty Corp.*, No. 06–10489. The Bankruptcy Court agreed. *Oneida*, 383 B.R. at 42. Thus, the Court refused to consider the PBGC’s financial stability in determining whether to discharge the DRA Premiums. *Id.* See *Chateaugay I*, 944 F.2d at 1002–05 (concluding that engaging in a balancing of conflicting statutes’ objectives would be improper to determine whether a claim is discharged).

D. Conclusion

Second Circuit precedent provides strong support for the Bankruptcy Court’s *Oneida* decision. While the Second Circuit’s variation of the third test is broad, other circuits’ variations of the third test would most likely discharge DRA Premiums as well. These circuits provide a difficult hurdle for creditors facing a 101(5)(A) issue to argue absence of facts showing that the parties could have contemplated the claim. Further, the first test, promulgated by the Third Circuit and most generous to creditors, will most likely face continued narrowing. Therefore, DRA Premiums will most likely remain dischargeable under chapter 11 pension terminations unless Congress amends the Bankruptcy Code.