Session Date: Friday, May 19, 2023

Session Time: 2:00pm – 3:00pm

Session Name: Judges Roundtable

Total Minutes: 60

Total Credit Hours: 1

JUDGE'S ROUNDTABLE: REACHING THE FINAL TABLE
HOT TOPICS IN COMMERCIAL BANKRUPTCY

In groups of judges and other attendees, discuss selected hot topics in commercial bankruptcy by drawing upon your expertise, knowledge, and experience. To elicit the participants' collective wisdom for a focused discussion, review the non-comprehensive material on these hot topics below. After group discussions, a group representative from each group will share observations with attendees at large.

I. POSTPETITION INTEREST IN SOLVENT DEBTOR CASES

In the chapter 11 cases of PG&E Corporation and Pacific Gas & Electric Company (together, "***PG&E***"), the United States Bankruptcy Court for the Northern District of California (Judge Dennis Montali) confirmed the debtors' plan of reorganization, which treated general unsecured claims as unimpaired claims while, at the same time, limiting the rate of postpetition interest accruing on such claims to the federal judgment rate (*i.e.*, 2.59%) as opposed to the rate dictated by contract or state law (*i.e.*, as high as the default rate of 10% under Cal. Civ. Code § 3289(b)). On appeal, the United States District Court for the Northern District of California (Judge Haywood S. Gilliam) affirmed. Both the bankruptcy court and the district court relied on *In re Cardelucci*, 285 F.3d 1231 (9th Cir. 2002), a Ninth Circuit decision that held that "[w]here a debtor in bankruptcy is solvent, an unsecured creditor is entitled to 'payment of interest at the legal rate from the date of the filing of the petition' prior to any distribution of remaining assets to the debtor," and that "legal rate" means the federal judgment rate.

The Ad Hoc Committee of Holders of Trade Claims (the "***Trade Committee***") objected to the treatment of general unsecured claims under PG&E's plan of reorganization in the bankruptcy court, on appeal in the district court, and before the Ninth Circuit. According to the Trade Committee, the Bankruptcy Code required that unsecured creditors be repaid in full, including postpetition interest, through the Bankruptcy Code's requirement that a plan of reorganization leave "unaltered" the "legal, equitable, and contractual rights" that arise from unimpaired claims. The Trade Committee argued that payment of postpetition interest at the federal judgment rate violated creditors' legal and contractual rights by disregarding the rates set by contract or otherwise by state law, and that PG&E's plan violated creditors' equitable rights by disregarding creditors' right to priority over PG&E's shareholders.

On August 29, 2022, a divided panel of the Ninth Circuit reversed the lower court rulings. *See In re PG&E Corporation*, 46 F.4th 1047 (9th Cir. 2022). The majority agreed with the Trade Committee's argument that a creditor has an equitable right to complete repayment before value can flow to shareholders. A creditor that is deemed unimpaired, therefore, may demand payment of postpetition interest at the rate that would apply outside of bankruptcy, absent countervailing equitable considerations, whenever the reorganization proposes to deliver value to equity. The majority grounded its holding in the Bankruptcy Code's protection of an unimpaired creditor's equitable rights and in the centuries of bankruptcy case law insisting that debtors repay creditors in full before distributing surplus value to shareholders. The panel decision strongly signaled that its analysis will require payment of postpetition interest at the state law or contract rates once the proceeding is remanded to the bankruptcy court to determine the exact amount of interest owed to trade creditors. On February 2, 2023, PG&E filed their petition for certiorari asking the United States Supreme Court to review the Ninth Circuit's decision.

The issue of what the appropriate rate of postpetition interest on unsecured claims should be in a solvent debtor case has been addressed by a number of other courts over the past year:

- *In re Hertz Corp.*, 637 B.R. 781 (Bankr. D. Del. 2021)
  - **Holding:** On December 22, 2021, the United States Bankruptcy Court for the District of Delaware (Judge Mary Walrath) held that neither section 1124(1) of the Bankruptcy Code nor the "solvent debtor exception" requires Hertz to pay postpetition interest to unimpaired noteholders at the contract rate and instead required payment of postpetition interest at the federal judgment rate
  - **Procedural Posture:** On December 29, 2022, Judge Walrath certified her postpetition interest ruling for direct appeal to the Third Circuit.
- *In re Ultra Petroleum Corp.* 51 F.4th 138 (5th Cir. 2022)
  - **Holding:** On October 14, 2022, the Fifth Circuit (majority) held that, in order to be unimpaired, unsecured creditors are entitled to what they barged for with the solvent debtor and must be paid postpetition interest at the contract rate (as opposed to the federal judgment rate).
  - **Procedural Posture:** On November 15, 2022, the debtors' request for *en banc* rehearing was denied.
- *In re LATAM Airlines Grp. S.A.*, 55 F.4th 377 (2d Cir. 2022)
  - **Holding:** On December 14, 2022, the Second Circuit unanimously ruled that general unsecured claims were not impaired by debtor Tam Linhas Aéreas S.A.'s ("***TLA***") plan of reorganization, which did not pay postpetition interest on such claims, because section 502(b)(2) of the Bankruptcy Code (which disallows "unmatured interest"), and not the plan, was the source of impairment; the Second Circuit also affirmed the bankruptcy court's assessment of TLA's insolvency.
  - **Procedural Posture:** On October 12, 2022, the Second Circuit heard oral argument in the appeal of the bankruptcy court's postpetition interest ruling.

<u>Questions</u>:

1. The Ninth Circuit remanded the case to the bankruptcy court to determine whether any compelling equities existed to modify the contractual or default interest rate. What equitable grounds potentially warrant modifying the contractual or default interest rate?

2. Will the *PG&E* decision impact the market for claims trading?

3. Although whether the Supreme Court will grant PG&E a writ of certiorari remains to be seen, is the postpetition interest issue one that is expected to be addressed by the Supreme Court at some point of time given the frequency with which it has been addressed in recent chapter 11 cases, including at the Circuit level on appeal?

4. Assuming the Supreme Court does eventually address the postpetition interest issue, could a ruling by the Supreme Court have broader implications than on what the appropriate rate of postpetition interest should be and the issue of impairment under Bankruptcy Code section 1124?

II. <u>UNITED STATES TRUSTEE FEES</u>

In 2017, Congress enacted a temporary increase in the United States Trustee ("***UST***") fee rates applicable to large chapter 11 cases to address a shortfall in the United States Trustee System Fund. *See* 131 Stat. 1229 (the "***2017 Act***"). The 2017 Act provided that the fee increase would become effective in the first quarter of 2018, last through 2022, and be applicable to then pending and newly filed cases. The Judicial Conference of the United States adopted the fee increase for the six judicial districts in North Carolina and Alabama that have opted out of the United States Trustee Program (such districts, the "***Administrator Program Districts***"), effective October 1, 2018, and applicable to only newly filed cases, while the districts in the Trustee Program (such districts, the "***Trustee Program Districts***") adopted the fee increase on the terms set forth in the 2017 Act (*e.g.*, applicable to both pending and newly filed cases). As a result, debtors that commenced chapter 11 cases in Trustee Program Districts were required to pay higher UST fees than debtors that commenced chapter 11 cases in Administrator Program Districts.

In 2008, Circuit City Stores, Inc. ("***Circuit City***"), commenced chapter 11 bankruptcy in the Eastern District of Virginia, a Trustee Program District. Because Circuit City's bankruptcy was still pending when the 2017 Act was enacted, the liquidating trustee appointed under Circuit City's plan of liquidation was required to pay, and did pay, $632,542 in total fees, which was significantly more than the $56,400 in fees the liquidating trustee would have had to pay absent the fee increase provided for in the 2017 Act. The liquidating trustee filed for relief against the Acting UST for Region 4, contending that the fee increase was nonuniform across Trustee Program Districts and Administrator Program Districts in violation of the Constitution's "Bankruptcy Clause."

In *Siegel v. Fitzgerald*, 142 S.Ct. 1770 (2022), the Supreme Court agreed with the liquidating trustee and unanimously held that the enactment of the 2017 Act, which imposed a significant fee increase that exempted debtors in only two states (North Carolina and Alabama), violated the Bankruptcy Clause's uniformity requirement, which empowered Congress to establish "uniform Laws on the subject of Bankruptcies throughout the United States." U. S. Const., Art. I, § 8, cl. 4.

<u>Questions</u>:

1. Prior to the Supreme Court's ruling in *Siegel*, courts were split on whether the 2017 Act violated the uniformity requirement of the Bankruptcy Clause. The Second and Tenth Circuits held that the 2017 Act did violate the uniformity requirement, whereas the Fourth, Fifth, and Eleventh Circuits found no Constitutional infirmity. Based on existing Ninth Circuit precedent, what would the Ninth Circuit's view have been on whether or not the 2017 Act violated the uniformity requirement?

2. Given that the Supreme Court did not opine on the appropriate remedy in *Siegel*, what are the practical implications of the decision? Are chapter 11 debtors that commenced bankruptcy in Trustee Program Districts and paid higher UST fees entitled to a refund of amounts in excess of what they would have paid in an Administrator Program District?

III. <u>SUBCHAPTER V, CORPORATE DISCHARGE, AND 11 U.S.C. § 523</u>

Do the exceptions to discharge identified in 11 U.S.C. § 523(a) apply to corporate subchapter V debtors? In a case of first impression, the Fourth Circuit reversed the United States Bankruptcy Court for the District of Maryland and held that the discharge exceptions do apply to corporate subchapter V debtors despite 11 U.S.C. § 523's preface that the exceptions only apply to *individual debtors*.

In *In re Cleary Packaging, LLC*, 36 F.4th 509 (4th Cir. 2022), the debtor was formed by Vincent Cleary Jr. after Mr. Cleary left a company in which he was on the board of directors and its former president and CEO. When Mr. Cleary left, he took numerous employees covered by noncompetition agreements and stole sensitive customer information which was to be used for his new competing business. Litigation commenced, and Mr. Cleary's prior company was awarded a judgment exceeding $4.7 million.

Thereafter, Mr. Cleary's company commenced a Chapter 11 bankruptcy proceeding, electing to proceed under Subchapter V. The debtor sought to confirm a plan that proposed to pay general unsecured creditors 2.98 percent of their allowed claims over five years. The prior company opposed the plan, sought a determination that its claim was nondischargeable and that the proposed payment under the plan would not discharge the judgment. The bankruptcy court confirmed the plan over the objection and concluded that § 523(a)'s discharge exceptions did not apply as the debtor was a corporate debtor.

On appeal, the Circuit Court was required to analyze the interplay between 11 U.S.C. §§ 1192(2) and 523(a). Section 1192(2) provides that a subchapter V debtor proceeding under a non-consensual plan is entitled to a discharge of its debts other than any debt "***<u>of the kind</u>*** specified in section 523(a)." Section 523, in turn, lists numerous discharge exceptions, but is prefaced by the statement that "[a] discharge under section 727, 1141, 1192, 1228(a), 1228(b), or 1328(b) … does not discharge ***<u>an individual debtor</u>***" of the debts listed.

In considering the interplay between the two sections, the Circuit Court held that § 523(a) applies to corporate debtors proceeding under non-consensual plans. While the Circuit Court recognized that § 523(a) applies only to individuals, the Circuit Court explained that § 1192 is the more specific provision and applies to both individual and corporate debtors. Important to the Circuit Court was the "importation of language into Subchapter V from the conceptually similar Chapter 12 proceedings." Like subchapter V, the Circuit Court explained that Chapter 12's scope of discharge also references an exception for debts "***<u>of a kind</u>*** specified in section 523(a)," and relied on a Western District of Texas Bankruptcy decision which held that the discharge exceptions identified in § 523(a) apply to both individual and corporate Chapter 12 debtors.

Notably, after the Fourth Circuit's decision, a decision came out of the bankruptcy court for the Western District of Texas which disagreed with Fourth Circuit and distinguished its prior decision on the applicability of § 523(a) to corporate debtors in Chapter 12. *In re GFS Industries, LLC*, 647 B.R. 337 (Bankr.W.D.Tex. 2022). The Bankruptcy Court explained that all bankruptcy courts that have confronted the issue have all held that § 523 does not apply to corporate debtors under Subchapter V.

The Bankruptcy Court's decision was appealed directly to the Fifth Circuit.

<u>Questions</u>:

1. If the debtor in *Cleary Packaging* had larger unsecured creditors that voted in favor of the plan, those creditors could have carried the class over the objections of the prior company alleging it held nondischargeability claims. Consequently, the plan could have been consensual, and § 523(a)'s exceptions would not apply. Do you think the Fourth Circuit's decision could lead to arbitrary results and undermine "the equality principles of creditor treatment under the Bankruptcy Code?"

2. How do you think the Fourth Circuit's decision impacts future subchapter V cases if other Circuit's agree?

3. The Fourth Circuit concluded its opinion by recognizing "that the relationship between § 523(a) and § 1192 might be a bit discordant – or perhaps more accurately,

clumsy." What other provisions of subchapter V may lead to similar issues (e.g. the debtor only being able to file a plan, and affiliates)?

IV. INNOCENT SPOUSE LIABILITY FOR FRAUD

In December 2022, the Supreme Court heard arguments in *Bartenwerfer v. Buckley* an appeal of a Ninth Circuit decision (860 Fed.Appx. 544). The dispute in *Bartenwerfer* involves whether a debtor wife could discharge a debt caused by the debtor husband's fraudulent concealment of defects in a house.

A California state court issued a judgment holding the debtor wife jointly liable for the debtor husband's nondisclosure of material facts. When the debtors filed for bankruptcy, the judgment creditor initiated an adversary proceeding arguing that the court judgment could not be discharged. The bankruptcy court agreed and held that the portion of the state court judgment that was traceable to the nondisclosure claim was nondischargeable. The bankruptcy court further held that the debtor husband's fraudulent conduct could be imputed to the debtor wife.

The debtors appealed to the Ninth Circuit Bankruptcy Appellate Panel ("BAP"). The BAP agreed with the bankruptcy court that collateral estoppel should apply to the decision rendered by the state court, but adopted the Eighth Circuit's "knew or should have known" standard. That is, whether the debtor wife "knew or should have known" of the debtor husband's fraud. On remand, the bankruptcy court held that the debtor husband's fraud could not be imputed to the debtor wife. The BAP affirmed.

The Ninth Circuit, however, reversed and applied basic partnership principles in imputing the debtor husband's fraud on the debtor wife:

> if, in the conduct of partnership business, ... one partner makes false or fraudulent misrepresentations of fact to the injury of innocent persons, ... his partners cannot escape pecuniary responsibility therefor upon the ground that such misrepresentations were made without their knowledge. This is especially so when ... the partners, who were not themselves guilty of wrong, received and appropriated the fruits of the fraudulent conduct of their associate in business.

Questions:

1. Can the Ninth Circuit's decision be reconciled with providing innocent debtors a fresh start? Why or Why not?

2. Argument before the Supreme Court centered around whether state law should govern whether the innocent spouse is liable for the husband's fraud or whether bankruptcy courts should apply a different standard when determining dischargeability under the Bankruptcy Code. Do you think state law should govern

the issue, or should there be a standard level of culpability that bankruptcy courts should consider? What would be the ramifications?

3. Justice Sotomayor issued the following hypothetical, "I obtain a loan fraudulently. Later, I sell that debt to my friend, Justice Thomas, who has no idea about the fraud. Justice Thomas then struggles to pay the debt and he files for bankruptcy. He wants to discharge the debt." Do you think Justice Thomas could discharge the debt? Why or why not?

I. POSTPETITION INTEREST IN SOLVENT DEBTOR CASES

- *In re PG&E Corporation*, 46 F.4th 1047 (9th Cir. 2022)
- *In re Hertz Corp*., 637 B.R. 781 (Bankr. D. Del. 2021)
- *In re Ultra Petroleum Corp.* 51 F.4th 138 (5th Cir. 2022)
- *In re LATAM Airlines Grp. S.A.*, 55 F.4th 377 (2d Cir. 2022)

46 F.4th 1047
United States Court of Appeals, Ninth Circuit.

IN RE PG&E CORPORATION; Pacific Gas & Electric Company, Debtors, Ad Hoc Committee of Holders of Trade Claims, Appellant,
v.
Pacific Gas and Electric Company, Appellee.

No. 21-16043
|
Argued and Submitted December 6, 2021 San Francisco, California
|
Filed August 29, 2022

Synopsis

Background: Parties sought to determine applicable postpetition interest to be paid to four classes of allowed unsecured and unimpaired claims under any Chapter 11 reorganization plan for solvent corporate debtors. The United States Bankruptcy Court for the Northern District of California, Dennis Montali, J., 610 B.R. 308, ruled that unsecured creditors were entitled to postpetition interest at the federal judgment rate, not at contractual or state statutory rate. Following denial of their motion for leave to file interlocutory appeal, 614 B.R. 344, unsecured creditors appealed the Bankruptcy Court's confirmation order, which incorporated its earlier postpetition interest order. The District Court, Haywood S. Gilliam, Jr., J., 2021 WL 2007145, affirmed. Unsecured creditors appealed.

Holdings: Addressing issues of first impression, the Court of Appeals, Lucero, Circuit Judge, sitting by designation, held that:

the long-standing equitable "solvent-debtor exception" to the prohibition on the collection of postpetition interest as part of a creditor's claim was not abrogated by passage of the Bankruptcy Code;

under the solvent-debtor exception, unsecured creditors whose claims are designated as unimpaired possess an equitable right to receive postpetition interest at the contractual or default state law rate, as opposed to the federal judgment rate, subject to any other equitable considerations, before the solvent debtor collects surplus value from the bankruptcy estate; and

under the circumstances, it was appropriate to remand to the Bankruptcy Court to weigh the equities and determine what rate of interest unsecured creditors were entitled to in this instance.

Reversed and remanded with instructions.

Ikuta, Circuit Judge, filed dissenting opinion.

Procedural Posture(s): On Appeal; Other.

***1050** Appeal from the United States District Court for the Northern District of California, Haywood S. Gilliam, Jr., District Judge, Presiding, D.C. No. 4:20-cv-04570-HSG

Attorneys and Law Firms

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Before: Carlos F. Lucero, [*] Sandra S. Ikuta, and Lawrence VanDyke, Circuit Judges.

Opinion by Judge Lucero;

Dissent by Judge Ikuta

OPINION

LUCERO, Circuit Judge:

***1051** This case involves an oddity in bankruptcy law: a solvent bankrupt. Specifically, it involves Pacific Gas & Electric Company ("PG&E"), which sought chapter 11 protection in a bid to proactively address massive potential liabilities related to a series of wildfires in Northern California. But PG&E was, and has remained, solvent. Its assets at the time of the bankruptcy filing exceeded its known liabilities by nearly $20 billion. As a result, several creditors—including plaintiffs, the Ad Hoc Committee of Holders of Trade Claims—claimed PG&E must pay postpetition interest at the rates required by their contracts in order for their claims to be "unimpaired" by the reorganization plan. *See* 11 U.S.C. § 1124(1). In other words, plaintiffs argued PG&E had to honor its contractual obligations before its shareholders reaped a surplus from the bankruptcy estate. The bankruptcy court and the district court disagreed. They concluded that *In re Cardelucci*, 285 F.3d 1231 (9th Cir. 2002), and the text of the Bankruptcy Code limited plaintiffs to recovery of postpetition interest at the much lower federal judgment rate. We have jurisdiction under 28 U.S.C. § 158(d)(1) and **REVERSE**.

I

PG&E filed for chapter 11 bankruptcy in January 2019. The company initiated the proceedings in response to catastrophic wildfires that occurred in Northern California during the preceding years. Following the fires, PG&E faced tens of billions of dollars in potential liabilities to fire victims, in addition to the tens of billions of dollars the company owed pursuant to its outstanding contractual commitments. [1] However, the company was solvent at the time of filing: it reported $71.4 billion in assets compared to $51.7 billion in known liabilities. PG&E nonetheless insisted bankruptcy was necessary to resolve its wildfire liabilities and ensure the liquidity needed to sustain operations. The company has never contested its ability to pay non-wildfire creditors in full.

After PG&E filed for bankruptcy, California enacted Assembly Bill 1054 ("A.B. 1054"). *See* Act of July 12, 2019, ch. 79, 2019 Cal. Stat. 1888 (codified in scattered sections of Cal. Pub. Util. Code). The act created a multi-billion-dollar safety net to compensate future victims of utility fires. Cal. Pub. Util. Code §§ 3284, 3288. For PG&E to participate in the fund, A.B. 1054 required that the bankruptcy court confirm its reorganization plan by June 30, 2020. *Id.* § 3292(b).

PG&E's proposed chapter 11 plan ("the plan") classified plaintiffs' non-wildfire-related claims as general unsecured claims. The plan provided that plaintiffs would be paid the full principal amount of these claims. It further stipulated that plaintiffs would receive postpetition interest at the federal judgment rate of 2.59 percent, *see* 28 U.S.C. § 1961(a), accruing from the date of PG&E's bankruptcy filing through the date of distribution. However, this interest rate was significantly lower than plaintiffs were entitled to under state law for contractual obligations not paid. Some of plaintiffs' contracts with PG&E contained bargained-for interest rates on unpaid obligations, while California law sets a default interest rate of ten percent. *See* ***1052** Cal. Civ. Code § 3289(b). Plaintiffs claim that, by paying them the lower federal judgment rate, PG&E's plan denied them roughly $200 million they would have received pursuant to interest rates in their contracts or, in the absence of such terms, the California default rate.

Notwithstanding the difference in interest payments, PG&E's plan classified plaintiffs' claims as "unimpaired," a statutory term used to denote which bankruptcy creditors are entitled to vote on a reorganization plan. *See* 11 U.S.C. § 1124. As supposedly unimpaired creditors, plaintiffs were deemed to automatically accept the plan and therefore had no power to vote. *See* 11 U.S.C. § 1126(f). Conversely, all classes of impaired claims were entitled to vote and could assert other statutory protections under the Bankruptcy Code if they voted against the plan. *See* 11 U.S.C. §§ 1129(a)(7), 1129(b)(1).

Plaintiffs and other unsecured creditors objected to the amount of postpetition interest provided under the plan. They argued that, because PG&E was solvent, they must receive interest at the contractual or default state law rates to be considered unimpaired. In a ruling prior to plan confirmation, the bankruptcy court disagreed. That court concluded it was bound by *Cardelucci*, which it read as establishing a broad rule that all unsecured creditors of a solvent-debtor, regardless of impairment status, are entitled only to postpetition interest at the federal judgment rate. The bankruptcy court alternatively ruled that, even if *Cardelucci* did not control, PG&E would prevail because the Bankruptcy Code limits unsecured creditors of a solvent debtor to interest at the federal judgment rate, and therefore plaintiffs' claims were not actually impaired. The bankruptcy court confirmed PG&E's plan on June 20, 2020, thus satisfying the deadline set by A.B. 1054.

Plaintiffs appealed the bankruptcy court's confirmation order, which incorporated the postpetition interest order, to the district court. That court affirmed, adopting the bankruptcy court's reasoning that *Cardelucci* controlled the postpetition interest dispute. Plaintiffs appeal that ruling to us.

II

We review de novo a district court's decision on appeal from a bankruptcy court, applying the same standard of review to the bankruptcy court's decision as did the district court. *Northbay Wellness Grp., Inc. v. Beyries*, 789 F.3d 956, 959 (9th Cir. 2015). The bankruptcy court's conclusions of law, including its interpretation of the Bankruptcy Code, are reviewed de novo. *In re Smith*, 828 F.3d 1094, 1096 (9th Cir. 2016).

III

The question we must answer is this: what rate of postpetition interest must a solvent debtor pay creditors whose claims are designated as unimpaired pursuant to § 1124(1) of the Bankruptcy Code? [2] No circuit court has addressed this issue, and bankruptcy courts have reached different conclusions. *Compare* *In re Ultra Petroleum Corp.*, 624 B.R. 178, 203–04 (Bankr. S.D. Tex. 2020) (unimpaired creditors must receive postpetition interest at the contract rate), *with* *In re Energy Future Holdings Corp.*, 540 B.R. 109, 124 (Bankr. D. Del. 2015) (unimpaired creditors are entitled to interest "under equitable principles" at a rate "the Court deems appropriate"), *and* ***1053** *In re The Hertz Corp.*, 637 B.R. 781, 800–01 (Bankr. D. Del. 2021) (unimpaired creditors need only receive interest at the federal judgment rate).

Plaintiffs contend that the bankruptcy and district courts in this case erred in holding that, as unimpaired creditors, they were only entitled to postpetition interest at the federal judgment rate of 2.59 percent. We agree that these rulings were in error. Under the long-standing "solvent-debtor exception," plaintiffs possess an equitable right to receive postpetition interest at the contractual or default state law rate, subject to any other equitable considerations, before PG&E collects surplus value from the bankruptcy estate. *Cardelucci*, which interpreted a statutory provision inapplicable to unimpaired creditors, does not hold otherwise. Moreover, we disagree with PG&E's assertion that this solvent-debtor exception was abrogated by passage of the Bankruptcy Code. To the contrary, the Code required PG&E's plan to leave "unaltered" all of plaintiffs' "legal, equitable, and contractual rights," § 1124(1)—including their equitable right to receive the bargained-for postpetition interest under the solvent-debtor exception. PG&E's plan failed to compensate plaintiffs accordingly.

A

Statutory analysis of the Bankruptcy Code is a "holistic endeavor." *United Sav. Ass'n of Texas v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 371, 108 S.Ct. 626, 98 L.Ed.2d 740 (1988). Our analysis in this case requires reference to various statutory and historic sources. We begin by summarizing (1) the common-law solvent-debtor exception, and (2) key provisions of the Bankruptcy Code.

1

Although the concept of a solvent bankrupt may seem contradictory, the scenario occurred frequently enough for the common law to develop a special rule for such cases. That rule, in short, is that a solvent debtor must generally pay postpetition interest accruing during bankruptcy at the contractual or state law rates before collecting surplus value from the bankruptcy estate.

The default rule in bankruptcy law is that interest ceases to accrue on a claim once a debtor has filed for bankruptcy. *See* *Sexton v. Dreyfus*, 219 U.S. 339, 344, 31 S.Ct. 256, 55 L.Ed. 244 (1911); 11 U.S.C. § 502(b)(2). This rule is one of necessity: in most chapter 11 cases, the debtor cannot pay all its creditors, and therefore payment of interest accruing after filing would diminish the value of the estate and result in disparate treatment of creditors. *See* *Vanston Bondholders Protective Comm. v. Green*, 329 U.S. 156, 163–64, 67 S.Ct. 237, 91 L.Ed. 162 (1946). But such concerns do not exist when a bankrupt has sufficient funds to pay all outstanding debts. *See* *Johnson v. Norris*, 190 F. 459, 462 (5th Cir. 1911) (emphasizing that the default rule halting accrual of interest during bankruptcy "was not intended to be applied to a solvent estate").

Accordingly, eighteenth century English courts developed the solvent-debtor exception, which required bankrupts to pay interest that accrued during bankruptcy before retaining value from an estate. *See, e.g.*, *Bromley v. Goodere* (1743) 26 Eng. Rep. 49, 51–52; 1 Atkyns 75, 79–81. American courts imported this doctrine and applied it under the Bankruptcy Act of 1898—the predecessor of the current Bankruptcy Code. *See, e.g.*, *City of New York v. Saper*, 336 U.S. 328, 330 n.7, 69 S.Ct. 554, 93 L.Ed. 710 (1949) (recognizing the solvent-debtor exception); *In re Beverly Hills Bancorp*, 752 F.2d 1334, 1339 (9th Cir. 1984) (same). The Supreme Court emphasized that "in the rare instances where the assets ultimately prove[ ] sufficient for the purpose, ... creditors [are] entitled to ***1054** interest accruing after adjudication." *Am. Iron & Steel Mfg. Co. v. Seaboard Air Line Ry.*, 233 U.S. 261, 266–67, 34 S.Ct. 502, 58 L.Ed. 949 (1914) ("*American Iron*").

The solvent-debtor exception was not codified, instead existing as a common-law exception to the Bankruptcy Act's prohibition on the collection of postpetition interest as part of a creditor's claim. *See* Bankruptcy Act of 1898, ch. 541, § 63, 30 Stat. 544, 562–63 (repealed) (stating that an allowed claim excludes "costs incurred and interests accrued after the filing of the petition"). Courts interpreted the exception as flowing from the purpose of bankruptcy law to ensure an equitable distribution of assets. *See Johnson*, 190 F. at 466; *Debentureholders Protective Comm. of Cont'l Inv. Corp. v. Cont'l Inv. Corp.*, 679 F.2d 264, 269 (1st Cir. 1982) ("*Debentureholders*") (calling the exception "fair and equitable"). The common-law absolute priority rule requires that a creditor be "made whole" before junior interests—including equity holders—take from the bankruptcy estate. *Consol. Rock Prods. Co. v. Du Bois*, 312 U.S. 510, 520–21, 61 S.Ct. 675, 85 L.Ed. 982 (1941); *see also Bank of Am. Nat'l Tr. & Sav. Ass'n v. 203 N. LaSalle St. P'ship*, 526 U.S. 434, 444, 119 S.Ct. 1411, 143 L.Ed.2d 607 (1999). Without a solvent-debtor exception, a solvent bankrupt could reap a windfall at their creditors' expense, pocketing "money which the debtor had promised to pay promptly to the creditor." *Debentureholders*, 679 F.2d at 269.

In *American Iron*, for example, the Supreme Court awarded interest that accrued during a period of receiver administration at the Virginia statutory rate. 233 U.S. at 264, 267, 34 S.Ct. 502. The Court explained that the general bar on payment of interest on debts in a receivership did not mean the claims "had lost their interest-bearing quality." *Id.* at 266, 34 S.Ct. 502. Rather, it was "a necessary and enforced rule" to retain equitable distribution between creditors. *Id.* But the need for such a rule disappeared when "the estate proved sufficient to discharge the claims in full." *Id.* Similarly, multiple circuit courts hearing cases under the Bankruptcy Act concluded that, in a solvent-debtor bankruptcy, "the task for the bankruptcy court is simply to enforce creditors' rights according to the tenor of the contracts that created those rights." *In re Chicago, Milwaukee, St. Paul & Pac. R.R. Co.*, 791 F.2d 524, 528 (7th Cir. 1986); *see also Debentureholders*, 679 F.2d. at 270 (reversing plan confirmation where a solvent debtor did not pay creditors their "contractual right" to interest); *Ruskin v. Griffiths*, 269 F.2d 827, 832 (2d Cir. 1959) (concluding that equity required the debtor to pay interest on creditors' claims at the "expressly-bargained-for" rate).[3]

In short, the solvent-debtor exception was well-established under the Bankruptcy Act. Under this exception, creditors of a solvent debtor were entitled to be made whole, including receiving postpetition interest pursuant to their contractual or state law default rates, before surplus value ***1055** was returned to the bankrupt. *See Chicago, Milwaukee*, 791 F.2d at 529; *Debentureholders*, 679 F.2d. at 270; *Ruskin*, 269 F.2d at 832; Chaim J. Fortgang & Lawrence P. King, *The 1978 Bankruptcy Code: Some Wrong Policy Decisions*, 56 N.Y.U. L. Rev. 1148, 1164 (1981) (describing the "well-established" pre-Bankruptcy Code principle that, when a debtor is solvent, "all claims are to be paid the full amount of their principal plus interest, both prepetition and postpetition at the contractual rate").

2

With this history in mind, we turn to the modern Bankruptcy Code ("the Code"). Congress passed the Code in 1978, replacing the prior statutory regime under the Bankruptcy

Act. *See* Bankruptcy Reform Act of 1978, Pub. L. No. 95-598, 92 Stat. 2549. "[W]hile pre-Code practice informs our understanding of the language of the Code, it cannot overcome that language." *Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 10, 120 S.Ct. 1942, 147 L.Ed.2d 1 (2000) (cleaned up).

This case revolves around the Code's concept of impairment. Section 1124(1) of the Code provides that a claim is impaired unless the bankruptcy plan "leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest." We have said that Congress "defined impairment in the broadest possible terms" and "any alteration" of a creditor's legal, equitable, and contractual rights by a debtor's plan constitutes impairment. *In re L&J Anaheim Assocs.*, 995 F.2d 940, 942 (9th Cir. 1993) (cleaned up). A debtor, as part of a proposed plan, must specify which classes of claims are unimpaired. § 1123(a)(2).

Impaired creditors receive several protections during plan confirmation that are not afforded to unimpaired creditors. First, only impaired claim holders may vote on whether to confirm a plan. *See* § 1126(a). Conversely, unimpaired claimants are presumed to accept a plan. § 1126(f). Each class of impaired claims must vote to accept a plan for a consensual confirmation to occur. § 1129(a)(8).

Moreover, an impaired creditor who votes against a plan must receive value "not less than ... such holder would so receive or retain if the debtor were liquidated under chapter 7" of the Code. § 1129(a)(7)(A)(ii). This provision, known as the best-interests-of-creditors test ("best-interests test"), incorporates by reference 11 U.S.C. § 726, which establishes the priority of distributions in chapter 7 liquidations. Section 726(a)(5) requires that creditors of a solvent debtor receive postpetition interest at "the legal rate"—a term we have said refers to the federal judgment rate established by 28 U.S.C. § 1961(a). *See Cardelucci*, 285 F.3d at 1234. Thus, pursuant to the best-interests test, a dissenting, *impaired* creditor of a solvent, chapter 11 debtor must receive postpetition interest on their claim at the federal judgment rate.

Conversely, no Code provision applies § 726(a)(5) to *unimpaired* chapter 11 claims. To the contrary, the Code expressly limits the application of § 726(a)(5) to chapter 7 liquidations. *See* 11 U.S.C. § 103(b) (stating that subchapter II of chapter 7, which includes § 726, applies only to chapter 7 cases). Section 726(a)(5) applies to chapter 11 cases solely through the best-interests test, § 1129(a)(7), which is inapplicable to unimpaired creditors. *See* *Energy Future Holdings*, 540 B.R. at 123; 7 Collier on Bankruptcy ¶ 1129.02[7][a] (16th ed. 2021) (noting the best-interests test applies "only to creditors ... who are members of impaired classes"). No provision of the Code specifies the rate of postpetition ***1056** interest a creditor must receive from a solvent debtor to be unimpaired. *See* *Ultra Petroleum*, 624 B.R. at 202. In fact, the Code is silent as to whether such creditors are entitled to any postpetition interest at all. *Id.*

Finally, when a class of impaired creditors votes against a plan, the bankruptcy court may only confirm the plan if it is "fair and equitable" with respect to that class. § 1129(b)(1). Some courts have held a solvent debtor may be required to pay contractual or default interest, over and above the required federal judgment rate, to objecting, impaired creditors in order to satisfy this "fair and equitable" requirement and secure court approval of a reorganization plan. *See, e.g.*, *In re Dow Corning Corp.*, 456 F.3d 668, 680 (6th Cir. 2006); *In re Mullins*, 633 B.R. 1, 20 (Bankr. D. Mass 2021).

In this case, PG&E's confirmed plan provided for postpetition interest on plaintiffs' claims at the federal judgment rate—the same rate plaintiffs would be entitled to as impaired creditors. However, because plaintiffs were designated as unimpaired, they could not (1) vote on the reorganization plan or (2) argue that their treatment was not "fair and equitable" under § 1129(b)(1).

B

Turning to the decisions below, we first address whether *Cardelucci* controls this case. PG&E argues—and the bankruptcy and district courts held—that *Cardelucci* established a broad rule that all unsecured claims in a solvent-debtor bankruptcy are entitled only to postpetition interest at the federal judgment rate, regardless of impairment status.

But *Cardelucci* merely held that the phrase "interest at the legal rate" in § 726(a)(5) refers to the federal judgment rate as defined by 28 U.S.C. § 1961(a). *Cardelucci*, 285 F.3d at 1234. As explained above, § 726(a)(5) only applies to *impaired* chapter 11 claims via the best-interests test. *See* 11 U.S.C. § 103(b); *Ultra Petroleum*, 624 B.R. at 202; *Energy Future Holdings*, 540 B.R. at 123–24. *Cardelucci* therefore does not tell us what rate of postpetition interest must be paid on plaintiffs' *unimpaired* claims.

Cardelucci involved a debtor who filed for bankruptcy after a state court entered a civil judgment in favor of the creditors. 285 F.3d at 1233. The parties agreed that the creditors were owed postpetition interest under § 726(a)(5), but they disagreed as to whether that provision required that interest be paid at the federal judgment or state law default rate. *Id.* This court opened its inquiry by explaining that the case involved "an award of postpetition interest *pursuant to 11 U.S.C. § 726(a)(5)*," and presented "the narrow but important issue of whether *such* post-petition interest is to be calculated using the federal judgment interest rate." *Id.* (emphasis added). We held that principles of statutory interpretation, among other reasons, compelled the conclusion that Congress intended "interest at the legal rate" in § 726(a)(5) to refer to the federal judgment rate. *Id.* at 1234–35 ("Congress' choice of the phrase 'interest at the legal rate' suggests that it intended for bankruptcy courts to apply one uniform rate defined by federal statute.").

The bankruptcy and district courts in this case held that *Cardelucci* established a broad rule that all unsecured creditors of a solvent debtor are entitled to postpetition interest at the federal judgment rate. Indeed, *Cardelucci* did not expressly limit its holding to impaired claims; it did not refer to impairment status at all. *See* *id.* at 1234 ("Where a debtor in bankruptcy is solvent, *an unsecured creditor* is entitled to 'payment of interest at the legal rate from the date of the filing of the petition' prior to any distribution of remaining assets ***1057** to the debtor.") (quoting § 726(a)(5)) (emphasis added). PG&E thus contends *Cardelucci*'s holding extends to cases involving unimpaired claims.

This argument fails for a simple reason: *Cardelucci* interpreted language from a specific statutory provision —§ 726(a)(5)—that does not apply to unimpaired claims. Rather, as discussed above, § 726(a)(5) only applies to chapter 11 cases through the best-interests test, § 1129(a)(7), which itself only applies to impaired creditors. *See* § 103(b); *Ultra Petroleum*, 624 B.R. at 202; *Energy Future Holdings*, 540 B.R. at 123–24; 7 Collier on Bankruptcy ¶ 1129.02[7][a]. Though our opinion in *Cardelucci* did not say so, the creditors in that case were impaired. Indeed, the creditors in *Cardelucci* had to be impaired for § 726(a)(5) to apply in the first place. Moreover, the parties in *Cardelucci* agreed that the amount of interest owed hinged solely on the interpretation of § 726(a)(5). *See* *Cardelucci*, 285 F.3d at 1233. Thus, the fact that *Cardelucci* did not reference the creditors' impaired status—or limit the scope of its holding to impaired claims—is not surprising. But *Cardelucci* provides no textual basis for applying § 726(a)(5) to unimpaired claims, nor could it for the reasons explained above.

We therefore decline to read *Cardelucci* as establishing the broad rule that PG&E advocates. *Cardelucci* merely held that the phrase "interest at the legal rate" in § 726(a)(5) refers to the federal judgment rate. *See, e.g.,* *Mullins*, 633 B.R. at 22 (citing *Cardelucci* for this proposition); *Ultra Petroleum*, 624 B.R. at 203 (same). But this holding does not answer what rate of interest is required where § 726(a)(5) does not apply—including for unimpaired claims. The bankruptcy and district courts erred in concluding that *Cardelucci* settles the issue before us.

C

The bankruptcy court alternatively held that even if *Cardelucci* does not limit plaintiffs to postpetition interest at the federal judgment rate, the Bankruptcy Code does. In essence, that court read several Code provisions as establishing a uniform postpetition interest rate for all unsecured claims in a solvent-debtor case. Because plaintiffs, in the bankruptcy court's view, received everything the Code entitled them to—that is, the full amount of their claims plus interest at the federal judgment rate—their "legal, equitable, and contractual rights" were not impaired under § 1124(1). *See* *In re Ultra Petroleum Corp.*, 943 F.3d 758, 763 (5th Cir. 2019) (holding impairment does not occur when the Code limits a creditor's rights); *In re PPI Enters. (U.S.), Inc.*, 324 F.3d 197, 204 (3d Cir. 2003) (same).

Analyzing this aspect of the bankruptcy court's holding requires us to first address an antecedent question: did the Bankruptcy Code displace the historic solvent-debtor exception? As discussed above, this equitable rule—widely recognized and applied under the Bankruptcy Act, even though it was not explicitly codified therein—entitled creditors to postpetition interest at the contract or default state law rate before a solvent debtor received surplus value from an estate. *See supra*, section III.A.1. We conclude passage of the Code did not abrogate the solvent-debtor exception, any more than passage of the Bankruptcy Act did so. The bankruptcy court thus erred in holding that the Code limits plaintiffs to recovery of postpetition interest at the federal judgment rate.

1

The Supreme Court has made clear that it "will not read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure." ***1058** *Cohen v. de la Cruz*, 523 U.S. 213, 221, 118 S.Ct. 1212, 140 L.Ed.2d 341 (1998) (quotation omitted); *see also* *Midlantic Nat'l Bank v. N.J. Dep't of Env't Prot.*, 474 U.S. 494, 501, 106 S.Ct. 755, 88 L.Ed.2d 859 (1986) ("The normal rule of statutory construction is that if Congress intends for legislation to change the interpretation of a judicially created concept, it makes that intent specific."). Thus, while "[t]he Bankruptcy Code can of course override by implication," any such implication must be "unambiguous." *BFP v. Resol. Tr. Corp.*, 511 U.S. 531, 546, 114 S.Ct. 1757, 128 L.Ed.2d 556 (1994). [4]

In this case, the parties agree that courts recognized a common-law, solvent-debtor exception under the Bankruptcy Act. And contrary to arguments made by PG&E and in the Dissent, we discern from the contemporary Code no "clear indication" that Congress meant to severely limit the scope of the solvent-debtor exception. *Cohen*, 523 U.S. at 221, 118 S.Ct. 1212. Rather, the Code's text, history, and structure compel the opposite conclusion: that creditors like plaintiffs continue to possess an "equitable right" to bargained-for postpetition interest when a debtor is solvent. § 1124(1).

PG&E argues—and the bankruptcy court agreed—that the combination of §§ 502(b)(2) and 726(a)(5) reflects Congressional intent to establish a uniform rate of postpetition interest for all unsecured claims when a debtor is solvent. Section 502(b)(2) prohibits the inclusion of "unmatured interest" as part of an allowed claim, codifying the long-standing rule that interest as part of a claim stops accruing once a bankruptcy petition is filed. *See* *Sexton*, 219 U.S. at 344, 31 S.Ct. 256. PG&E notes that § 502(b)(2)'s bar on postpetition interest is subject to only two statutory exceptions, including § 726(a)'s liquidation waterfall, which applies to impaired chapter 11 creditors through the best-interests test, § 1129(a)(7). [5] To the extent that courts allowed for recovery of contractual postpetition interest under the Bankruptcy Act, PG&E asserts these Code provisions indicate Congress' intent to depart from this practice and ensure all unsecured creditors of a solvent debtor receive the same rate of interest. The Dissent goes even farther, concluding that § 502(b)(2), alongside other Code provisions, mandates that creditors who are paid their allowed claims in full are not entitled to any postpetition interest, even when a debtor is solvent.

We are not persuaded. No Code provisions—alone or together—unambiguously displace the long-established solvent-debtor exception or preclude supposedly unimpaired creditors from asserting an equitable right to contractual postpetition interest. Notably, § 502(b)(2)'s prohibition on the collection of "unmatured interest" as part of a claim effectively restates its predecessor provision, § 63 of the Bankruptcy Act. Bankruptcy Act of 1898, ch. 541, § 63, 30 Stat. 544, 562–63 (repealed) (excluding from recovery "costs incurred and interest accrued after the filing of the petition"). The Senate Report accompanying ***1059** the passage of the Bankruptcy Code emphasized that § 502(b) simply restated "principles of [then] present law." S. Rep. No. 95-989, at 63 (1978), reprinted in 1978 U.S.C.C.A.N. 5787, 5849. The mere recodification of § 63—under which the equitable solvent-debtor exception was widely applied, *see, e.g.*, *Saper*, 336 U.S. at 330 n.7, 69 S.Ct. 554—fails to reflect any Congressional instruction to limit a solvent debtor's obligation to pay interest on claims against it.

Moreover, § 502(b)(2) simply excludes postpetition interest from "the amount of" a creditor's allowed claim. But "there is a significant distinction between whether postpetition interest can be *part of* an allowed claim and whether there are circumstances under which the debtor may be required to pay postpetition interest *on* an allowed claim." *Mullins*, 633 B.R. at 15 (emphasis added); *see also* *Ultra Petroleum*, 624 B.R. at 195 (explaining that while "interest as part of a claim ceases to accrue upon the filing of a bankruptcy petition ... in some circumstances, creditors may demand post-petition interest on their claims"); *Energy Future Holdings*, 540 B.R. at 111 (same). The text of § 502(b)(2) is entirely consistent with the conclusion that, in some instances, a creditor must receive postpetition interest *on* their allowed claim to be considered unimpaired. [6] Indeed, PG&E concedes that plaintiffs are entitled to some interest on their allowed claims in this case. Thus, PG&E's own argument forecloses the notion that § 502(b)(2) alone limits unimpaired creditors' ability to collect postpetition interest.

PG&E also points to § 726(a)(5). But that provision does not unambiguously abrogate the equitable solvent-debtor exception because, as explained above, it only applies to *impaired* chapter 11 creditors via the best-interests test, § 1129(a)(7). *See* *Ultra Petroleum*, 624 B.R. at 202; *Energy Future Holdings*, 540 B.R. at 123; 7 Collier on Bankruptcy ¶ 1129.02[7][a]. If Congress meant to limit all unsecured, chapter 11 creditors to interest at the federal judgment rate, it could have done so directly. Instead, the Code only applies § 726(a)(5)'s limited grant of interest "at the legal rate" to impaired creditors, who (unlike unimpaired creditors) also receive other protections under the Code, including the right to vote on a plan, § 1126(a), and the right to invoke § 1129(b)(1)'s "fair and equitable" requirement. This scheme does not reflect a "clear" requirement to fully depart from the solvent-debtor exception's equitable rule that creditors are entitled to postpetition interest pursuant to their contracts. *Cohen*, 523 U.S. at 221, 118 S.Ct. 1212. [7]

***1060** The statutory history of § 1124 also supports our conclusion that the equitable solvent-debtor exception survives today. As noted above, no Code provision explicitly entitles a supposedly unimpaired creditor to *any* postpetition interest. *See* *Ultra Petroleum*, 624 B.R. at 202. However, Congress has foreclosed the possibility that creditors designated as unimpaired need not receive postpetition interest, despite this statutory vacuum. In 1994, Congress repealed a Code provision that stated that a creditor was unimpaired if it was paid the "the allowed amount of [its] claim." *See* § 1124(3) (repealed); Bankruptcy Reform Act of 1994, Pub. L. 103-394, § 213, 108 Stat. 4106, 4126. At least one court strictly interpreted § 1124(3), holding that a creditor may be classified as unimpaired if it was paid the full principal of its claim without any postpetition interest. *See* *In re New Valley Corp.*, 168 B.R. 73, 79–80 (Bankr. D.N.J. 1994). The House Reporter explained that the repeal of § 1124(3) was meant to preclude *New Valley*'s "unfair result" from occurring again. H.R. Rep. No. 103-835, § 214 at 48 (1994). These actions by Congress confirm that creditors of a solvent debtor who are designated as unimpaired *must* receive postpetition interest on their claim—notwithstanding § 502(b)(2), or the fact that no Code provision expressly entitles such creditors to unaccrued interest.

In addition to Congressional action, the solvent-debtor exception fits comfortably within the text of the Code—specifically, its requirement that a debtor's plan leave unaltered a creditor's "legal, *equitable*, and contractual rights." § 1124(1) (emphasis added); *see* *Law v. Siegel*, 571 U.S. 415, 421, 134 S.Ct. 1188, 188 L.Ed.2d 146 (2014) ("[W]hatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code." (quotation omitted)). While, as discussed, no Code provision legally entitles supposedly unimpaired creditors to postpetition interest, pre-Code practice conclusively establishes creditors' equitable entitlement to contractual postpetition interest when a debtor is solvent, subject to any other countervailing equities. *See supra*, section III.A.1. Absent this equitable right, creditors whose claims were paid in full and designated as unimpaired would not be entitled to any postpetition interest—the exact result Congress sought to preclude by repealing § 1124(3). *See* *Energy Future Holdings*, 540 B.R. at 123 (explaining that unimpaired creditors' equitable right to interest "resolves a conflict between" § 502(b)(2) and the repeal of § 1124(3)).

Finally, our conclusion that the equitable solvent-debtor exception survives is supported by the Code's structure. The Code offers procedural and substantive protections for creditors who are impaired by a plan: including the right to vote on a plan, § 1126(a), and the ability for a dissenting, impaired class to invoke § 1129(b)(1)'s requirement that a plan be "fair and equitable" to be confirmed. By "defin[ing] impairment ***1061** in the broadest possible terms," *L&J Anaheim*, 995 F.2d at 942 (quotation omitted), Congress ensured that creditors whose rights were altered in any way by a plan could avail themselves of these protections. *See* *PPI Enters.*, 324 F.3d at 203 ("The Bankruptcy Code creates a presumption of impairment so as to enable a creditor to vote on acceptance of the plan." (quotation omitted)).

But PG&E wants to have its cake and eat it too: it seeks to pay plaintiffs the same, reduced interest rate as impaired creditors, while depriving them of the statutory protections that impaired creditors enjoy. *See* *Energy Future Holdings*, 540 B.R. at 123 (equitable principles require that unimpaired creditors not be treated inferior to impaired creditors); *Ultra Petroleum*, 624 B.R. at 203 (same). [8] We decline to adopt a reading of the Code that permits PG&E to end-run these statutory rights while reaping a windfall of hundreds of millions of dollars. Such an outcome is contrary to both a plain text reading of the Code and equitable principles that persist under the modern bankruptcy regime. *See* *Dow Corning*, 456 F.3d at 671 ("[S]olvent-debtor cases present a situation where all parties ought to be granted the benefit of their bargains, unless the equities compel a contrary result."). Rather, a more sensible reading of the Code gives solvent debtors a choice: compensate creditors in full pursuant to the solvent-debtor exception or designate them as impaired claimants entitled to the full scope of the Code's substantive and procedural protections.

In sum, we agree with plaintiffs that the Code lacks any "clear indication," *Cohen*, 523 U.S. at 221, 118 S.Ct. 1212, that Congress meant to displace the historic solvent-debtor exception. *See* *Ultra Petroleum*, 624 B.R. at 198–200 (holding the same). In so holding, we join multiple sibling circuits in recognizing that the equitable solvent-debtor exception—and its core principle that creditors should be made whole when the bankruptcy estate is sufficient—persists under the Code. *See* *Dow Corning*, 456 F.3d at 680 ("We conclude, like the other courts to have considered this issue, that there is a presumption that [contract or state law] default interest should be paid to unsecured claim holders in a solvent debtor case."); *Ultra Petroleum*, 943 F.3d at 765 ("As other circuits have recognized, absent compelling equitable considerations, when a debtor is solvent, it is the role of the bankruptcy court to enforce the creditors' contractual rights." (quotation omitted)); *Gencarelli v. UPS Cap. Bus. Credit*, 501 F.3d 1, 7 (1st Cir. 2007) ("This is a solvent debtor case and, as such, the equities strongly favor holding the debtor to his contractual obligations ...."). Accordingly, under the Code, unsecured creditors of a solvent debtor retain an equitable right to postpetition interest pursuant to their contracts, subject to any other equities in a given case. A failure to compensate creditors according to this equitable right as part of a bankruptcy plan results in impairment. *See* § 1124(1).

2

The Dissent adopts a radically different approach. It concludes that the Code's text clearly establishes that unsecured creditors are not entitled to *any* postpetition interest from a solvent debtor if they are paid their allowed claims in full. It is telling ***1062** that not even PG&E advocates this position, instead conceding that the Code entitles plaintiffs, at minimum, to postpetition interest on their claims at the federal judgment rate. Likewise, post-*New Valley* courts all agree that a solvent debtor must pay creditors *some* postpetition interest to classify their claims as unimpaired. *See* *Ultra Petroleum*, 624 B.R. at 203–04; *Energy Future Holdings*, 540 B.R. at 124; *The Hertz Corp.*, 637 B.R. at 800–01.

This unanimity is not surprising. The Dissent's reading of the Code cannot be squared with Congress' repeal of §

1124(3) following the *New Valley* decision. As explained, Congress eliminated this provision expressly to prevent *New Valley*'s "unfair result," which allowed solvent debtors to designate creditors as unimpaired simply because their allowed claims were paid in full. H.R. Rep. No. 103-835, § 214 at 48. To adopt the Dissent's reasoning would effectively nullify the 1994 amendment and allow solvent debtors to replicate "exactly the same result that led Congress to delete section 1124(3)" in the first place. *Energy Future Holdings*, 540 B.R. at 123; *see also* *PPI Enters.*, 324 F.3d at 203 (adopting bankruptcy court's holding that, after the repeal of § 1124(3), unimpaired creditors must receive interest from a solvent debtor). We have no grounds for ignoring Congress' clear instruction on this matter.

The Dissent nonetheless insists that Congress' repeal of § 1124(3) does not support our holding. In essence, it concludes that because Congress left various other provisions of the Code intact—and because these provisions, in the Dissent's view, clearly dictate that unsecured creditors paid their claims in full are unimpaired—the plaintiffs' claims remain governed by the "general rule disallowing postpetition interest." *See* Dissent at 1069, 1073 (quotation omitted). But that "general rule disallowing postpetition interest" derives from a provision—§ 502(b)(2)—that cannot carry the weight the Dissent ascribes to it. *See supra* at 1058–59. We find it implausible that Congress meant to abrogate the equitable solvent-debtor exception by recodifying § 63 of the Bankruptcy Act, under which that exception was widely applied. Moreover, the fact that the best-interests test created by § 1129(a)(7) only applies to impaired creditors is hardly grounds for concluding that creditors designated as unimpaired need not receive any interest at all when a debtor is solvent, for the reasons explained above. *See supra* at 1059–61.

More broadly, the Dissent's framing of the issue—that is, "whether unsecured creditors holding unimpaired claims ... are entitled to postpetition interest," Dissent at 1065—elides the antecedent question of what constitutes unimpairment in the first place. As discussed, the Code "creates a presumption of impairment," *PPI Enters.*, 324 F.3d at 203, by requiring that a debtor's plan "leave[ ] unaltered" an unimpaired creditor's "legal, *equitable*, and contractual rights," § 1124(1) (emphasis added). *See also* *L&J Anaheim*, 995 F.2d at 942 (emphasizing that Congress "define[d] impairment in the broadest possible terms" (citation omitted)). We clarify today that, pursuant to the solvent-debtor exception, unsecured creditors possess an "equitable right" to postpetition interest when a debtor is solvent. § 1124(1).[9] A failure to ***1063** provide for postpetition interest according to this equitable right as part of a bankruptcy plan results in impairment. No Code provision dictates otherwise, and no other result coheres the Code with Congress' repeal of § 1124(3).[10]

3

Having concluded that the equitable solvent-debtor exception survives under the Code, we now address whether the bankruptcy court erred in holding that PG&E's plan provided plaintiffs with all the Code entitled them to as unimpaired creditors. We have little trouble concluding it did.

Once again, because PG&E designated the plaintiffs' claims as unimpaired, plaintiffs' "legal, equitable, and contractual rights" must be "unaltered" by the reorganization plan. § 1124(1). Prior to PG&E's bankruptcy filing, plaintiffs possessed a contractual right to interest on debts not paid—either at rates stipulated by their contracts or the California default rate of ten percent. *See* Cal. Civ. Code § 3289(b). But this contractual right, as applied to postpetition debts, was superseded by the Code—specifically, by § 502(b)(2)'s prohibition on the inclusion of "unmatured interest" as part of a claim. *See* *Ultra Petroleum*, 943 F.3d at 763.[11] As a result, plaintiffs' claims do not include any contractual right to postpetition interest. Moreover, plaintiffs did not have a legal right to interest on their claims, as no provision of the Code expressly provides for postpetition interest for unimpaired creditors. *Energy Future Holdings*, 540 B.R. at 123–24.

***1064** Because PG&E was solvent, however, plaintiffs' claims *did* entail an equitable right to receive postpetition interest under the solvent-debtor exception. *See* *Ultra Petroleum*, 624 B.R. at 203–04; *Dow Corning*, 456 F.3d at 678 (emphasizing that "equitable considerations operate differently when the debtor is solvent"). This equitable right entitled plaintiffs to recovery of interest pursuant to their contracts, subject to any countervailing equities, before PG&E's shareholders received surplus value. However, PG&E's plan did not compensate plaintiffs accordingly. Rather, the plan provided for postpetition interest at the much lower federal judgment rate of 2.59 percent. Thus, PG&E's plan—and not the Code—altered plaintiffs' equitable right to postpetition interest under the solvent-debtor exception. *Ultra Petroleum*, 624 B.R. at 203–04; *Energy Future Holdings*, 540 B.R. at 123–24. The bankruptcy court erred in holding that plaintiffs received all that the Code entitled them to.

D

All that remains is to determine how much postpetition interest plaintiffs, as unimpaired creditors, are entitled to in this case. We reiterate that creditors of a solvent debtor—including plaintiffs in this case—enjoy an equitable right to contractual or state law default postpetition interest before allocation of surplus value from a bankruptcy estate. *See, e.g., Dow Corning*, 456 F.3d at 679–80 (noting that the solvent-debtor exception entails "a presumption that [contractual or state law] default interest should be paid to unsecured claim holders"). However, we are cognizant of the Supreme Court's admonition that "exceptions to the denial of postpetition interest are not rigid," and that "the touchstone of each decision on allowance of interest in bankruptcy has been a balance of equities between creditor and creditor or between creditors and the debtor." *Ron Pair*, 489 U.S. at 248, 109 S.Ct. 1026 (cleaned up). Accordingly, we remand to the bankruptcy court to weigh the equities and determine what rate of interest plaintiffs are entitled to in this instance.

We join our sibling circuits, however, in emphasizing that the solvent-debtor exception, though equitable in nature, does not give bankruptcy judges "free-floating discretion to redistribute rights in accordance with [their] personal views of justice and fairness." *Dow Corning*, 456 F.3d at 679 (quoting *Chicago, Milwaukee*, 791 F.2d at 528). Rather, "absent compelling equitable considerations, when a debtor is solvent, it is the role of the bankruptcy court to enforce the creditors' contractual rights." *Ultra Petroleum*, 943 F.3d at 765 (quotation omitted). We are confident that in most solvent-debtor cases involving unimpaired creditors, the equitable role of the bankruptcy court will be "simply to enforce creditors' rights according to the tenor of the contracts that created those rights." *Chicago, Milwaukee*, 791 F.2d at 528. However, we acknowledge the possibility that cases could arise where payment of contractual or default interest could impair the ability of other similarly situated creditors to be paid in full, or where other "compelling equitable considerations" could counsel in favor of payment of postpetition interest at a different rate. *Dow Corning*, 456 F.3d at 679; *Ultra Petroleum*, 943 F.3d at 765.

We see no sign of any "compelling equitable considerations" in this case that would defeat the presumption that plaintiffs are entitled to contractual or default postpetition interest. However, we acknowledge that the record before us is limited.[12] We therefore remand to the ***1065** bankruptcy court, which is most familiar with the facts of the case and the financial conditions of the parties.

IV

For the reasons stated, we **REVERSE** the district court's opinion affirming the bankruptcy court's postpetition interest ruling. We **REMAND** to the district court with instructions to remand to the bankruptcy court for further proceedings consistent with this opinion.

IKUTA, Circuit Judge, dissenting:

This case raises the question whether unsecured creditors holding unimpaired claims in bankruptcy under 11 U.S.C. § 1124(b) are entitled to post-petition interest on their claims when the debtor is solvent. The text of the Code provides a clear answer: No. In order to reach the opposite result, the majority erroneously holds that pre-Code practice is binding unless the text of the Code clearly abrogates it. Maj. at 1057–58, 1061. But the Supreme Court has directed us to take the exact opposite approach: so long as the Code is clear, we do not refer to pre-Code practice. *See United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 241, 109 S.Ct. 1026, 103 L.Ed.2d 290 (1989). Here, the text of the Code is clear and does not authorize an award of post-petition interest to unimpaired creditors. I therefore dissent.

I

The debtor in this case is Pacific Gas & Electric Company (PG&E), a California-based utility company. Between 2015 and 2018, California suffered a series of catastrophic wildfires. PG&E faced over $30 billion in potential liability related to those wildfires, excluding punitive damages and civil penalties. Unrelated to the wildfires, PG&E also owed billions of dollars to traditional creditors. Although PG&E was solvent at the time it filed its petition in bankruptcy (its assets exceeded known liabilities by approximately $20 billion), PG&E concluded that it lacked the resources to resolve wildfire claims that had been asserted against it (as well as future wildfire claims related to the fires between 2015 and 2018) while also continuing to provide electric and gas services, invest in wildfire-related safety practices, and service the billions of dollars in traditional debt obligations. Accordingly, on January 29, 2019, PG&E filed for Chapter 11 bankruptcy, which would allow PG&E to continue its operations while also resolving all wildfire claims. In September 2019, PG&E filed its proposed bankruptcy plan.

The appellants here are unsecured trade creditors in PG&E's bankruptcy proceedings who formed the Ad Hoc Committee of Holders of Trade Claims ("Trade Committee"). In the Chapter 11 proceedings, PG&E proposed a plan that would give the members of the Trade Committee the full cash value of their allowed claims as of the date the petition was filed. Under 11 U.S.C. § 1124, these claims were not "impaired." The plan also provided that the members of the Trade Committee would receive interest on their claims at the federal judgment rate accruing from the petition date through the date of distribution.

Rather than argue that the plan should designate their claims as "impaired," the members of the Trade Committee argued that because PG&E was a solvent debtor, and the proposed plan treated their claims as unimpaired, they were entitled to post-petition interest on their claims at the rate provided for by contract or applicable state law. The bankruptcy court rejected this argument, concluding that, under *In re Cardelucci*, 285 F.3d 1231 (9th Cir. 2002), unimpaired creditors in a solvent-debtor ***1066** case are entitled to post-petition interest only at the federal judgment rate. The district court affirmed.

On appeal, the Trade Committee members assert that they are entitled to post-petition interest at the contract or state default rates. According to the Trade Committee, this result is compelled by the solvent-debtor exception which had been adopted and applied by bankruptcy courts before the Code was enacted. The Trade Committee asserts that we must interpret the Code in light of this pre-Code practice, and the majority adopts this reasoning.

II

A

In order to address the Trade Committee's argument, it is crucial to understand the Supreme Court's framework for interpreting the Code. According to the Supreme Court, in interpreting the Code, as with any other congressional enactment, "we begin with the understanding that Congress 'says in a statute what it means and means in a statute what it says there.' " *Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 6, 120 S.Ct. 1942, 147 L.Ed.2d 1 (2000) (quoting *Connecticut Nat. Bank v. Germain*, 503 U.S. 249, 254, 112 S.Ct. 1146, 117 L.Ed.2d 391 (1992)). Therefore, "when the statute's language is plain, the sole function of the courts—at least where the disposition required by the text is not absurd—is to enforce it according to its terms." *Id.* (cleaned up). "[A]s long as the statutory scheme is coherent and consistent, there generally is no need for a court to inquire beyond the plain language of the statute." *Ron Pair*, 489 U.S. at 240–41, 109 S.Ct. 1026.

Because the statutory text takes precedence, practices adopted by bankruptcy courts before the Code was enacted play a limited role. Indeed, the Court has recognized that Congress's intent in enacting the Code was to "codify creditors' rights *more clearly than the case law.*" *Id.* at 248, 109 S.Ct. 1026 (emphasis original) (cleaned up). Therefore, "[w]here the meaning of the Bankruptcy Code's text is itself clear ... its operation is unimpeded by contrary ... prior practice." *Hartford*, 530 U.S. at 10, 120 S.Ct. 1942 (citation omitted); *see also* *Ron Pair*, 489 U.S. at 241, 109 S.Ct. 1026 (holding that where Congress expresses its intent "with sufficient precision," then "reference to legislative history and to pre-Code practice is hardly necessary"). The Supreme Court has relied on pre-Code practice merely to clarify ambiguities in the text of the Code, or to "fill in the details of a pre-Code concept that the Code had adopted without elaboration." *Hartford*, 530 U.S. at 11, 120 S.Ct. 1942. In other words, pre-Code practice is "a tool of construction, not an extratextual supplement," *id.* at 10, 120 S.Ct. 1942, and "there are limits to what may constitute an appropriate case" for employing that tool of construction, *Ron Pair*, 489 U.S. at 245, 109 S.Ct. 1026.

B

It is important to understand how this interpretative framework works with the Code's statutory scheme. "A business may file for bankruptcy under either Chapter 7 or Chapter 11" of the Code. *Czyzewski v. Jevic Holding Corp.*, 580 U.S. 451, 137 S. Ct. 973, 978, 197 L.Ed.2d 398 (2017). "In Chapter 7, a trustee liquidates the debtor's assets and distributes them to creditors." *Id.* (citing 11 U.S.C. § 701 *et seq.*). "In Chapter 11, debtor and creditors try to negotiate a plan that will govern the distribution of valuable assets from the debtor's estate and often keep the business operating as a going concern." *Id.*

In a case filed under chapter 11 of the Code, the debtor-in-possession or trustee proposes a plan of reorganization, which ***1067** designates "classes of claims" and interests. The Code defines the term "claim" as a "right to payment" or a "right to an equitable remedy for breach of performance if such breach gives rise to a right to payment." 11 U.S.C. § 101(5). A claim is allowed in bankruptcy proceedings if the creditor files a proof of claim, and there is no objection. *Id.* § 502(a). If an objection is made, the bankruptcy court (after notice and a hearing) will allow the claim in the amount determined by the court subject to several exceptions. *Id.* § 502(b).

A key exception here is for "unmatured interest." *Id.* Section 502(b)(2) establishes that "creditors are not entitled to include un-matured or post-petition interest as part of their claims in the bankruptcy proceeding and cannot collect such interest from the bankruptcy estate." *In re Pardee*, 193 F.3d 1083, 1085 n.3 (9th Cir. 1999). In light of § 502(b)(2), there is no dispute that an allowed claim stops accruing interest as of the date the debtor files a petition in bankruptcy. *See In re Weiss*, 251 B.R. 453, 463 (Bankr. E.D. Pa. 2000). All other circuits are in accord. [1] Because § 502(b)(2) establishes "the general rule disallowing postpetition interest," *United Sav. Ass'n of Texas v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 373, 108 S.Ct. 626, 98 L.Ed.2d 740 (1988), it "does not simply prohibit certain creditors from filing a proof of claim for post-petition interest; it prohibits those creditors from collecting the interest from the bankruptcy estate." *Victor*, 121 F.3d at 1387. There is no basis for the majority's interpretation of § 502(b)(2) as prohibiting interest *as part of* an allowed claim but not prohibiting interest *on* a claim once it is allowed. Maj. at 1058–59.

Once the allowed claims have been identified, the trustee must specify which classes of claims are impaired and which are unimpaired. *See* 11 U.S.C. § 1123(a)(2), (3). An allowed claim is unimpaired if it "leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest." [2] *Id.* § 1124(1). Reading this definition together with § 502(b)(2) and § 101(5) (defining a "claim" as a "right to payment" or a "right to an equitable remedy for breach of performance," *id.* § 101(5)), a claim is unimpaired so long as the proposed plan gives the creditor the same legal or contractual right to payment, or right to an equitable remedy, that the creditor had as of the date the petition ***1068** was filed. Such a claim would include any interest that had matured by the time the petition was filed. *See id.* § 1124(1). The statutory language provides no basis for the majority's theory that a creditor's "claim," which may not include post-petition interest, *see* § 502(b), is nevertheless deemed "impaired" if the debtor turns out to be solvent and the creditor does not obtain post-petition interest at the end of the bankruptcy case. Maj. at 1062–63 & n.9.

Because creditors with unimpaired claims are set to receive full payment of those claims under the plan, they are conclusively presumed to have accepted the plan. *See id.* § 1126(f). By contrast, creditors with impaired claims are entitled to vote on whether to accept or reject a plan, *see id.* § 1126(a), and the plan cannot be confirmed by consent unless each class of claims has accepted the plan, *see id.* § 1129(a)(8). If all classes of impaired claims do not accept the plan, the bankruptcy court can still approve the plan "provided the plan is fair and equitable and does not unfairly discriminate against any impaired claims, and the plan meets all the statutory requirements of § 1129(a)." *In re Barakat*, 99 F.3d 1520, 1524 (9th Cir. 1996) (internal citation omitted).

Although a claim stops accruing interest at the time the petition in bankruptcy is filed, § 502(b)(2), the members of the Trade Committee argue that they are nevertheless entitled to post-petition interest under the solvent debtor exception applied in pre-Code practice. Before the Code was enacted, bankruptcy proceedings were governed by the Bankruptcy Act of 1898 ("the Bankruptcy Act"). Like § 502(b)(2) of the modern Code, § 63 of the Bankruptcy Act prohibited an award of post-petition interest to creditors. *See* Bankruptcy Act of 1898, ch. 541, § 63, 30 Stat. 544, 562–63 (repealed) (excluding "costs incurred and interests accrued after the filing of the petition" from allowed claims). However, courts recognized equitable exceptions to § 63 of the Bankruptcy Act. *See* *Ron Pair*, 489 U.S. at 246, 109 S.Ct. 1026. One of those equitable exceptions, known as the solvent-debtor exception, "allowed postpetition interest when the debtor ultimately proved to be solvent." *Id.*

In enacting the Code, Congress implicitly incorporated this solvent debtor exception in certain circumstances, and therefore identified exceptions to § 502(b)(2)'s "general rule disallowing postpetition interest." *Timbers of Inwood Forest*, 484 U.S. at 373, 108 S.Ct. 626. For example, although an allowed claim in a Chapter 7 case does not include post-petition interest, *see* 11 U.S.C. § 502(b), the holder of such a claim may nevertheless receive post-petition interest as part of the distribution of property of the estate after higher priority distributions have been made, *see id.* § 726(a)(5) (providing that the fifth priority of property distribution is "in payment of interest at the legal rate from the date of the filing of the petition" on an allowed claim.). The Code also implicitly incorporated the solvent debtor exception in the "best interest of creditors" tests set forth in § 1129(a)(7)(a)(ii).[3] This section provides that, to confirm a proposed plan, creditors with unsecured *impaired* claims must accept the plan or receive property of a value "as of the effective date of the plan, that is not less than ... such holder would so receive or retain if the debtor were liquidated under chapter 7" of the Code. *Id.* 1129(a)(7). This means that a Chapter 11 plan cannot be confirmed unless each objecting, unsecured creditor holding impaired claims receives the same post-petition ***1069** interest as that creditor would have received under § 726(a)(5) if the debtor's estate had been liquidated. *See* *In re Cardelucci*, 285 F.3d 1231, 1234 (9th Cir. 2002) (citing 11 U.S.C. § 726(a)(5)). This section applies only to unsecured creditors holding impaired claims.[4] 11 U.S.C. § 1129(a)(7).

As these provisions demonstrate, "Congress knew how to draft the kind of statutory language that petitioner seeks to read into [the Code]." *State Farm Fire & Cas. Co. v. U.S. ex rel. Rigsby*, 580 U.S. 39, 137 S. Ct. 436, 444, 196 L.Ed.2d 340 (2016); *see* 11 U.S.C. §§ 506(b), 726(a)(5), 1127(a)(7), 1322(b)(10). But despite incorporating exceptions to the general rule disallowing post-petition interest into these specific sections, Congress chose not to make a similar exception authorizing an award of post-petition interest to unsecured creditors holding unimpaired claims, regardless of whether the debtor ends up solvent. As a general rule, "[w]here Congress explicitly enumerates certain exceptions to a general prohibition, additional exceptions are not to be implied, in the absence of evidence of a contrary legislative intent." *Hillman v. Maretta*, 569 U.S. 483, 496, 133 S.Ct. 1943, 186 L.Ed.2d 43 (2013) (citation omitted). This canon of construction has even greater weight in the bankruptcy context, where the Supreme Court has warned us not "to inquire beyond the plain language of the statute," *Ron Pair*, 489 U.S. at 241, 109 S.Ct. 1026, where Congress's "statutory scheme is coherent and consistent," *id.* at 240, 109 S.Ct. 1026. Accordingly, we should conclude that unsecured creditors holding unimpaired claims are governed by "the general rule disallowing postpetition interest," even in a solvent debtor case. *Timbers of Inwood Forest*, 484 U.S. at 373, 108 S.Ct. 626.

Therefore, because the members of the Trade Committee hold unsecured claims classified as unimpaired, I would hold that they are not entitled to post-petition interest, despite PG&E's solvency.

III

Notwithstanding the absence of any provision entitling an unimpaired creditor to post-petition interest, as the majority itself recognizes, *see* Maj. at 1060, the majority nevertheless decides that unimpaired creditors are entitled to post-petition interest—even though Congress chose not to make an exception for such creditors. All of the majority's justifications for this addition are flawed.

A

The majority's central rationale is that unimpaired creditors are entitled to the post-petition interest they would have received under pre-Code practice because Congress did not expressly abrogate such practice. Maj. at 1058–59. The majority's argument proceeds in several steps. First, it claims (contrary to the Supreme Court's direction) that there is a presumption that the Code incorporates pre-Code practice unless the Code contains a clear indication that Congress intended to abrogate that practice. *See* Maj. at 1057–59 (citing ***1070** *Cohen v. de la Cruz*, 523 U.S. 213, 221, 118 S.Ct. 1212, 140 L.Ed.2d 341 (1998)). Under pre-Code practice, courts awarded post-petition interest to unimpaired creditors, even though § 63 of the Bankruptcy Act precluded the accrual of interest on a claim once the petition in bankruptcy has been filed. Because Congress did not expressly state that bankruptcy courts must stop awarding post-petition interest to unimpaired creditors, and § 502(b)(2) is just a recodification of § 63, the majority infers that courts can continue to award post-petititon interest to unimpaired creditors notwithstanding § 502(b)(2). Maj. at 1057–61.

This reasoning fails because the majority's underlying principle—that pre-Code practice applies unless Congress clearly abrogated it—is wrong. As explained above, courts must start with the language of the Code and rely on pre-Code practice only as "a tool of construction, not an extratextual supplement," *Hartford*, 530 U.S. at 10, 120 S.Ct. 1942. "[A]s long as the statutory scheme is coherent and consistent, there generally is no need for a court to inquire beyond the plain language of the statute," including by looking to pre-Code practice. *Ron Pair*, 489 U.S. at 240–41, 109 S.Ct. 1026. Moreover, because "the [pre-Code] exceptions to the denial of postpetition interest are not rigid doctrinal categories" but are instead "flexible guidelines" that were "developed by the courts in the exercise of their equitable powers," there is "no reason to think that Congress, in enacting a contrary standard, would have felt the need expressly to repudiate it." *Id.* at 248, 109 S.Ct. 1026 (cleaned up).

The majority bases its erroneous rule of interpretation on statements taken out of context from Supreme Court decisions. In its central statement of this "rule," the majority cites *Cohen v. de la Cruz* for the proposition that the Supreme Court "will not read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure." Maj. at 1057 (citing 523 U.S. at 221, 118 S.Ct. 1212). But in context, *Cohen* faithfully followed the Supreme Court's textualist approach to the Code. *Cohen* construed 11 U.S.C. § 523(a)(2)(A), which makes nondischargeable "any debt ... for money ... to the extent obtained by ... actual fraud." 523 U.S. at 214–15, 118 S.Ct. 1212. *Cohen* held that the statutory language encompassed an award against the debtor of treble damages, attorneys' fees, and costs due to the debtor's fraudulent conduct. *Id.* at 219, 118 S.Ct. 1212. In so holding, *Cohen* first performed a thorough textual analysis, *see id.* at 217–21, 118 S.Ct. 1212, and concluded that, "[w]hen construed in the context of the statute as a whole ... § 523(a)(2)(A) is best read to prohibit the discharge of any liability arising from a debtor's fraudulent acquisition of money, property, etc., including an award of treble damages for the fraud," *id.* at 220–21, 118 S.Ct. 1212. Only after an in-depth analysis of the statutory text did the Court turn to pre-Code practice for confirmation of its interpretation, stating that "[t]he history of the fraud exception *reinforces* our reading of § 523(a)(2)(A)." *Id.* at 221, 118 S.Ct. 1212 (emphasis added). Because the statutory language in § 523(a)(2)(A) was substantially the same as the language in the Bankruptcy Act, the Court stated that it would not "read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure, and the change to the language of § 523(a)(2)(A) in 1984 in no way signals an intention to narrow the established scope of the fraud exception along the lines suggested by petitioner." *Id.* at 220–21, 118 S.Ct. 1212 (cleaned up). In other words, the Court confirmed its interpretation of statutory language by reference to pre-Code interpretation of substantially the ***1071** same statutory language. This by no means gives courts carte blanche to give creditors rights unsupported by (and inconsistent with) the Code. [5]

Once the majority's erroneous approach is eliminated, there is no support for the majority's conclusion. The majority's boon to unimpaired creditors neither interprets an ambiguous phrase nor "fill[s] in the details of a pre-Code concept that the Code had adopted without elaboration," *Hartford*, 530 U.S. at 11, 120 S.Ct. 1942. Instead, the majority overrides the scheme set forth in the Code, which does *not* allow for an award of post-petition interest to unimpaired creditors but rather adopted a different scheme that incorporated the solvent debtor exception in limited circumstances, *see* 11 U.S.C. §§ 506(b), 726(a), 1129(a)(7)(A)(ii), 1322(b)(10). In short, the majority is using pre-Code practice as an "extratextual supplement" in violation of Supreme Court directions, *Hartford*, 530 U.S. at 10, 120 S.Ct. 1942, and therefore exceeds the "limits to what may constitute an appropriate case" for relying on pre-Code practice, *Ron Pair*, 489 U.S. at 245, 109 S.Ct. 1026.

Contrary to the majority, its ruling is not supported by our sister circuits. Maj. at 1061. None of the cases the majority cites awarded post-petition interest to *unimpaired* creditors pursuant to the solvent-debtor exception. For example, the Sixth Circuit held that *impaired* creditors in a solvent debtor case are generally entitled to post-petition interest at the contract rate pursuant to 11 U.S.C. § 1129(b). *See In re Dow Corning Corp.*, 456 F.3d 668, 677–80 (6th Cir. 2006). The Sixth Circuit did not address unimpaired claims. The First Circuit held that a creditor could be entitled to bargained-for prepayment penalties because the debtor was solvent, *see Gencarelli v. UPS Cap. Bus. Credit*, 501 F.3d 1, 6 (1st Cir. 2007), but did not address post-petition interest, let alone whether such interest applies to unimpaired claims in a solvent debtor case. To the contrary, the First Circuit noted that cases addressing post-petition interest were "inapposite" because, unlike the prepayment penalties at issue in the case, post-petition interest is barred by "an explicit statutory provision." *Id.* at 6 n.2 (citing 11 U.S.C. § 502(b)(2)). Finally, although the Fifth Circuit stated in dicta that it discerned "no reason why the solvent-debtor exception could not apply" to unimpaired claims, *In re Ultra Petroleum Corp.*, 943 F.3d 758, 765 (5th Cir. 2019), this dicta lacks persuasive force, since the Fifth Circuit relied on *In re Dow*, which did not address unimpaired claims, *see* 456 F.3d at 677–80, and *In re Chicago, Milwaukee, St. Paul and Pac. R.R. Co.*, 791 F.2d 524, 528 (7th Cir. 1986), which was decided pursuant to the Bankruptcy Act, not the Code, *see id.* at 525–26. [6]

B

The majority also attempts to justify its decision that unimpaired creditors are entitled to post-petition interest based on legislative history. Even though "no Code provision legally entitles unimpaired creditors ***1072** to postpetition interest," Maj. at 1060, the majority claims that "Congress has foreclosed the possibility that unimpaired creditors need not receive postpetition interest." Maj. at 1060.

This bold statement is based on a 1994 amendment to the Code, deleting § 1124(3), which had stated that a claim was unimpaired if the proposed plan in a Chapter 11 bankruptcy provided the holder of such a claim "cash equal to ... the allowed amount of such claim." 11 U.S.C. § 1124(3) (1993). A report of the House Judiciary Committee indicated that this amendment was intended to overrule a bankruptcy court decision, *In re New Valley Corp.*, 168 B.R. 73, 79 (1994), which ruled that unimpaired creditors were not entitled to post-petition interest when the debtor was solvent. In reaching this conclusion, *In re New Valley Corp.* relied on several sections of the Code, including § 1129(a)(7)(A) (applying the "best interest of creditors" test to impaired claims), § 502(b)(2) (providing that an allowed claim does not include unmatured interest); and § 1124(3) (providing that a claim that is paid in full is not impaired). *Id.* The report of the House Judiciary Committee explained that its deletion of § 1124(3) would establish that creditors who are paid in full could still be "impaired," and therefore entitled to post-petition interest under § 1129(a)(7) in a solvent debtor case. H.R. Rep. No. 103-835, § 214 at 48 (1994). [7] But according to the report, the deletion of § 1124(3) would not affect § 1129(a)(7) of the Code, "which excluded from application of the best interests of creditors test classes that are unimpaired under section 1124." *Id.* The 1994 amendments did not delete or amend § 1129(a)(7)(a) or § 502(b)(2) in any relevant way, nor amend the Code to establish that an unimpaired creditor was entitled to post-petition interest.

The deletion of § 1124(3) and the House Judiciary Committee report provide no support for the majority's attempt to benefit unimpaired creditors. First, any reliance on legislative history is unwarranted where, as here, the Code's language is unambiguous. [8] *See Toibb v. Radloff*, 501 U.S. 157, 162, 111 S.Ct. 2197, 115 L.Ed.2d 145 (1991). Second, even if the report merited consideration, it provides no support for the majority's rule that unimpaired creditors are entitled to post-petition interest. As indicated above, the report stated that the deletion of § 1124(3) was intended to expand the definition of impaired claims, so more creditors would be deemed to be holding impaired claims, and thus be entitled to post-petition interest under one of the established "best interests of creditors" tests. *See* H.R. Rep. No. 103-835, § 214 at 48. But the report also makes clear that unimpaired creditors would still ***1073** be deprived of post-petition interest. *See id.* Therefore, the report would not help creditors with unimpaired claims, because such claims (which cannot include postpetition interest, *see* § 502(b)) are not automatically transformed into impaired claims merely because a court determines that the creditor is entitled to post-petition interest in addition to the claim. *See infra* at Section III.C. Finally, the report fails on its own terms, because it does not accurately describe the effect of the deletion of § 1124(3). Although Congress eliminated the section defining a claim as unimpaired if the creditor obtains the full amount of the claim, this deletion did not provide any guidance for differentiating impaired from unimpaired claims, expressly state that claims such as the ones held by members of the Trade Committee should be classified as impaired, or alter the Code's "general rule disallowing postpetition interest." *Timbers of Inwood Forest*, 484 U.S. at 373, 108 S.Ct. 626.

C

The majority makes the related contention that § 1124(1), which states that a claim is impaired unless the plan "leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest," requires holding that an unsecured claim must be classified as impaired in a solvent debtor case unless the creditor obtains post-petition interest. The majority reasons that the term "equitable ... rights" in § 1124(1) includes the right to post-petition interest under the solvent debtor exception, and "[a] failure to provide for postpetition interest according to this equitable right as part of a bankruptcy plan results in impairment." Maj. at 1062–63.

This argument fails for multiple reasons.[9] First, § 1124(1) explains when a "class of claims or interests" is impaired. Because a claim cannot include post-petition interest, *see* § 502(b)(2), the failure of a plan to provide for payment of post-petition interest cannot impair the claim itself. The majority argues that even if a claim does not include post-petition interest, a claim can *entitle* its holder to such interest. Maj. at 1062–63 n.9. But this ignores the language of § 1124(1), which explains only when a *claim* is impaired. The statute does not describe when a *holder's* equitable rights are impaired, nor is there any basis for concluding that a holder's loss of some equitable right under pre-Code practice would impair the holder's *claim.* Moreover, because the Code establishes that an allowed claim does *not* include post-petition interest, *see* § 502(b)(2), it is not plausible to read § 1124(1), as the majority does, as contemplating that a claim *must* include post-petition interest (when the debtor is solvent), or it would be impaired.

Second, the majority misinterprets the term "equitable ... rights" in § 1124(1). By its terms, § 1124(1) focuses on the creditor's claim, and the scope of the rights included in that claim. Congress defined "claim" broadly to include any "right to payment" and any "right to an equitable remedy for breach of performance if such breach gives rise to a right to payment." § 101(5).[10] Therefore, a creditor's ***1074** claim includes equitable rights such as restitution, quantum meruit, or other equitable remedy to which the creditor has a right at the time of filing.[11] If the plan fails to provide for payment of any of these rights, then under § 1124(1), that claim is impaired. This is the only plausible reading of the term "equitable rights" in § 1124(1), because it gives effect to the statute's purpose of explaining when a claim is impaired due to the failure to pay the full amount of the allowed claim as of the date of the petition in bankruptcy. By contrast, interpreting the term "equitable rights" in § 1124(1) as authorizing a bankruptcy court to provide creditors with an equitable benefit beyond the amount of the allowed claim makes no sense, because a court's failure to provide such a benefit could not "impair" the allowed claim itself. Moreover, interpreting § 1124(1) as authorizing courts to provide creditors with extra-textual equitable benefits would be contrary to the Supreme Court's rulings that bankruptcy courts may not use equitable powers to provide benefits not permitted by the Code. *See* *Law v. Siegel*, 571 U.S. 415, 421–22, 134 S.Ct. 1188, 188 L.Ed.2d 146 (2014) (holding that a bankruptcy court cannot make additional funds available to defray administrative expenses by imposing an "equitable surcharge" on a debtor's homestead exemption). "[W]hatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code." *Id.* at 421, 134 S.Ct. 1188 (citations omitted).

Finally, the majority's holding that a "failure to provide for postpetition interest according to this equitable right as part of a bankruptcy plan results in impairment," Maj. at 1062–63, means that an unimpaired claim automatically and retroactively becomes an impaired claim if the creditor is not awarded postpetition interest in a solvent debtor case. But such an unprecedented backwards-looking impact has no basis in the Code. "[T]he amount and priority of an unsecured creditor's claim is fixed on the date of the filing of the petition." *In re LCO Enterprises*, 12 F.3d 938, 941 (9th Cir. 1993). Obligations accruing *after* the petition is filed are not part of a claim, and so a debtor's failure to fulfill those obligations does not result in impairment. Even where post-petition interest is available, it is inherently an obligation that accrues *after* the petition for bankruptcy is filed. *See* *In re Pardee*, 193 F.3d at 1085 n.3; *see also* *Bursch v. Beardsley & Piper, a Div. of Pettibone Corp.*, 971 F.2d 108, 114 (8th Cir. 1992) (explaining that post-petition interest "is unmatured at the time of filing"). Indeed, as § 726(a)(5) indicates, the solvency of the debtor may be unknown until the property of the estate is being distributed. [12] Therefore, regardless ***1075** whether a creditor is entitled to post-petition interest *in addition to* the amount of its claim under a solvent debtor exception, a creditor's failure to obtain post-petition interest does not affect a claim's designation as impaired or unimpaired, nor does it retroactively make an unimpaired claim "impaired."

D

Finally, the majority makes the policy argument that prohibiting unimpaired claimants from receiving post-petition interest (or limiting their post-petition interest to the same rate as impaired creditors) is inconsistent with "the Code's structure," Maj. at 1060–61, because unimpaired creditors should not be treated worse than impaired creditors. But "the pros and cons of [treating different classes of creditors differently] are for the consideration of Congress, not the courts." *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 566 U.S. 639, 649, 132 S.Ct. 2065, 182 L.Ed.2d 967 (2012). "[I]t is not for the courts to alter the balance struck by the statute," *Siegel*, 571 U.S. at 427, 134 S.Ct. 1188, especially after Congress "worked on the formulation of the Code for nearly a decade," *Ron Pair*, 489 U.S. at 240, 109 S.Ct. 1026, and "standardize[d] an expansive (and sometimes unruly) area of law," *RadLAX*, 566 U.S. at 649, 132 S.Ct. 2065. Rather, "the sole function of the courts is to enforce [the Code's plain language] according to its terms," *Ron Pair*, 489 U.S. at 241, 109 S.Ct. 1026 (citation omitted), even if that "may produce inequitable results for trustees and creditors," *Siegel*, 571 U.S. at 426, 134 S.Ct. 1188. Moreover, even if policy considerations were relevant, Congress could have chosen to give impaired creditors greater protections than unimpaired creditors, because impaired creditors (such as classes of wildfire victims here) may not receive payment of their claims in full. Thus, "depriving [unimpaired creditors] of the statutory protections that impaired creditors enjoy" does not "end-run th[e] statutory rights" of unimpaired creditors. Maj. at 1061. To the contrary, it enforces the Code's express terms, and it is the majority that allows unimpaired creditors to end-run Congress's prohibition on post-petition interest.

* * *

Because I would follow the Supreme Court's direction, and leave it to Congress to decide whether creditors holding claims that are fully paid under a plan of reorganization are entitled to post-petition interest when the debtor is solvent, I respectfully dissent.

All Citations

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Footnotes

* The Honorable Carlos F. Lucero, United States Circuit Judge for the U.S. Court of Appeals for the Tenth Circuit, sitting by designation.

1 In a declaration accompanying the bankruptcy filing, a PG&E executive estimated that the company's wildfire-related liabilities "could exceed $30 billion, without taking into account potential punitive damages, fines and penalties or damages with respect to 'future claims.' "

2 PG&E has said at previous stages of this litigation that, should plaintiffs prevail in the postpetition interest dispute, it would amend the plan to pay plaintiffs the amount of postpetition interest they are entitled to under the Code as unimpaired creditors.

3 PG&E contends that early American cases recognizing the solvent-debtor exception, including *Johnson*, did not specify that postpetition interest should be paid at contractual or default state law rates. But it is unclear what other rates those courts could have contemplated. The statute setting a uniform federal judgment rate of interest, 28 U.S.C. § 1961, was not established until 1948. *See* Pub. L. 80-773, 62 Stat. 869, 957–58 (1948). Accordingly, a creditor's entitlement to postpetition interest accruing on debt would have naturally been understood to arise from state law, either pursuant to the parties' contracts or the applicable default state law rate. *See* *American Iron*, 233 U.S. at 266–67, 34 S.Ct. 502 (awarding the state law default rate in a solvent-debtor receivership case).

4 The Dissent correctly recognizes the Supreme Court's admonition that pre-Code practice cannot abrogate the Code's plain text. *See* Dissent at 1065–66. But for the reasons discussed below, we cannot say the Code's text is clear that the equitable solvent-debtor exception does not apply to creditors who are designated as unimpaired. *See infra* at 1058–59. And pre-Code practice remains relevant to the construction of provisions that are "subject to interpretation" or contain ambiguities. *Hartford Underwriters*, 530 U.S. at 10, 120 S.Ct. 1942 (quotations omitted). Moreover, as we explain, the Dissent's reading of the Code cannot be squared with Congress' subsequent action to amend the Code after its passage. *See infra* at 1060, 1061–62.

5 The second exception, which applies to oversecured creditors and is located at 11 U.S.C. § 506(b), is not relevant to this dispute.

6 The Dissent claims there is "no basis" for distinguishing between interest payments made *on* as opposed to *part of* an allowed claim. Dissent at 1067. Yet it is the Dissent that ignores both the text of § 502(b)(2) and the weight of authority acknowledging this difference. *See* *Ultra Petroleum*, 624 B.R. at 195; *Mullins*, 633 B.R. at 15; *Energy Future Holdings*, 540 B.R. at 111.

7 Seeking to overcome the lack of any statute applying § 726(a)(5) to unimpaired creditors, PG&E next argues that payment of postpetition interest in bankruptcy is analogous to payment of interest on a judgment in federal court. It is true that *Cardelucci* made such a comparison, albeit in dicta. *See* *Cardelucci*, 285 F.3d at 1235. PG&E reasons that Congress, by applying § 726(a)(5) to unsecured creditors via the best-interests test, confirmed that all awards of postpetition interest to such creditors, regardless of impairment status, are akin to awards of post-judgment interest given at the federal judgment rate.

We are not convinced. Once again, PG&E cannot overcome the fatal flaw in its argument: no statute applies § 726(a)(5) and its limited award of postpetition interest "at the legal rate" to unimpaired claims. Thus, there is no "clear indication" that Congress meant to modify the solvent-debtor exception to limit unimpaired creditors to interest at this amount. *Cohen*, 523 U.S. at 221, 118 S.Ct. 1212.

Moreover, we disagree with PG&E that the historic cases discussing the solvent-debtor exception treated awards of postpetition interest as akin to post-judgment interest. PG&E points to passing language from

Johnson, a Fifth Circuit case, noting that another court had compared allowed bankruptcy claims to judgments. *See* *Johnson*, 190 F. at 465 (citing *In re John Osborn's Sons & Co.*, 177 F. 184 (2d Cir. 1910)). But PG&E directs us to no other historic case that made such a comparison. To the contrary, cases applying the solvent-debtor exception under the Bankruptcy Act repeatedly emphasized that the equitable purpose of the exception was to require debtors to honor their "expressly-bargained-for" contracts, lest they realize a windfall. *Ruskin*, 269 F.2d at 832; *see also, e.g.,* *Chicago, Milwaukee*, 791 F.2d at 528; *Debentureholders*, 679 F.2d. at 270.

8 Plaintiffs note that some courts (including one circuit court) have held that, in a solvent-debtor scenario, a "fair and equitable" plan under § 1129(b)(1) may require paying unsecured creditors interest at the contractual rate before the debtor can receive surplus value. *See* *Dow Corning*, 456 F.3d at 677–78; *Mullins*, 633 B.R. at 20. We express no opinion on this issue, but merely point out that PG&E's designation of plaintiffs as unimpaired precluded them from potentially making this argument to the bankruptcy court.

9 The Dissent would hold that the "equitable rights" referred to by § 1124(1) encompass only a single right: the "right to an equitable remedy for breach of performance," which is part of a claim pursuant to 11 U.S.C. § 101(5). Dissent at 1067, 1073–74. But this novel reading relies on the faulty premise that the "equitable rights" contemplated by § 1124(1) encompass only those rights that are part of an allowed claim. Numerous courts have rejected this logic, holding that a claim may entitle its holder to postpetition interest as an equitable right when a debtor is solvent, even though such a right is not part of the claim itself. *See, e.g.,* *Ultra Petroleum*, 624 B.R. at 203–04, *Energy Future Holdings*, 540 B.R. at 124, *supra* at 1073–74. That § 101(5) indisputably confers a statutory right to an equitable remedy *as part of a claim* is hardly grounds for construing § 1124(1)'s reference to equitable rights in the narrow fashion advocated by the Dissent. This is especially true, given that the Dissent's construction would conflict with the ample textual, historical, and structural evidence we survey above supporting the solvent-debtor exception's survival under the Code. *See supra* at 1057–61.

Moreover, we do not hold (as the Dissent asserts) that claims "retroactively" become impaired when a creditor of a solvent debtor is denied postpetition interest. Dissent at 1074. Impairment is a concept rooted in § 1124, "the plain language of [which] says that a creditor's claim is 'impaired' unless its rights are left 'unaltered' *by the Plan.*" *L&J Anaheim*, 995 F.2d at 943 (emphasis added); *see also* *PPI Enters.*, 324 F.3d at 204 ("Impairment results from what the *plan* does ...." (quotation omitted) (emphasis in original)). Our holding "recognizes that the equitable prong of § 1124 applies differently when the debtor is solvent"—as PG&E undisputedly is in this case—by entitling claim holders to postpetition interest as an equitable right. *Ultra Petroleum*, 624 B.R. at 203. A failure by a bankruptcy plan to leave this equitable right unaltered results in impairment from the outset, unless and until a plan is amended accordingly.

10 Although we rely on the text, history, and structure of the Code to reach today's result, even the Dissent's authorities acknowledge that pre-Code practice is relevant in interpreting sections of the Code that are otherwise incoherent or inconsistent. *See, e.g.,* *United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 240–41, 109 S.Ct. 1026, 103 L.Ed.2d 290 (1989).

11 As our sibling circuits have held, an alteration of pre-bankruptcy rights that occurs by operation of the Code does not result in impairment. *Ultra Petroleum*, 943 F.3d at 763 ("The plain text of § 1124(1) requires that 'the plan' do the altering."); *PPI Enters.*, 324 F.3d at 204 ("[W]e must examine whether the plan itself is a source of limitation on a creditor's legal, equitable, or contractual rights."); *see also* *In re Sylmar Plaza, L.P.*,

314 F.3d 1070, 1075 (9th Cir. 2002) ("In enacting the Bankruptcy Code, Congress made a determination that an eligible debtor should have the opportunity to avail itself of a number of Code provisions which adversely alter creditors' contractual and nonbankruptcy rights." (quotation omitted)).

12 The record fails to disclose, for example, the extent of PG&E's solvency post-bankruptcy, or the precise amount of postpetition interest that would be owed to plaintiffs were the contract or default state law rates enforced.

1 *See* *Gencarelli v. UPS Cap. Bus. Credit*, 501 F.3d 1, 6 n.2 (1st Cir. 2007) (noting that § 502(b)(2) is an "explicit statutory provision" that bars post-petition interest); *SummitBridge Nat'l Invs. III, LLC v. Faison*, 915 F.3d 288, 295 (4th Cir. 2019) (describing § 502(b)(2) as a "general rule against allowance" of post-petition interest); *Matter of Johnson*, 146 F.3d 252, 260 (5th Cir. 1998) ("Post-petition interest is disallowed against the bankruptcy estate under section 502." (citation omitted)); *In re Kentucky Lumber Co.*, 860 F.2d 674, 676 (6th Cir. 1988) (citing § 502(b)(2) to explain the "general rule of actions in bankruptcy [ ] that unsecured creditors are not entitled to postpetition interest upon their allowable claims"); *Matter of Fesco Plastics Corp., Inc.*, 996 F.2d 152, 155 (7th Cir. 1993) ("[C]reditors cannot recover post-petition interest on their claims. This rule has been written into the Bankruptcy Code at 11 U.S.C. § 502(b)(2)."); *Bursch v. Beardsley & Piper, a Div. of Pettibone Corp.*, 971 F.2d 108, 114 (8th Cir. 1992) ("In general, under section 502(b), a creditor is not entitled to postpetition prejudgment interest because such interest is unmatured at the time of filing."); *United States v. Victor*, 121 F.3d 1383, 1387 (10th Cir. 1997) ("Section 502(b) does not simply prohibit certain creditors from filing a proof of claim for post-petition interest; it prohibits those creditors from collecting the interest from the bankruptcy estate.").

2 A claim may be unimpaired even if the holder of the claim is deprived of a contractual or legal right to demand accelerated payment under certain circumstances. 11 U.S.C. § 1124(2).

3 The best interest of creditors test is also available in a Chapter 12 or Chapter 13 bankruptcy, *see* 11 U.S.C. § 1225(a)(4) and § 1325(a)(4).

4 Congress specified other circumstances where post-petition interest was allowed. Congress permitted an award of contract-rate interest for creditors holding secured claims, up to the amount of the creditor's collateral. *See* 11 U.S.C. § 506(b). Undersecured creditors are not entitled to post-petition interest. *Timbers of Inwood Forest*, 484 U.S. at 373, 108 S.Ct. 626. In a Chapter 13 bankruptcy, Congress also allowed for post-petition interest on nondischargeable debts "to the extent that the debtor has disposable income available to pay such interest after making provision for full payment of all allowed claims," 11 U.S.C. § 1322(b)(10). Nondischargeable debts are specified in 11 U.S.C. § 523 and include tax debts, *id.* § 523(a)(1), debts for money procured through fraud, *id.* § 523(a)(2), and restitution payments under Title 18, *id.* § 523(a)(13).

5 The majority's reliance on *Midlantic Nat. Bank v. New Jersey Dept. of Environmental Protection*, 474 U.S. 494, 106 S.Ct. 755, 88 L.Ed.2d 859 (1986), and *BFP v. Resolution Trust Corporation*, 511 U.S. 531, 114 S.Ct. 1757, 128 L.Ed.2d 556 (1994), is equally flawed. *BFP* relied on pre-Code practice merely to clarify the meaning of an ambiguous phrase, *see* 511 U.S. at 543, 546–47, 114 S.Ct. 1757, and *Midlantic*

relied on pre-Code practice to "fill in the details" of the "codification of trustee's abandonment power" that "the Code had adopted without elaboration," *Hartford*, 530 U.S. at 11, 120 S.Ct. 1942.

6 Another case relied on by the majority, *Debentureholders Protective Comm. of Cont'l Inv. Corp. v. Cont'l Inv. Corp.*, 679 F.2d 264, 265 (1st Cir. 1982), was also decided pursuant to the Bankruptcy Act, not the Code, *see id.*

7 Specifically, according to the report, with this deletion "if a plan proposed to pay a class of claims in cash in the full allowed amount of the claims, the class would be impaired, entitling creditors to vote for or against the plan of reorganization," which would protect dissenting creditors by requiring compliance with the "best interests of creditors" test under § 1129(a)(7) of the Bankruptcy Code. H.R. Rep. No. 103-835, § 214 at 48.

8 The majority confuses legislative history with legislation by referring to statements in this House Judiciary Committee report as "Congress' clear instruction on this matter," Maj. at 1062, and as Congress's "express[ ]" statement that it intended to prevent the "unfair result" in *New Valley*. Maj. at 1061–62. But "the best evidence" of Congress's instruction on a matter "is the statutory text adopted by both Houses of Congress and submitted to the President." *W. Virginia Univ. Hosps., Inc. v. Casey*, 499 U.S. 83, 98–99, 111 S.Ct. 1138, 113 L.Ed.2d 68 (1991). "[W]here, as here, the statute's language is plain, the sole function of the courts is to enforce it according to its terms," and "reference to legislative history and to pre-Code practice is hardly necessary." *Ron Pair Enterprises, Inc.*, 489 U.S. at 241, 109 S.Ct. 1026.

9 As a threshold matter, the argument fails because the members of the Trade Committee did not distinctly argue to the bankruptcy court that their claims were impaired, and such an argument is therefore forfeited.

10 Indeed, in enacting § 101(5), Congress intended to "adopt the broadest available definition of 'claim,' " including any "enforceable obligation," be it legal or equitable. *Johnson v. Home State Bank*, 501 U.S. 78, 83, 111 S.Ct. 2150, 115 L.Ed.2d 66 (1991); *see also* *In re Davis*, 778 F.3d 809, 813 (9th Cir. 2015) (explaining that the language of § 101(5) "permits the broadest possible relief in the bankruptcy court") (quoting H.R. Rep. 95-595, 309 (1978)).

11 The majority argues that reading § 1124(1) as referring only to equitable rights that are part of the allowed claim is "novel" and based on a "faulty premise." Maj. at 1062–63 n.9. To the contrary, it is based on the plain language of § 1124(1), and the definition of "claim" in § 101(5).

12 The solvency of a debtor may not be known at the time the petition is filed. *See, e.g.,* *In re Kentucky Lumber Co.*, 860 F.2d 674, 675 (6th Cir. 1988) (describing a debtor that was "clearly perceived as insolvent on the date of confirmation of the plan" but "subsequently achieved a large and unexpected structured settlement" rendering the debtor solvent). Accordingly, the majority's statement that "[a] failure by a bankruptcy plan to leave this equitable right unaltered results in impairment *from the outset*, unless and until a plan is amended accordingly," Maj. at 1063 n.9 (emphasis added), indicates that either *every* plan must include the statement that all unimpaired creditors are entitled to post-petition interest if the debtor turns out solvent, or that by force of law, the failure to distribute post-petition interest at the end of the bankruptcy case causes a nunc pro tunc transformation of a claim to the status of impairment "from the outset."

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637 B.R. 781
United States Bankruptcy Court, D. Delaware.

IN RE: The HERTZ CORP., et al., Debtors.
Wells Fargo Bank, N.A., as Indenture Trustee, Plaintiffs,
and
US Bank, as Indenture Trustee, Intervenor-Plaintiff,
v.
The Hertz Corp., et al., Defendants.

Case No. 20-11218 (MFW) Jointly Administered
|
Adv. No. 21-50995 (MFW)
|
Signed December 22, 2021

Synopsis
Background: Indenture trustee brought adversary complaint on behalf of unsecured noteholders, seeking declaratory judgment that Chapter 11 debtors, which had issued notes prepetition, were required to pay redemption premium and/or postpetition interest allegedly due under notes. Debtors filed motion to dismiss for failure to state claim.

Holdings: The Bankruptcy Court, Mary F. Walrath, J., held that:

whether debtors were required to pay redemption premium depended on terms of redemption provision, not acceleration clause;

debtors' redemption of notes was optional, as required for liability for redemption premium;

term "maturity," as used in redemption provision, referred to acceleration caused by bankruptcy filing;

notes were redeemed after "maturity," so that debtors were not required to pay redemption premium;

debtors were required to pay premium for second set of notes for which governing redemption provision did not mention "maturity";

noteholders plausibly alleged that claim for redemption premium was not economic equivalent of unmatured interest disallowed by Code; and

noteholders were not "impaired" creditors within meaning of Code.

Motion granted in part and denied in part.

Procedural Posture(s): Petition for Declaratory Judgment; Motion to Dismiss for Failure to State a Claim.

Attorneys and Law Firms

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Rel. Docs. 5, 15, 16, 17

MEMORANDUM OPINION [1]

Mary F. Walrath, United States Bankruptcy Judge

Before the **Court** **is** the **Debtors**' **Motion** **to** **Dismiss** the **complaint** **filed** **by** the **Indenture** **Trustees**, **on** **behalf** **of** the **holders** **of** **a** **series** **of** **unsecured** **notes** **issued** **by** the **Debtors** **pre-petition** (the "Noteholders"), for recovery of a redemption premium and/or post-petition interest allegedly due under the Notes. For the reasons stated below, the Court will grant in part and deny in part the Debtors' Motion to Dismiss the redemption premium count and grant the Debtors' Motion to Dismiss the post-petition interest count.

I. BACKGROUND

On May 22, 2020, the Hertz Corporation and its affiliates (collectively "the Debtors") filed voluntary petitions under chapter 11 of the Bankruptcy Code. The filing was due in large part to the disruption caused to travel and its business operations by the Covid-19 pandemic. (D.I. 28 ¶¶ 3-9.) [2] After a downsizing of their fleet and a sale of a non-core part of their business, the Debtors obtained an offer from a proposed plan sponsor. After designating a stalking horse bidder and conducting an auction process, the Debtors selected a winning bidder and filed the Second Modified Third Amended Plan of Reorganization ("the Plan") to effectuate a reorganization in accordance with that bid. (D.I. 5178.) The Plan provided generally for payment in full in cash on the effective date to creditors plus post-petition interest to the effective date at the federal judgment rate or in the amount necessary to render them unimpaired and a distribution to shareholders of cash and new warrants or subscription rights. (Id. at Art. III.B.) The Plan was accepted by the shareholders. (D.I. 5181.) On June 10, 2021, the Court confirmed the Plan. (D.I. 5261.) The Confirmation Order preserved the rights of the Noteholders to assert entitlement to a make-whole premium and additional interest and other claims as necessary to render their claims unimpaired, as well as the Debtors' right to object to those claims. (Id. at ¶¶ 26 & 27.) The Plan went effective on June 30, 2021 (the "Effective Date"). (D.I. 5477.)

On July 1, 2021, Wells Fargo Bank, N.A. ("Wells Fargo"), as Indenture Trustee for a series of unsecured notes issued by the Debtors pre-petition (the "Senior Notes"), filed a complaint seeking a declaratory ***784** judgment that, in addition to the principal and pre-petition interest paid to the Senior Noteholders on the Effective Date (in excess of $2.7 billion), the Debtors must pay approximately $272 million consisting of (1) a make-whole premium due under the Senior Notes (totaling approximately $147 million) and (2) post-petition interest on their claims at the contract default rate in excess of the federal judgment rate (approximately $125 million). (Adv. D.I. 1 at Ex. A.) US Bank, N.A. ("US Bank"), as Indenture Trustee for the 7% Unsecured Promissory Noteholders, intervened as a plaintiff seeking relief only on the second claim. (Adv. D.I. 14.)

On August 2, 2021, the Debtors filed a Motion to Dismiss both counts for failure to state a claim. The Motion was fully briefed and oral argument was held on November 9, 2021. The matter is ripe for decision.

II. JURISDICTION

The Court has subject matter jurisdiction over this adversary proceeding. 28 U.S.C. §§ 157, 1334. The Court has the power to enter a final judgment in this adversary because it concerns the allowance of claims against the estate. 28 U.S.C. § 157(2)(A) & (O). Stern v. Marshall, 564 U.S. 462, 499, 131 S.Ct. 2594, 180 L.Ed.2d 475 (2011). In addition, the parties have consented to entry of a final order by this Court. (Adv. D.I. 1 at ¶ 39, 5 at ¶12 & 14 at ¶ 15.) Wellness Int'l Network, Ltd. v. Sharif, 575 U.S. 665, 135 S.Ct. 1932, 191 L.Ed.2d 911 (2015) (holding that even where Article III concerns would preclude the bankruptcy court from entering final judgment over a party's opposition, a court may do so if the parties consent).

III. DISCUSSION

A. Standard of Review

A Rule 12(b)(6) motion challenges the sufficiency of the factual allegations in the complaint. Kost v. Kozakiewicz, 1 F.3d 176, 183 (3d Cir. 1993). To survive a motion to dismiss, the complaint must contain sufficient factual matter, accepted as true, "to state a claim to relief that is plausible on its face." Bell Atl. Corp. v. Twombly, 550 U.S. 544, 570, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007). A claim is facially plausible when "the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." Ashcroft v. Iqbal, 556 U.S. 662, 678, 129 S.Ct. 1937, 173 L.Ed.2d 868 (2009) (citing Twombly, 550 U.S. at 556, 127 S.Ct. 1955). The court must draw all reasonable inferences in favor of the plaintiff. E.g., Alpizar-Fallas v. Favero, 908 F.3d 910, 914 (3d Cir. 2018).

In weighing a motion to dismiss, the court should undergo a three-part analysis. "First, the court must take note of the elements needed for a plaintiff to state a claim." Santiago v. Warminster Twp., 629 F.3d 121, 130 (3d Cir. 2010) (citing Iqbal, 556 U.S. at 675, 129 S.Ct. 1937). Second, the court must separate the factual and legal elements of the claim, accepting all of the complaint's well-pled facts as true and disregarding any legal conclusions. Id.; Fowler v. UPMC Shadyside, 578 F.3d 203, 210 (3d Cir. 2009) (citing Iqbal, 556 U.S. at 679, 129 S.Ct. 1937). Third, the court must determine whether the facts alleged in the complaint are sufficient to show that the plaintiff has a plausible claim for relief. Santiago, 629 F.3d at 130.

The Court may consider documents to which the complaint refers if they are central to the claim and no party questions their authenticity. Marder v. Lopez, 450 F.3d 445, 448 (9th Cir. 2006). See also Chambers v. Time Warner, Inc., 282 F.3d 147, 153 n.3 (2d Cir. 2002).

***785** B. Redemption Premium

In Count 1 of the Complaint, Wells Fargo seeks a declaratory judgment that the Debtors must pay the redemption premium provided in the Senior Notes because they were redeemed prior to their maturity.

The Debtors seek to dismiss this count for failure to state a claim asserting that (a) no redemption premium is allowed under the express language of the Indentures or (b) the redemption premium is unmatured interest which must be disallowed under the Bankruptcy Code. Wells Fargo disputes both of these contentions.

1. Terms of the Indentures [3]

a. Acceleration Clause

The Debtors rely initially on section 602 of the Indentures which provides that upon the filing of a bankruptcy petition the Senior Notes are automatically accelerated and "the principal of and accrued but unpaid interest on all Outstanding Notes of such series will ipso facto become immediately due and payable without any declaration or other act on the part of the Trustee or any Holder." Because section 602 does not provide for the payment of any redemption premium on acceleration, the Debtors contend that none is due.

Wells Fargo responds that the Debtors' argument must be rejected based on controlling Third Circuit precedent. In re Energy Future Holdings Corp., 842 F.3d 247 (3d Cir. 2016) (hereafter "EFH"). In EFH, Wells Fargo contends, the Third Circuit considered similar language in acceleration clauses under New York law [4] and concluded that the issue of whether a redemption premium was due depended not on the terms of the acceleration clause, but on the terms of the redemption provision. 842 F.3d at 257-60.

The Debtors seek to distinguish EFH by noting that the language in the two series of notes at issue in that case provided that on acceleration all "outstanding Notes" were due or all "principal, interest, and applicable premium" were due. Id. at 254, 257. Therefore, they assert that the Third Circuit held that the acceleration clause and the redemption provision were not in conflict. Id. at 256. In contrast, they contend that the acceleration clause in this case, which provides for payment only of "the principal of and accrued but unpaid interest," cannot be read in harmony with the redemption provision which requires payment of an additional premium.

The Court finds that argument is a distinction without significance. While the Third Circuit rejected the EFH debtor's argument that the acceleration and redemption provisions in that case were in conflict, it concluded that the two sections "simply address different things: § 6.02 causes the maturity of EFHI's debt to accelerate on its bankruptcy, and § 3.07 causes a make-whole to become due when there is an optional redemption before" the maturity date. Id. The Third Circuit concluded that the redemption provision "is the only provision that specifically addresses redemption." Id. That conclusion applies to the Senior Notes in this case, as well. Therefore, the Court concludes that the acceleration clause in the Indentures is not the operative provision in determining whether the redemption premium is due.

b. Redemption Provision

The Debtors argue that, even under the language of the redemption provision, no ***786** redemption premium is due on the Senior Notes for several reasons.

i. At the Debtors' Option

The Debtors argue, initially, that for any redemption premium to be due, the redemption must have been "at the [Debtors'] option." [5] They contend that the Senior Notes were not redeemed at the Debtors' option. They assert that they were forced to file bankruptcy because of the collapse of their business due to the pandemic. The Debtors argue that, upon the bankruptcy filing, the Senior Notes were automatically accelerated and required to be paid in full. E.g., In re MPM Silicones, L.L.C., 874 F.3d 787, 803 (2d Cir. 2017) (holding that payment was mandated by acceleration of the notes on the filing of bankruptcy and therefore that payment was not a voluntary redemption by the debtor).

Wells Fargo disagrees, arguing that the MPM case on which the Debtors rely is contrary to the decision in EFH which is binding on this Court. It argues that the Third Circuit in EFH specifically concluded that the automatic acceleration caused by a bankruptcy filing did not make any later redemption nonvoluntary. EFH, 842 F.3d at 255.

The Court agrees with Wells Fargo. The Third Circuit in EFH expressly held that the mere acceleration of notes as a result of a bankruptcy filing does not mean that the debtor in that case could not be liable for a redemption premium upon subsequently redeeming the notes. Id. Although MPM is to the contrary, it is not the law in this Circuit. The Third Circuit in EFH disagreed with the bankruptcy court's decision which was upheld in MPM and distinguished the AMR decision (on which the Second Circuit relied in MPM). 842 F.3d at 258-60 (citing In re AMR Corp., 730 F.3d 88 (2d Cir. 2013)).

The Debtors assert, nonetheless, that EFH is distinguishable because, unlike the debtor in that case, they did not file bankruptcy in a strategic effort to avoid the payment of a redemption premium. Id. at 251. [6]

Wells Fargo disagrees, noting that there is nothing in EFH requiring an intent to avoid the make-whole obligation in order to find that a redemption of notes is voluntary. Wells Fargo argues that no court has held that if an issuer does not have an intent to avoid the redemption provision, its action is not voluntary. Instead, Wells Fargo asserts that the cases which find a redemption involuntary are predominately cases where the acceleration was at the lenders' option. [7]

The Court agrees with Wells Fargo. The EFH Court did not conclude that the voluntariness of the redemption was dependent on a finding that the debtor filed bankruptcy to avoid the obligation to pay the noteholders a redemption premium. Instead, the Third Circuit found that the debtor had filed a voluntary petition in bankruptcy and once in bankruptcy, had the option to reinstate the notes. ***787** EFH, 842 F.3d at 255. The other cases cited by the Debtors are similarly distinguishable. [8] In fact, several cases have found a redemption voluntary even where the issuer acted in the utmost good faith. [9]

Finally, the Debtors argue that any option to reinstate the Senior Notes was hypothetical at best. They contend that they could not continue to operate without filing bankruptcy because they lost over 90% of their revenues as a result of the pandemic. Further, they argue that they had no ability to formulate a plan that reinstated the Senior Notes because they received no offers that allowed that option. Rather, the Debtors assert that, once in bankruptcy, they had a fiduciary duty to accept the highest and best bid they received at the auction, which precluded the reinstatement of the Senior Notes. Therefore, the Debtors argue that the repayment of the Senior Notes pursuant to the terms of the Plan was not a redemption "at the Company's option" which is necessary to trigger the requirement to pay the redemption premium.

Wells Fargo argues that the Debtors' bankruptcy filing was a strategic, voluntary decision and that the Debtors had many options for restructuring their obligations once in bankruptcy, including specifically the choice to reinstate the Senior Notes. 11 U.S.C. § 1124(2). It, therefore, contends that the Plan which was filed by the Debtors and ultimately confirmed was a redemption of the Senior Notes at the Debtors' option.

The Court agrees with Wells Fargo. The Third Circuit found, in concluding that the redemption of notes in EFH was voluntary, that the debtor there "filed for Chapter 11 protection voluntarily. Once there, it had the option, per its plan of reorganization, to reinstate the accelerated notes' original maturity date under Bankruptcy Code § 1124(2) rather than paying them off immediately. It chose not to do so." EFH, 842 F.3d at 255.

Similarly, in this case the Debtors filed a voluntary petition in bankruptcy. It was perhaps the best option for the Debtors in light of the drastic effects on their business caused by the pandemic, but it was not the only option. Further, while the Debtors chose to conduct an auction for a plan sponsor and ultimately selected the highest and best offer, that too was not the Debtors' only option. At numerous junctures in any bankruptcy case, a debtor in possession has multiple paths from which to choose. That the Debtors here chose a path that resulted in a fantastic result for all of their creditors and shareholders does not mean that it was not a voluntary choice. Even though the Debtors acted in good faith and in the fulfillment of their fiduciary duties, the Court concludes that their actions were voluntary. As noted above, courts have found that even actions taken in good faith and in fulfillment of a ***788** debtor's fiduciary duty can be voluntary resulting in liability for a redemption premium. See cases discussed in note 9, supra.

Therefore, the Court concludes that Wells Fargo has alleged sufficient facts which, accepted as true, state a facially plausible claim that the redemption of the Senior Notes was at the Debtors' option. Twombly, 550 U.S. at 570, 127 S.Ct. 1955.

ii. Applicability of Section 6(a)

The Debtors further argue that, even if the redemption is determined to be voluntary, no redemption premium is due under the express terms of the Indentures because they were redeemed after they matured upon the bankruptcy filing. The Debtors rely preliminarily on section 6(a) of the Supplemental Indentures which provides that the "[Senior] Notes will be redeemable, at the Company's option, in whole or in part, at any time and from time to time on or after [a specified date] and prior to maturity thereof at the applicable redemption price set forth below." (Adv. D.I. 5, Exs. B, D, E & G (emphasis added).)

a. 2022/2024 Senior Notes

Wells Fargo concedes that section 6(a) is the provision applicable to the 2022/2024 Senior Notes. It argues, however, that the term "prior to maturity" in section 6(a) means prior to the original maturity date of the Senior Notes in 2022 and 2024. Because the Debtors redeemed the Senior Notes before the date that they were due to mature, Wells Fargo contends that the redemption premium is due.

The Debtors respond that the Indentures contained a defined term (the "Stated Maturity") for the date when each of the series of Senior Notes was originally due. They argue that the failure to use that defined term in section 6(a) establishes that the phrase "prior to maturity" must mean something broader than that specific date. They cite several other sections of the Indentures which distinguish Stated Maturity from maturity arising "on acceleration" or "otherwise." (Adv. D.I. 5, Exs. A, C, E, G at §§ 1301(a), 601(ii), 301(6).) The Debtors also argue that if "prior to maturity" simply meant the Stated Maturity date, that it would have been unnecessary (and mere surplusage) [10] to include the term at all because the chart in section 6(a) makes reference to what premium is due at all times prior to the Stated Maturity date.

The Court agrees with the Debtors' analysis. The date when the Senior Notes are due is a defined term, Stated Maturity. If section 6(a) was meant to apply only to redemptions before the Stated Maturity date, rather than prior to a maturity caused by some other event, such as a bankruptcy filing, it would have used the term Stated Maturity. Further, if the phrase simply meant redemption prior to the Stated Maturity it would have been surplusage, because the chart included in that section stated what needed to be paid at any time before the Stated Maturity date.

Accordingly, the Court concludes that the undefined term "maturity" in section 6(a) must refer to the common meaning of maturity, which under the terms of the Senior Notes includes upon the acceleration caused by a bankruptcy filing. E.g., Sapp v. Indus. Action Servs., LLC, C.A. No. 19-912-RGA, 2020 WL 2813176, at *3 (D. Del. May 29, 2020) ("[W]hen the same term appears in different sections of the agreement and is capitalized in one section but not the other, the non-capitalized term will have its 'ordinary, plain meaning.' ") (citing ***789** Derry Finance N.V. v. Christiana Cos., 797 F.2d 1210, 1214 (3d Cir. 1986)). This interpretation is confirmed by sections 601(ii) and 301(6) of the Indentures which use the lower case term "maturity" in reference to acceleration of the Senior Notes on bankruptcy or a default.

Therefore, under the express terms of section 6(a) of the redemption provision, the Court concludes that Wells Fargo has failed to state a plausible claim that a redemption premium is due on the 2022/2024 Senior Notes because they were redeemed after the initial period stated therein but not prior to the maturity arising as a result of the bankruptcy filing. Therefore, the Court will grant the Motion to Dismiss Count 1 as to the 2022/2024 Senior Notes.

b. 2026/2028 Senior Notes

The Debtors argue that the same result applies to the Senior Notes originally due to mature in 2026 and 2028.

Wells Fargo responds that section 6(a) is not applicable to those Senior Notes because they were not redeemed "on or after" the date specified in that section. Instead, it contends that section 6(c) governs, which provides that "At any time prior to [the specified date], the [Senior Notes] may also be redeemed (by the Company or any other person) in whole or in part, at the Company's option, at ... the Redemption Price ...."

The Debtors assert, however, that section 6(a) is incorporated in full into section 6(c) because the latter provides circumstances under which the Senior Notes may "also" be redeemed.

Wells Fargo responds that if "also" meant that all of section 6(a) was incorporated into section 6(c) then there would have been no need to repeat provisions from section 6(a) in section 6(c) such as "at the Company's option" and "in whole or in part."

The Court agrees with Wells Fargo that the use of "also" in section 6(c) does not mean that all of section 6(a) is incorporated into section 6(c). If it did, section 6(c) would contain surplusage, which is to be avoided in contract interpretation. E.g., Burlington Ins., 57 N.Y.S.3d 85, 79 N.E.3d at 482. It would also create an internal contradiction: section 6(a) is only applicable if redemption occurs after a specified date, while section 6(c) applies only if redemption occurs before that date, and each section provides a different redemption price. Rather than accept the Debtors' tortured reading, the Court reads section 6(c) as simply providing the Debtors with the ability to redeem under the circumstances in that section, in addition to their redemption rights under section 6(a). While redemption under section 6(a) requires that it occur before maturity, section 6(c) contains no such requirement.

Therefore, the Court concludes that Wells Fargo has stated a plausible claim, under the express terms of section 6(c) of the redemption provision, that a premium would be due on the 2026/2028 Senior Notes because they were redeemed before the initial period stated therein.

2. Economic Equivalent of Interest

The Debtors argue that, even if the redemption premium is due under the terms of the 2026/2028 Senior Notes, however, it cannot be an allowed claim because section 502(b)(2) of the Bankruptcy Code expressly provides that any claim for unmatured interest must be disallowed. Although that term is not defined in the Code, the Debtors assert that courts look to substance over form and have disallowed claims that are the "contractual equivalent" of future interest. [11] The Debtors ***790** also note that, although the Third Circuit did not directly address this issue in EFH, it characterized a redemption premium as the "contractual substitute for interest lost on Notes redeemed before their expected due date." 842 F.3d at 251. [12]

Wells Fargo argues that the redemption premium is not interest. It contends that interest is a payment for the "use" of money, while the redemption premium is being paid to the Senior Noteholders for the Debtors' "failure to use" their money. Wells Fargo asserts that, unlike interest, the redemption premium does not accrue over time but is a fixed one-time charge upon redemption, and, unlike interest, the redemption premium is contingent: it is only due if the Debtors redeem the Senior Notes in accordance with the terms of the redemption provision. Wells Fargo contends that the redemption premium is intended to compensate the Senior Noteholders for the uncertainty and potential losses incurred in reinvesting that money in a different market environment, which implicates numerous factors beyond simply the periodic payment of interest. It argues that the majority of courts agree, holding that redemption premiums are not unmatured interest. [13]

While the cases cited by Wells Fargo are useful, the Court notes that there is a minority of courts who disagree. [14] Further, although the Third Circuit in EFH described a redemption premium as the "contractual substitute for interest lost on Notes redeemed before their expected due date," it was not addressing the issue of whether it could be characterized as such to preclude its payment under section 502(b)(2). 842 F.3d at 251, 253 n.1. Similarly, while the Fifth Circuit in Ultra Petroleum suggested that some make-wholes may be the equivalent of unmatured interest, it did not decide whether the ones in that case were, instead remanding the issue ***791** to the bankruptcy court. 943 F.3d at 765. [15]

The Court is not prepared to conclude, as a legal matter, that make-wholes cannot be disallowed as unmatured interest as

Wells Fargo, the cases it cites, and academics [16] suggest. Calling a make-whole a contract right or a liquidated damages provision does not answer the question of whether it is unmatured interest. [17] In deciding whether a charge is unmatured interest "courts look to the economic substance of the transaction to determine what counts as interest." Doctors Hosp., 508 B.R. at 705. If it were enough to just label a make-whole claim liquidated damages, damages for breach of contract, or a "separate contract right" from the obligation to pay interest, then a contract providing that on default or redemption "all unmatured interest" would be immediately due and payable could avoid the effect of section 502(b)(2) completely. This is contrary to the express provisions of the Code and, consequently, the Court concludes that the characterization of a make-whole as a contract right or liquidated damages is not dispositive.

Instead, the Court concludes that the determination of whether the redemption premium that Wells Fargo seeks in this case is, in fact, the economic equivalent of unmatured interest is not a legal question, but is instead a factual one: namely whether the redemption provision in the 2026/2028 Senior Notes is actually the economic equivalent of unmatured interest.

In considering the actual language of the redemption premium in this case, the Court finds it significant that it is calculated, in large part, on the present value of the unmatured interest due on the Senior Notes as of the Redemption Date. [18] At oral argument, Wells Fargo presented a powerpoint that appeared to suggest, however, that the redemption provision was much less than a simple present value of the unmatured interest and very favorable to the Debtors because it is tied to the Treasury rate. That was, of course, merely ***792** argument and no evidence was presented to support that assertion. Nor did the Debtors have an opportunity to rebut the assertion with any evidence. Instead, the Debtors argued that the test is not whether the redemption premium equals the unpaid interest but whether it is the economic equivalent of the interest which the Senior Noteholders will not receive because of the early redemption of the Senior Notes. Doctors Hosp., 508 B.R. at 705-06.

The presentation by Wells Fargo (and the language of the redemption provision itself), however, are sufficient to convince the Court that Wells Fargo has stated a plausible claim for relief. Santiago, 629 F.3d at 130. While the redemption premium clearly was not due until the redemption occurred on the Effective Date of the Plan and, therefore, was "unmatured" as of the petition date, the Court concludes that Wells Fargo may be able to present evidence that the redemption premium in the 2026/2028 Senior Notes is not, in fact, the economic equivalent of unmatured interest due under those Senior Notes.

Accordingly, the Court concludes that Count 1 of the Complaint states a claim that is plausible on its face that the Debtors must pay the redemption premium on the 2026/2028 Senior Notes but does not state a plausible claim that the Debtors must pay the redemption premium on the 2022/2024 Senior Notes. Accordingly, the Court will grant the Debtors' Motion to Dismiss Count 1 as to the 2022/2024 Senior Notes but deny the Debtors' Motion as to the 2026/2028 Senior Notes.

3. Other Arguments

Wells Fargo also contends, however, that regardless of how the redemption provision is characterized, that portion of the Senior Noteholders' claim cannot be disallowed because the Debtors treated their class as unimpaired in the Plan, thereby precluding them from voting on the Plan. As a result, Wells Fargo contends that the Debtors cannot impair any of the Senior Noteholders' legal, contractual, or equitable rights and must pay the Senior Noteholders all that they are entitled to receive under the Indentures and under equity. 11 U.S.C. § 1124(1). The failure to pay the Senior Noteholders their contractual entitlement to the redemption premium, Wells Fargo contends, impairs the Senior Noteholders' contractual and equitable rights. It also argues that, because the Debtors were "wildly solvent" (returning in excess of $ 1.5 billion to equity holders), the Senior Noteholders are entitled to all of their contract rights (including the make-whole even if it is unmatured interest) under the "solvent debtor exception."

The Debtors argue that the "impairment" and the "solvent debtor exception" arguments are relevant only if the make-whole is determined to be unmatured interest. If it is not unmatured interest, then the Debtors apparently concede that it is not impaired by the Code or by the Plan and is due to the Senior Noteholders.

The Court agrees with the Debtors that it is only if the redemption premium is determined to be the economic equivalent of unmatured interest that Wells Fargo's other arguments would be relevant. However, if it is unmatured interest, then the claim would be subject to the same analysis as the claims of all Noteholders' to post-petition interest. Therefore, the Court considers the parties' arguments on impairment and the solvent debtor exception together below.

C. Unmatured Interest

In Count 2 of the Complaint, Wells Fargo and US Bank (collectively, the "Indenture Trustees") seek a declaratory judgment that the Noteholders are entitled to post-petition interest on their claims, from the petition date to the date they were paid in full, at the contract rate. As noted ***793** above, Wells Fargo also asserts that to the extent the Court concludes that the make-whole claim is unmatured interest, the Senior Noteholders are nonetheless entitled to it under the express terms of the Indentures.

The Debtors seek to dismiss both the claim for post-petition interest and any claim for the redemption premium that is properly characterized as unmatured interest, contending that general unsecured claims for unmatured interest are disallowed under the Bankruptcy Code. 11 U.S.C. § 502(b). They contend that at most the Noteholders are entitled to interest from the petition date to the date the claims were paid in full only at the federal judgment rate as allowed in section 726(a)(5).

1. Unimpaired

The Indenture Trustees contend, however, that the Noteholders were treated as unimpaired under the Plan and, therefore, their claims for post-petition interest and/or the redemption premium must be paid in accordance with the terms of the Indentures. They rely on section 1124(1) which provides in relevant part that

> a class of claims or interests is impaired under a plan unless, with respect to each claim or interest of such class, the plan -
>
> (1) leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest ....

11 U.S.C. § 1124(1).

The Debtors disagree. Because any claim for unmatured interest is disallowed by operation of the Bankruptcy Code, rather than the Plan, the Debtors argue that the Noteholders' claims are not impaired. In re PPI Enters. (US), Inc., 324 F.3d 197, 204 (3d Cir. 2003) (holding that a creditor is unimpaired if it is the effect of the Bankruptcy Code that modifies its rights, not the debtor's plan).

The Indenture Trustees argue that PPI is distinguishable because it dealt with the effect of section 502(b)(6) rather than section 502(b)(2). They assert that section 502(b)(6) imposes an absolute cap on a landlord's claim, while section 502(b)(2) is not absolute and, in fact, is not effective where the debtor is solvent as it is here (pursuant to sections 726(a)(5) and 1129(a)(7)).

The Court finds the distinction illusory. Section 502(b) addresses the allowance of claims; sections 1129(a)(7) and 726(a)(5) address the treatment of claims where the debtor is solvent. The Indenture Trustees are conflating the allowance of claims with the treatment of claims. If one considers only the allowance issue, the Court concludes that section 502(b)(2) is as absolute as section 502(b)(6), because it disallows all unmatured interest on general unsecured claims.

It is true that in the rare solvent chapter 11 debtor case, some claims may be entitled to post-petition interest under sections 1129(a)(7) and 726(a)(5). [19] However, those sections do not reinstate the creditors' contract or state law rights to unmatured interest that has been disallowed by section 502(b)(2). Instead as discussed below, sections 1129(a)(7) and 726(a)(5) require the treatment of claims in accordance with the mandates of those sections which courts have concluded require the payment of post-petition interest only at the federal judgment rate. [20]

***794** In Ultra Petroleum, the creditors made the same argument as the Indenture Trustees do in this case. They contended that they were impaired because the debtor's plan did not pay their make-whole amount or post-petition interest at their contract rate. The Bankruptcy Court agreed. In re Ultra Petroleum Corp., 575 B.R. 361, 373 (Bank. S.D. Tex. 2017). On direct appeal, the Fifth Circuit reversed, concluding that "[w]e agree with PPI, every reported decision identified by either party, and Collier's treatise. Where a plan refuses to pay funds disallowed by the Code, the Code - not the plan - is doing the impairing." Ultra Petroleum, 943 F.3d at 762-64.

Following binding precedent in this Circuit (and the analysis of the Fifth Circuit with respect to claims similar to the Noteholders' claims), the Court concludes that any modification of the Noteholders' claim to unmatured interest or to the redemption premium (if it is the economic equivalent of unmatured interest) is an impairment of the Noteholders' contract claims by operation of section 502(b)(2) of the Bankruptcy Code, not the Debtors' Plan. Consequently, the Noteholders' claims are not impaired within the meaning of section 1124(1). E.g., PPI, 324 F.3d at 204; Ultra Petroleum, 943 F.3d at 765; PG&E, 610 B.R. at 315.

2. Solvent Debtor Exception

The Indenture Trustees argue, nonetheless, that they are entitled to their contract rate of interest under the equitable doctrine known as the "solvent debtor exception." They contend that the Bankruptcy Code incorporated that equitable concept which arose under the Bankruptcy Act and provided that creditors were entitled to their full contract rights, if a debtor was solvent. The Indenture Trustees assert that the equities of this case clearly support their claims: the Debtors are awash in cash, paid all creditors in full, and provided a substantial return on investment to equity (in cash and warrants).

a. Express Terms of the Code

The Debtors argue that equitable principles cannot override express provisions of the Code, such as section 502(b)(2) which disallows all unmatured interest on general unsecured claims, without regard to whether a debtor is solvent. They contend that, while sections 726(a)(5) and 1129(a)(7) [21] require the payment of post-petition interest on general unsecured claims where the debtor is solvent, courts have held that the interest is set at the federal judgment rate, not at the contract rate. [22]

The Indenture Trustees respond that section 1129(a)(7) only incorporates section 726(a)(5) in chapter 11 cases with respect to impaired claims. Because the Noteholders' claims are unimpaired under the Debtors' Plan, they assert that any limitation of post-petition interest to the federal judgment rate contained in those sections is not applicable to them.

The Court agrees with the Indenture Trustees, in part. By their express terms, sections 1129(a)(7) and 726(a)(5) provide ***795** what treatment impaired creditors are entitled to receive, not what treatment unimpaired claims are entitled to receive in a solvent chapter 11 debtor case. In essence, the Code is silent on what treatment unimpaired creditors must receive in a solvent chapter 11 debtor case.

b. Repeal of § 1124(3)

The Indenture Trustees argue, however, that Congress has made it clear that unimpaired creditors are entitled to receive post-petition interest at their contract rate by its repeal of section 1124(3). Before it was repealed, section 1124(3) had provided that a creditor is unimpaired if "the holder of such claim ... receive[s] ... cash equal to the allowed amount of such claim" on the effective date of the plan. 11 U.S.C. § 1124(3) (1988). Its repeal was prompted by the decision of a Bankruptcy Court that because sections 726(a)(5) and 1129(a)(7) were only applicable to impaired creditors and because section 1124(3) required only the payment of the allowed amount of their claims, unimpaired creditors were not entitled to post-petition interest. In re New Valley Corp., 168 B.R. 73, 79-81 (Bankr. N.J. 1994). The Indenture Trustees contend that the Legislative History makes it clear that denial of post-petition interest to unimpaired creditors in the New Valley case was "unfair." [23] Thus, the Indenture Trustees conclude that the repeal of section 1124(3) makes it clear that unimpaired creditors must receive interest at their contract rate.

The Debtors argue that the repeal of section 1124(3) is irrelevant to the issue at hand. They note that the repeal occurred before the Third Circuit's decision in PPI and did not affect its conclusion that creditors are unimpaired if their rights are altered by the Bankruptcy Code rather than the plan. PPI, 324 F.3d at 206-07. Thus, they contend that the repeal of section 1124(3) does not alter the fact that section 502(b)(2) does not permit the payment of post-petition interest on the Noteholders' claim.

The Court disagrees with the Debtors' analysis of PPI. The Third Circuit in PPI agreed with the bankruptcy court's conclusion in that case that the repeal of section 1124(3) meant that unimpaired creditors were entitled to the payment of postpetition interest if the debtor was solvent. Id. However, the Court does not read the repeal of section 1124(3) as expansively as the Indenture Trustees to mandate that unimpaired creditors must receive their contract rate of interest. Congress explained the repeal's effect, as follows:

> The principal change in this section is set forth in subsection (d) and relates to the award of postpetition interest. In a recent Bankruptcy Court decision in In re New Valley Corp., 168 B.R. 73 (Bankr. D.N.J. 1994), unsecured creditors were denied the right to receive postpetition interest on their allowed claims even though the debtor was liquidation and reorganization solvent.... In order to preclude this unfair result in the future, the Committee finds it appropriate to delete section 1124(3) from the Bankruptcy Code.
>
> As a result of this change, if a plan proposed to pay a class of claims in cash in the full allowed amount of the claims, the class would be impaired, entitling creditors to vote for or against the plan of reorganization. If creditors vote for the plan of reorganization, it can be confirmed over the vote of dissenting class of creditors only if it complies with the "fair and equitable" test under section 1129(b)(2) of the Bankruptcy Code ***796** and it can be confirmed over the vote of dissenting individual creditors only if it complies with the "best interests of creditors" test under section 1129(a)(7) of the Bankruptcy Code.
>
> The words "fair and equitable" are terms of art that have a well established meaning under the case law of the Bankruptcy Act as well as under the Bankruptcy Code. Specifically, courts have held that where an estate is solvent, in order for a plan to be fair and equitable, unsecured and undersecured creditors' claims must be paid in full, including postpetition interest, before equity holders may participate in any recovery.

H.R. Rep. No. 103-835, at 48 (1994) (emphasis added), reprinted in 1994 U.S.C.C.A.N. 3340, 3356-57.

Thus, in its repeal of section 1124(3), Congress did express its belief that the Bankruptcy Code contained an exception in cases where the debtor is solvent to the principle that creditors are not entitled to post-petition interest. The Legislative History, however, suggests that Congress believed that this solvent debtor exception is embodied in the "fair and equitable" and "best interests of creditors" tests contained in sections 1129(b) and 1129(a)(7).

While Congress stated that it would be unfair in a solvent chapter 11 debtor case for unimpaired creditors to receive no interest, it did not point to any provision of the Code that would allow interest to be paid to unimpaired creditors. Instead, it suggested that the failure to pay any interest to unsecured creditors in a solvent chapter 11 debtor would make them impaired and thus eligible to be paid interest by application of sections 1129(a)(7) and 1129(b)(2).

The Indenture Trustees argue, however, that Congress made it clear that unimpaired creditors under section 1124(1) would not be limited to the interest due under sections 1129(a)(7) and 726(a)(5).[24] While the Court agrees that Congress did state that the repeal of section 1124(3) was not meant to modify the 1984 amendment to section 1129(a)(7) which excluded unimpaired creditors, the Court does not conclude that it was intended to suggest that any interest due to unimpaired creditors cannot be capped at the federal judgment rate applicable under section 726(a)(5). Id. The 1984 amendment to section 1129(a)(7) was made in conjunction with an amendment of section 1129(a)(10) to require the vote of "impaired" claims, rather than all claims.[25] The Legislative History to those amendments reveals that they were meant to require that debtors only need obtain the requisite vote (or satisfaction of the best interest of creditors test) with respect to "real" creditors, i.e., those impaired by the plan, rather than intended to assure that unimpaired creditors get more than the federal judgment rate in the case of the debtor's solvency. See S. Rep. No. 98-65, at 80 (1983) ("Paragraph (10) makes clear the intent of section 1129(a)(10) that one "real" class of creditors must vote for the plan of reorganization.")

Nowhere in the repeal of section 1124(3) or its Legislative History did Congress state what the Indenture Trustees argue, namely that unimpaired creditors must be ***797** paid their contract rate of interest in a solvent chapter 11 debtor case. Congress could have so provided (1) by amending section 1124(3) to require that unimpaired creditors receive their contract rate of interest, in addition to payment in full of their allowed claim, or (2) by amending section 502(b)(2) to provide that unmatured interest is disallowed "except in the case of a solvent debtor." It did neither.

Thus, the repeal of section 1124(3) does not support the Indenture Trustees' argument that an unimpaired creditor must receive post-petition interest at its full contract rate.

c. Solvent Debtor Exception Cases

The Indenture Trustees argue that, because there is no express answer in the Bankruptcy Code or Legislative History, the answer lies in the solvent debtor exception articulated by the courts. While that concept arose under the Bankruptcy Act, they contend that it survives under the Bankruptcy Code because it has not been repudiated by any of the provisions of the Code. E.g., Cohen v. de la Cruz, 523 U.S. 213, 221, 118 S.Ct. 1212, 140 L.Ed.2d 341 (1998) (interpreting dischargeability provisions consistently with practice under the Bankruptcy Act because the Court "will not read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure"). The Indenture Trustees assert that the solvent debtor exception (as articulated by courts under the Act and the Code) mandates that, because the Debtors are solvent, all of the Noteholders' contract rights must be preserved, including the right to be paid post-petition interest at their contract rate. [26]

The Debtors contend that none of the Supreme Court cases cited by the Indenture Trustees support their contention, because they were all cases dealing with the entitlement of secured creditors to post-petition interest. [27] The Debtors further argue that the Bankruptcy Code expressly incorporated the rulings of those cases in sections 506(b) and 1129(b)(2)(A). They contend that cases granting secured creditors post-petition interest cannot be extended to unsecured creditors in the face of specific provisions of the Code, such as sections 502(b) and 506(b). Law v. Siegel, 571 U.S. 415, 421, 134 S.Ct. 1188, 188 L.Ed.2d 146 (2014) (holding that "equitable powers [that] remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code").

The Court agrees with the Debtors that cases cited by the Indenture Trustees which mandate the payment of interest to secured creditors at their contract rate when a debtor is solvent [28] are not applicable to the instant case which concerns ***798** unsecured creditors' rights. Timbers of Inwood, 484 U.S. at 379, 108 S.Ct. 626 (holding that the right to post-petition interest provided under section 506(b) is not applicable to undersecured creditors but that, instead, section 726(a)(5) provides the rule for treatment of unsecured creditors in the rare solvent debtor case).

The other Supreme Court case cited by the Indenture Trustees is Saper, which is also not supportive of their argument. City of New York v. Saper, 336 U.S. 328, 331, 69 S.Ct. 554, 93 L.Ed. 710 (1949) (holding that interest on tax claims, like other unsecured claims, stopped accruing on the bankruptcy filing date). The Court in Saper relied on English law from which the Bankruptcy Act was derived and did note, albeit in dicta, that English law had an exception to that rule, in the event that a debtor was solvent. Id. at 330 n.7, 69 S.Ct. 554 (1949). The Supreme Court made no comment, however, on what post-petition interest was required by that exception.

Although the Indenture Trustees cite Circuit Court cases which hold that unsecured creditors in solvent chapter 11 debtor cases are also entitled to post-petition interest at their contract rate, a closer reading of those cases show that many of them (1) relied on Supreme Court and other authority mandating such treatment for secured creditors, [29] without explaining why it applies to unsecured creditors, (2) relied on the fair and equitable test embodied in section 1129(b) which on its face is not applicable to unimpaired creditors, [30] and/or (3) expressly acknowledged that any right of an unsecured creditor to interest is subject to section 502(b). [31]

In a recent case, the Bankruptcy Court on remand in Ultra Petroleum also concluded that the passage of the Bankruptcy Code did not abolish the solvent debtor exception. 624 B.R. at 196-200. The Ultra Petroleum Court determined that under that exception, unimpaired creditors in a solvent chapter 11 debtor case were entitled to post-petition interest at the default rates provided in their contracts because they were entitled to have their equitable rights fully enforced under section 1124(1). Id. at 203-04.

The Ultra Petroleum Court's analysis is not persuasive. A bankruptcy court cannot use equitable principles to modify express language of the Code. ***799** United States v. Noland, 517 U.S. 535, 538, 116 S.Ct. 1524, 134 L.Ed.2d 748 (1996). Section 502(b)(2) expressly disallows claims of unsecured creditors for unmatured interest. When a debtor is solvent, the Bankruptcy Code does not waive the application of section 502(b)(2). The Third Circuit has held that section 1124(1) does not mandate that unimpaired creditors receive all of their contract rights where those rights are expressly disallowed by section 502(b) of the Code. PPI, 324 F.3d at 202-03. [32] Therefore, under Third Circuit precedent, this Court cannot agree with the Bankruptcy Court in Ultra Petroleum that being unimpaired mandates that the Noteholders receive their contract rate of interest in contravention of section 502(b)(2).

The Indenture Trustees also rely on the Bankruptcy Court's decision in Energy Future. In re Energy Future Holdings Corp., 540 B.R. 109 (Bankr. D. Del. 2015). In that case the Bankruptcy Court was considering an objection to the unsecured PIK noteholders' claims to post-petition interest and concluded that any claim for post-petition interest must be disallowed as a result of section 502(b). Id. at 111. The Court, however, then elaborated on what the debtors' plan would have to provide in order for those creditors to be unimpaired. It concluded that the "plan in this case need not provide for the payment in cash on the effective date of post-petition interest at the contract rate in order for the PIK Noteholders to be unimpaired." Id. (citing PPI, 324 F.3d at 205). Nonetheless, the Court concluded that under the equitable concepts embodied in the fair and equitable test under section 1129(b), "the Court has the discretion to exercise its equitable power to require, among other things, the payment of post-petition interest, which may be at the contract rate or such other rate as the Court deems appropriate." Id. at 124.

The Court finds the test articulated by the Bankruptcy Court in Energy Future, however, to be problematic. First, the Court relied on the fair and equitable test of section 1129(b), which by its express terms does not apply to unimpaired creditors. [33] Further, it provides no guidance to debtors or creditors as to precisely how unimpaired creditors must be treated and thus will result in endless litigation. Finally, leaving the determination of what interest, if any, an unimpaired creditor is entitled to receive in a solvent chapter 11 debtor case completely within the discretion of the bankruptcy court also runs counter to recent Supreme Court jurisprudence (and Congressional amendments) that have sought to curb the bankruptcy court's exercise of equitable discretion. [34]

***800** d. Proper Treatment of Unimpaired Creditors in Solvent Chapter 11 Debtor Cases

The Court is not persuaded that the Bankruptcy Code incorporated the solvent debtor exception to the extent suggested by the Bankruptcy Courts in Ultra Petroleum (to mandate the reinstatement of all contract rights to interest notwithstanding their disallowance by section 502(b)) and in Energy Future (to permit the exercise of broad equitable discretion by the bankruptcy court to determine what interest, if any, unimpaired creditors are entitled to receive). Rather, after consideration of the cases cited by the parties, the express language of the Bankruptcy Code, and its Legislative History, the Court is convinced that the solvent debtor exception survived passage of the Bankruptcy Code only to a limited extent. The Bankruptcy Code expressly codified the solvent debtor exception in section 506(b) as to oversecured creditors and in section 1129(a)(7) and 726(a)(5) as to unsecured creditors. While the latter sections currently only apply to impaired creditors, when the Bankruptcy Code was originally enacted they applied to all unsecured creditors, impaired and unimpaired. [35] As the Court concluded above, when the 1984 amendment made section 1129(a)(7) applicable to impaired creditors only, Congress was motivated by the desire to require voting only by impaired creditors, rather than by a desire to assure that unimpaired creditors get their contract rate of interest. [36]

Significantly, neither the Bankruptcy Code nor the Legislative History expressly state that unimpaired creditors are entitled to their contract rate of interest or even to more than impaired creditors in the case of a solvent debtor. Instead the Legislative History provides strong evidence Congress intended that unimpaired creditors in a solvent chapter 11 debtor case should receive post-petition interest only in accordance with sections 1129(a)(7) and 726(a)(5).[37] That is what the Debtors contend the Noteholders are entitled to receive in this case.

The Indenture Trustees complain, however, that the Debtors treated the Noteholders not as impaired, but as unimpaired, thereby depriving them of the right to vote. The Court finds that the result would have been no different. If the Noteholders had been treated as impaired and if they had voted against the Plan, they would have received the same treatment: payment in full in cash of their allowed claim plus post-petition interest in accordance with sections 1129(a)(7) and 726(a)(5).[38]

It is important to emphasize that the Court's ruling in this case is limited to the issue of what post-petition interest unimpaired creditors must receive in the rare case when a chapter 11 debtor proves to be solvent and their claims are being paid in full in cash on the effective date of the plan. Concluding that sections 1129(a)(7) and 726(a)(5) apply to both impaired and unimpaired unsecured creditors where the debtor is solvent does not offend the basic policy of the Bankruptcy Code to assure that creditors of the same priority generally receive like treatment. While section 726(a)(5) is made applicable in chapter 11 cases only to impaired creditors, when a ***801** debtor is solvent, impaired creditors essentially are unimpaired, in the sense that they are entitled to payment in full of their allowed claims and postpetition interest, albeit at the federal judgment rate, before any distribution can be made to equity. 11 U.S.C. §§ 726(a)(5) & 1129(a)(7). The Legislative History to section 1124(3)'s repeal suggests that Congress believed that there is no legitimate reason when a debtor is solvent to distinguish between impaired and unimpaired unsecured creditors who are receiving payment of their claims in cash in full. Consequently, the Court concludes that both should receive the same treatment: payment of their allowed claim plus post-petition interest at the federal judgment rate in accordance with section 726(a)(5).

Such a rule promotes several important policies of the Bankruptcy Code. First, as noted, it is consistent with the underlying principle of the Bankruptcy Code that creditors with the same priority (such as unsecured creditors) should be similarly treated. Providing that all general unsecured creditors are entitled to the same post-petition interest in a solvent chapter 11 debtor case prevents a debtor from paying preferred creditors more than others simply by classifying them as unimpaired.

Second, it is an easy and predictable rule to apply (as opposed to determining interest based on each creditor's contract rights or relying on discretion exercised by the court on a case by case basis). This promotes predictability and the efficient administration of the bankruptcy estate.[39]

The Court in PG&E reached a similar conclusion. 610 B.R. at 315. That Court addressed the arguments of numerous unimpaired creditors that they were entitled to post-petition interest at various rates, determined by contracts between the debtors and the respective claimants, different state's judgment rates, or some other rate. Id. at 310. It rejected those arguments noting that

> Cardelucci, in answering the narrow question [of what the proper rate of post-petition interest is in a solvent chapter 11 debtor case], drew no distinction as to whether the rule it announced was confined only to impaired claims. The clear and unequivocal analysis based on section 726(a)(5) is obvious: it applies to all unsecured and undersecured claims in a surplus estate.

Id. at 315.

Consequently, the Court concludes that the Indenture Trustees have not stated a plausible claim that the Debtors must pay post-petition interest on the Notes at the rates specified in the Indentures rather than at the federal judgment rate. As a result, the Court will grant the Debtors' Motion to Dismiss Count 2 of the Complaint. [40]

IV. CONCLUSION

For the reasons set forth above, the Court will grant the Debtors' Motion to Dismiss Count 1 as to the 2022/2024 Senior Notes, but deny it as to the 2026/2028 Senior Notes, and grant the Debtors' Motion to Dismiss Count 2.

All Citations

637 B.R. 781

Footnotes

1 The Court is not required to state findings of fact or conclusions of law pursuant to Rule 7052 of the Federal Rules of Bankruptcy Procedure. Instead, the facts recited are those averred in the Complaint, which must be accepted as true for the purposes of the Motion to Dismiss. Ashcroft v. Iqbal, 556 U.S. 662, 678, 129 S.Ct. 1937, 173 L.Ed.2d 868 (2009).

2 References to the docket in this adversary proceeding are to "Adv. D.I. #" while references to the docket in the main case are to "D.I. #."

3 The Indentures and Supplemental Indentures for the Senior Notes contain substantially identical terms for purposes of the issues at bar. (Adv. D.I. 5 at Exs. A-H.)

4 The Indentures in this case are also governed by New York law. (Adv. D.I. 5, Exs. A & C, § 115, Exs. E & G, § 113.)

5 Adv. D.I. 5, Exs. B, D, F, H at § 6.

6 See also Sharon Steel Corp. v. Chase Manhattan Bank, N.A., 691 F.2d 1039, 1053 (2d Cir. 1982) (enforcing make-whole where debtor filed a voluntary plan of liquidation in an attempt to substitute the buyer for the debtor as obligor under low interest debentures); Wilmington Sav. Fund Soc'y v. Cash Am. Int'l, Inc., No. 15-CV-5027 (JMF), 2016 WL 5092594, at *7 (S.D.N.Y. Sept. 19, 2016) (enforcing make-whole where issuer breached indenture in connection with a spin-off).

7 E.g., In re Granite Broad. Corp., 369 B.R. 120, 144 (Bankr. S.D.N.Y. 2007) (citing In re LHD Realty Corp., 726 F.2d 327, 330 (7th Cir. 1984)). See also EFH, 842 F.3d at 260 (noting that "by electing to accelerate the debt, a lender forgoes its right to a stream of payments in favor of immediate repayment" and cannot claim a redemption premium).

8 E.g., Sharon Steel, 691 F.2d at 1053 (simply holding that where issuer breached the indenture, the trustee had the option to enforce the redemption provision rather than accelerate the notes); WSFS, 2016 WL 5092594, at *7 (concluding that cases interpreting Sharon Steel as requiring bad faith intent to avoid redemption premium were incorrect and no such intent was necessary to allow enforcement of redemption clause).

9 E.g., Chesapeake Energy Corp. v. Bank of N.Y. Mellon Tr. Co. N.A., 837 F.3d 146 (2d Cir. 2016) (enforcing redemption provision even though company acted in good faith, in reliance on a declaratory judgment, later

reversed on appeal, that its actions would not trigger the provision); In re Imperial Coronado Partners, Ltd., 96 B.R. 997, 1000 (9th Cir. BAP 1989) (concluding that decision to sell property was voluntary even though debtor did not have the financial means to reinstate the note and the sale made good business sense).

10 E.g., Burlington Ins. Co. v. NYC Transit Auth., 29 N.Y.3d 313, 57 N.Y.S.3d 85, 79 N.E.3d 477, 482 (2017) (holding that courts should interpret contracts in a manner that does not render a portion of a provision superfluous or meaningless).

11 E.g., In re Chateaugay Corp., 961 F.2d 378, 380 (2d Cir. 1992) (concluding that unamortized portion of original issue discount was unmatured interest disallowed by § 502(b)(2)); In re Doctors Hosp. of Hyde Park, Inc., 508 B.R. 697, 705-06 (Bank. N.D. Ill. 2014) (holding that yield maintenance premium was a liquidated damages provision in the nature of disallowable unmatured interest); In re Ridgewood Apts., 174 B.R. 712, 721 (Bank. S.D. Ohio 1994) (prepayment penalty could be disallowed as unmatured interest because it was meant to compensate lender for loss of interest income). See also In re Ultra Petroleum Corp., 943 F.3d 758, 765 (5th Cir. 2019) (noting that make-whole premium could be unmatured interest and remanding to bankruptcy court for determination based on the unique dynamics of the case).

12 See also MPM, 874 F.3d at 802 (noting that a make-whole premium "was intended to ensure that the Senior-Lien Note holders received additional compensation to make up for the interest they would not receive if the Notes were redeemed prior to the maturity date.")

13 E.g., In re Ultra Petroleum Corp., 624 B.R. 178, 188-95 (Bankr. S.D. Tex. 2020) (on remand, concluding that make–whole premium was not the economic equivalent of unmatured interest and not disallowed under § 502(b)(2)); In re School Specialty, Inc., Bank. No. 13-10125 (KJC), 2013 WL 1838513, at *5 (Bank. D. Del. 2013) (agreeing with Trico and holding that make-whole premium should not be disallowed as unmatured interest); In re Trico Marine Servs. Inc., 450 B.R. 474, 481 (Bank. D. Del. 2011) (reviewing cases and concluding that "Th[e] Court is persuaded by the soundness of the majority's interpretation of make-whole obligations, and therefore finds that the Indenture Trustee's claim on account of the Make-Whole Premium is akin to a claim for liquidated damages, not for unmatured interest."). See also 4 Collier on Bankruptcy ¶ 502.03 (16th ed 2021) (collecting cases).

14 E.g., Doctors Hosp., 508 B.R. at 706 (disagreeing with the Trico analysis because liquidated damages may well include unmatured interest); In re MPM Silicones LLC, Bankr. No. 14-22503 (RDD), 2014 WL 4436335, at *17-18 (Bankr. S.D.N.Y. Sept. 9, 2014) (concluding that noteholders claim to a make-whole based on debtor's breach of no call provision was unmatured interest disallowed under § 502(b)(2)), aff'd in part and rev'd in part on other grounds, 874 F.3d 787 (2d Cir. 2017).

15 Although the Bankruptcy Court held on remand that make-whole premium was not unmatured interest, that decision is currently on appeal. Ultra Petroleum Corp. v. Ad Hoc Comm. of OpCo Unsecured Creditors, Case No. 21-20008 (oral argument was held before the Fifth Circuit on 10/04/2021).

16 See Douglas Baird, Making Sense of Make-Wholes, 94 Am. Bankr. L.J. 567 (2020).

17 In re Long John Silver's Rests., Inc., 230 B.R. 29, 33 n.4 (Bankr. D. Del. 1999) (quoting William Shakespeare, Romeo & Juliet, Act II, scene ii).

18 The Supplemental Indenture provides in relevant part that prior to the stated date, the Debtors may redeem the 2028 Senior Notes for a price "equal to 100.0% of the principal amount thereof plus the Applicable Premium (as defined below) as of, and accrued but unpaid interest, if any, to, but not including, the Redemption Date." (Adv. D.I. 5, Ex. H, § 6(c)). That section further defines the Applicable Premium to mean

> with respect to a 2028 Note at any Redemption Date, the greater of (i) 1.00% of the principal amount of such 2028 Note and (ii) the excess of (A) the present value at such Redemption Date, calculated as of the date of the applicable redemption notice, of (1) the redemption price of such 2028 Note on January 15, 2023 (such redemption price being that described in Section 6(a)), plus (2) all required remaining scheduled interest payments due on such 2028 Note through such date (excluding accrued and unpaid interest to the Redemption Date), computed using a discount rate equal to the Treasury Rate plus 50 basis points, over (B) the principal amount of such 2028 Note on such Redemption Date, as calculated by the Company in good faith (which calculation shall be conclusive) or on behalf of the Company by such Person as the Company shall designate; provided that such calculation shall not be a duty or obligation of the Trustee.

(Id. (emphasis added)).

19 United Sav. Ass'n of Texas v. Timbers of Inwood Forest Assocs., 484 U.S. 365, 379, 108 S.Ct. 626, 98 L.Ed.2d 740 (1988).

20 E.g., In re Cardelucci, 285 F.3d 1231, 1234 (9th Cir. 2002) (concluding that post-petition interest on general unsecured claims is payable under sections 726(a)(5) and 1129(a)(7) only at the federal judgment rate, not at the contract rate); In re PG&E Corp., 610 B.R. 308, 315 (Bank. N.D. Cal. 2019) (same); In re Washington Mutual, Inc., 461 B.R. 200, 242 (Bank. D. Del. 2011) (same), vacated on other grounds, 2012 WL 1563880 (Bank. D. Del. Feb. 24, 2012).

21 11 U.S.C. §§ 726(a)(5) (providing payment of postpetition interest at "the legal rate" to creditors, before any distribution to the debtor (or equity), in the event there are funds left after paying all other claims in a chapter 7 liquidation case), & 1129(a)(7) (providing that with respect to each impaired class of claims or interests, each holder of such claim has either accepted the plan or will receive at least what it would have received in a liquidating chapter 7 case).

22 E.g., Cardelucci, 285 F.3d at 1234; PG&E, 610 B.R. at 315; Washington Mutual, 461 B.R. at 242.

23 H.R. Rep. No. 103-835, at 48 (1994) (emphasis added), reprinted in 1994 U.S.C.C.A.N. 3340, 3356-57.

24 H.R. Rep. 103-835, 48 (1994), reprinted in 1994 U.S.C.C.A.N. 3340, 3357 ("With respect to section 1124(1) and (2), subsection (d) would not change the beneficial 1984 amendment to section 1129(a)(7) of the Bankruptcy Code, which excluded from application of the best interests of creditors test classes that are unimpaired under section 1124.").

25 See An Act to amend title 28 of the United States Code regarding jurisdiction of bankruptcy proceedings, to establish new Federal judicial positions, to amend title 11 of the United States Code, and for other purposes, Pub. L. 98-353, § 512(a)(7) & (10), 98 Stat. 333 (1984) (amending 11 U.S.C. § 1129(a)(7) & (10)).

26 E.g., City of New York v. Saper, 336 U.S. 328, 330 n.7, 69 S.Ct. 554, 93 L.Ed. 710 (1949); Vanston Bondholders Protective Comm. v. Green, 329 U.S. 156, 67 S.Ct. 237, 91 L.Ed. 162 (1946); Consolidated Rock Prods. Co. v. Du Bois, 312 U.S. 510, 61 S.Ct. 675, 85 L.Ed. 982 (1941); Am. Iron & Steel Mfg. Co. v.

Seaboard Air Line Ry., 233 U.S. 261, 264, 34 S.Ct. 502, 58 L.Ed. 949 (1914); In re Ultra Petroleum, 943 F.3d at 765; Gen. Elec. Capital Corp. v. Future Media Prods., Inc., 547 F.3d 956, 961 (9th Cir. 2008); In re Gencarelli, 501 F.3d 1, 7 (1st Cir. 2007); In re Dow Corning Corp., 456 F.3d 668, 679-80 (6th Cir. 2006); In re Terry Ltd. P'ship, 27 F.3d 241, 243 (7th Cir. 1994); In re Laymon, 958 F.2d 72, 75 (5th Cir. 1992).

27 Vanston Bondholders, 329 U.S. 156, 67 S.Ct. 237; Consolidated Rock, 312 U.S. 510, 61 S.Ct. 675, 85 L.Ed. 982; Am. Iron, 233 U.S. 261, 34 S.Ct. 502.

28 Vanston Bondholders, 329 U.S. 156, 67 S.Ct. 237; Consolidated Rock, 312 U.S. 510, 61 S.Ct. 675; Am. Iron, 233 U.S. 261, 34 S.Ct. 502; GECC, 547 F.3d at 961; Gencarelli, 501 F.3d at 5, 8; Terry Ltd., 27 F.3d at 242-43; Laymon, 958 F.2d at 75; Ruskin v. Griffiths, 269 F.2d 827, 830-832 (2d Cir. 1959).

29 Dow Corning, 456 F.3d at 679 (relying on In re Chicago, Milwaukee, St. Paul & Pac. R.R. Co., 791 F.2d 524, 528 (7th Cir. 1986), Ruskin, 269 F.2d at 831, and Debentureholders Protective Comm. of Cont'l Inv. Corp. v. Cont'l Inv. Corp., 679 F.2d 264, 269 (1st Cir. 1982)); Chicago, 791 F.2d at 528 (simply stating the solvent debtor exception applied to unsecured creditors without citation to any caselaw in support, while also acknowledging that "[t]he fact that a proceeding is equitable does not give the judge a free-floating discretion to redistribute rights in accordance with his personal views of justice and fairness, however enlightened those views may be."); Debentureholders, 679 F.2d at 269 (relying on Vanston, 329 U.S. 156, 67 S.Ct. 237 and Ruskin, 269 F.2d 827).

30 Dow Corning, 456 F.3d at 678-80 (ruling was premised on section 1129(b), because the court was considering the rights of impaired creditors, not unimpaired creditors, in a solvent chapter 11 debtor case). Further, Dow Corning is contrary to the many cases that conclude that impaired creditors are only entitled to post-petition interest at the federal judgment rate under sections 1129(a)(7) and 726(a)(5). E.g., Cardelucci, 285 F.3d at 1234; PG&E, 610 B.R. at 315; Washington Mutual, 461 B.R. at 242.

31 In Gencarelli, the First Circuit held that the contractual claims of unsecured creditors should be enforced in solvent chapter 11 debtor cases "unless one of the section 502 exceptions applies" and remanded the case to determine if any provision of that section did apply. 501 F.3d at 5, 8.

32 Significantly, in PPI, the Third Circuit held that a landlord's claim was capped by section 502(b)(6) even though that conclusion meant that the debtor's equity would be getting a distribution (i.e., it was a solvent chapter 11 debtor case). 324 F.3d at 200-04.

33 11 U.S.C. § 1129(b) (mandating that the court "shall confirm the plan ... if the plan does not discriminate unfairly, and is fair and equitable, with respect to each class of claims or interests that is impaired under, and has not accepted, the plan.") (emphasis added). See also PPI, 324 F.3d at 205 n.14.

34 E.g., Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 206, 108 S.Ct. 963, 99 L.Ed.2d 169 (1988) (rejecting equitable arguments that absolute priority rule did not apply to the case at bar, the Court concluded that "whatever equitable powers remain in the bankruptcy courts must and can only be exercised within the confines of the Bankruptcy Code."); In re Frederickson, 545 F.3d 652, 658 (8th Cir. 2008) ("In enacting BAPCPA, Congress reduced the amount of discretion that bankruptcy courts previously had over the calculation of an above-median debtor's income and expenses .... to eliminate what it perceived as widespread abuse of the system. ...").

35 An Act to Establish a uniform Law on the Subject of Bankruptcies, Pub. L. No. 95-598, § 1129(a)(7), 92 Stat. 2549 (1978).

36 See discussion in Part C.2.b, supra.

37 Id.

38 Of course, even unimpaired creditors have the right to object to confirmation of the plan. It appears that the Indenture Trustees agreed that, rather than object to confirmation of the Debtors' Plan in this case, their objection to treatment of the Noteholders' claims would be decided in this adversary (or the claims resolution process). (D.I. 5261 at ¶¶ 26 & 27.)

39 While the Indenture Trustees assert that the calculation of their contract interest claim is a relatively simple math exercise, in large cases with multiple unimpaired creditors that would not be true. E.g., PG&E, 610 B.R. at 310.

40 As a result of this conclusion, to the extent that the Court determines that the redemption premium is the economic equivalent of interest, that claim too would be limited by the application of the federal judgment rate.

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51 F.4th 138
United States Court of Appeals, Fifth Circuit.

IN RE: ULTRA PETROLEUM CORPORATION; Keystone Gas Gathering, L.L.C.; Ultra Resources, Incorporated; Ultra Wyoming, Incorporated; Ultra Wyoming LGS, L.L.C.; UP Energy Corporation; UPL Pinedale, L.L.C.; UPL Three Rivers Holdings, L.L.C., Debtors,
Ultra Petroleum Corporation; Keystone Gas Gathering, L.L.C.; Ultra Resources, Incorporated; Ultra Wyoming, Incorporated; Ultra Wyoming LGS, L.L.C.; UP Energy Corporation; UPL Pinedale, L.L.C.; UPL Three Rivers Holdings, L.L.C., Appellants,
v.
Ad Hoc Committee of Opco Unsecured Creditors; Opco Noteholders; Allstate Life Insurance Company; Allstate Life Insurance Company of New York, Appellees.

No. 21-20008
|
FILED October 14, 2022

Synopsis
Background: In surplus case, Chapter 11 debtors objected to creditors' claim for make-whole premium and postpetition interest at contractual default rate. The United States Bankruptcy Court for the Southern District of Texas, Marvin P. Isgur, J., 575 B.R. 361, denied objection, and subsequently certified a direct appeal to the Court of Appeals, 2017 WL 4863015. The Court of Appeals, Oldham, Circuit Judge, 943 F.3d 758, reversed in part, vacated in part, and remanded. On remand, the Bankruptcy Court, Isgur, Chief Judge, 624 B.R. 178, determined that disputed "make-whole amount" was enforceable under New York law and allowable under the Bankruptcy Code, awarded postpetition interest at contractual default rate rather than federal judgment rate, and subsequently granted debtors' motion for certification of direct appeal.

Holdings: The Court of Appeals, Elrod, Circuit Judge, held that:

creditors' claim for the contractual "make-whole amount" was a claim for the economic equivalent of unmatured interest and, as such, was subject to disallowance by the Bankruptcy Code;

the judicially-created solvent-debtor exception survived enactment of the Code;

in the case at bar, the solvent-debtor exception operated to suspend disallowance of the make-whole amount, and so debtors had to pay what they promised now that they were financially capable of doing so;

the make-whole amount was not an unenforceable penalty under New York law but, rather, constituted enforceable liquidated damages; and

given debtor's solvency, postpetition interest was to be calculated according to the agreed-upon contractual default rate, not at the much lower federal judgment rate.

Affirmed.

Oldham, Circuit Judge, filed dissenting opinion.

Procedural Posture(s): On Appeal; Objection to Proof of Claim.

***142** Appeal from the United States Bankruptcy Court for the Southern District of Texas, Houston Division, USBC No. 4:16-MC-3064, Marvin P. Isgur, U.S. Bankruptcy Judge

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Before Jolly, Elrod, and Oldham, Circuit Judges.

Opinion

Jennifer Walker Elrod, Circuit Judge:

Bankruptcy is ordinarily for the insolvent. The Bankruptcy Code enables economically viable businesses in financial distress to restructure and shed some of the debt burden that crippled them. Sometimes, however, initially insolvent debtors regain solvency during extended bankruptcy proceedings. This is one such case. Ultra Petroleum Corp. (HoldCo) and its affiliates, including its subsidiary Ultra Resources, Inc. (OpCo), entered Chapter 11 bankruptcy deep in the hole. But during the bankruptcy process, these debtors (collectively, Ultra) hit it big—as natural gas prices soared, they became supremely solvent. What, then, of their debt and interest must they (re)pay their creditors now that they can?

Ultra proposed a $2.5 billion bankruptcy plan. It provided that OpCo's creditors would be paid—in full and in cash—their outstanding principal and all interest that had accrued *before* bankruptcy, plus interest on both at the Federal Judgment Rate for the duration of the bankruptcy proceeding. Two groups of creditors complain that the plan falls some $387 million short: They contend that they are entitled to a "Make-Whole Amount," a lump sum calculated to give them the present value of the interest payments they would have received but for Ultra's bankruptcy. These creditors further claim that they are owed post-petition interest at a contractually specified rate that is materially higher than the Federal Judgment Rate.

This case asks us to decide: first, whether the Bankruptcy Code precludes the creditors' claims for the Make-Whole Amount; second, even if it does, whether the traditional solvent-debtor exception applies; and third, whether post-judgment interest is to be calculated at the contractual or Federal Judgment rate. We hold that the Bankruptcy Code disallows the Make-Whole Amount as the economic equivalent of unmatured interest. But because Congress has not clearly abrogated the solvent-debtor exception, we hold that it applies to this case. And the solvent-debtor exception demands that Ultra pay what it promised now that it is financially capable. We likewise hold that, given Ultra's solvency, post-petition interest is to be calculated according to the agreed-upon contractual rate. Thus, we AFFIRM.

***143** I.

Ultra is a family of natural gas exploration and production companies. In 2014 and 2015, a sharp decline in natural gas prices drove Ultra to insolvency and thence to the protection of Chapter 11 bankruptcy in early 2016. During the bankruptcy proceedings, the same volatile commodity prices that hurled Ultra into insolvency propelled the debtors back into solvency. Indeed, Ultra became "massively solvent."

Ultra proposed a plan that would pay—in full and in cash—all unsecured claims, including those of its noteholders and revolving credit facility creditors (collectively, Creditors). [1] Ultra would thus pay Creditors' entire outstanding principal along with all accrued *pre*-petition interest at the contractual rate, plus *post*-petition interest at the Federal Judgment Rate, as specified at 28 U.S.C. § 1961(a). [2] In Ultra's view, the plan paid Creditors fully for every claim that the Bankruptcy Code allowed. For this reason, Ultra classified these Creditors as "unimpaired" under 11 U.S.C. §§ 1123(a)(2), 1124. And given their status as "unimpaired," Creditors were thus "conclusively presumed to have accepted the plan" per § 1126(f). In other words, they had no right to vote on it.

Creditors objected. They contended that the plan *did* impair them because it did not allow for claims stemming from two contractual provisions in their debt instruments—a shortfall of some $387 million. Not so, countered Ultra—those two provisions simply did not give rise to allowable claims under the Bankruptcy Code.

The parties stipulated that this dispute could be resolved after plan confirmation. Ultra created a $400 million reserve to cover the alleged shortfall, and the bankruptcy court confirmed the plan. The bankruptcy court then addressed Creditors' "impaired" status vis-à-vis the disputed amounts, concluding that Creditors remained impaired unless they were paid the full amount permitted under applicable non-bankruptcy law. *In re Ultra Petroleum Corp.*, 575 B.R. 361, 366–75 (Bankr. S.D. Tex. 2017). Ultra appealed directly to this court.

We reversed. *In re Ultra Petroleum Corp.*, 943 F.3d 758 (5th Cir. 2019). We held that "[w]here a plan refuses to pay funds disallowed by the Code, the Code—not the plan—is doing the impairing." *Id.* at 765. The issue of impairment thus set aside, the only question remaining was whether Creditors were, in fact, entitled to the disputed claims under the Bankruptcy Code's disallowance provisions. On this score, we remanded to the bankruptcy court to render a decision in the first instance. *Id.* at 765–66.

On remand, the bankruptcy court faced the dispositive question of whether Creditors' disputed claims were indeed disallowed under the Bankruptcy Code. Creditors' ***144** disputed claims stemmed from two OpCo debt instruments:

1. OpCo Notes issued under a Master Note Purchase Agreement (MNPA) (totaling $1.46 billion in principal); and

2. a Revolving Credit Facility (RCF) ($999 million in principal).

Creditors claimed a "Make-Whole Amount" under the MNPA, and under both the MNPA and the RCF, they claimed interest calculated according to a contractually specified "default rate" on all amounts due and payable at the time that Ultra filed for bankruptcy.

Under both the MNPA and the RCF, the occurrence of any contractually enumerated "Event of Default" renders any outstanding principal immediately due and payable. Under the MNPA, such an Event also triggers the requirement that OpCo pay Creditors an additional Make-Whole Amount. The Make-Whole Amount, stripped of the contract's financial jargon, is simply the value of all future unmatured interest payments on the Notes, expressed in today's dollars. [3]

Among the Events of Default that trigger principal acceleration and the Make-Whole provision is the filing of a petition for bankruptcy. Thus, the moment that Ultra filed, the remaining principal on both debt instruments became due, and Ultra contractually owed the Noteholders the Make-Whole Amount—a sum clocking in around $201 million.

On top of this, both the MNPA and the RCF specified a hefty contractual "default rate" of interest to accrue on the accelerated principal and the Make-Whole Amount for so long as these amounts remained unpaid. [4] Since bankruptcy's automatic stay prevents payment, this default-rate interest effectively accrued until plan confirmation. Creditors accordingly sought to recover $106 million in interest on the accelerated principal and $14 million in interest on the Make-Whole Amount.

Ultra objected to both the Make-Whole Amount and the default-rate interest, which together totaled some $387 million. In its view, the Make-Whole Amount was either an unenforceable penalty under governing New York law or else impermissible "unmatured interest," both of which are disallowed by the Bankruptcy Code. Ultra further urged that the interest accrued at the contractual default rate far exceeded the appropriate amount of interest, which, it contended, should be calculated at the Code's "legal rate" of post-petition interest: namely, the Federal Judgment Rate. [5]

On remand from this court to decide in the first instance whether these disputed amounts were allowable under the Bankruptcy Code (and, therefore, necessary for ***145** Creditors to be deemed unimpaired), the bankruptcy court ruled in Creditors' favor. *In re Ultra Petroleum Corp.*, 624 B.R. 178, 191–95, 202–04 (Bankr. S.D. Tex. 2020). The Make-Whole Amount, it held, was enforceable under New York law, and it constituted neither "unmatured interest" nor its "economic equivalent" for the purpose of § 502(b)(2). *Id.* at 191–95. As to post-petition interest, the bankruptcy court held that the historically rooted "solvent-debtor exception" to the Bankruptcy Code's prohibition of unmatured interest entitled Creditors to such interest at the contractual default rate rather than the lower Federal Judgment Rate. *Id.* at 195–204. All told, the bankruptcy court's ruling would require Ultra to pay Creditors the entire $387 million that they sought. Ultra again appealed timely and directly to this court. [6]

II.

This appeal presents pure questions of bankruptcy law, which we review *de novo*. *Ultra*, 943 F.3d at 762.

We begin with the Make-Whole Amount. Because we need only address the solvent-debtor exception to the extent that the Bankruptcy Code would disallow the Make-Whole Amount, we first consider whether the Make-Whole Amount constitutes disallowed unmatured interest under 11 U.S.C. § 502(b)(2). Concluding that it does, we then consider whether the solvent-debtor exception survived the enactment of the Bankruptcy Code in 1978 and thus whether it still applies to suspend the Code's disallowance of the Make-Whole Amount as unmatured interest. Because the exception does indeed survive intact, we then consider whether the Make-Whole Amount is an unenforceable penalty under New York law, in which case the exception could not save it. But because it is enforceable under state law, we conclude that Ultra must pay the Make-Whole Amount as a solvent debtor.

Finally, we turn to the rate of post-petition interest. Because, as the parties agree, Ultra must receive *some* post-petition interest to remain unimpaired, we must decide only which rate to apply: the contractual default rate or the Federal Judgment Rate. We conclude that in this solvent-debtor case, the contractual default rate is appropriate. We therefore affirm.

A.

Section 502(b)(2) of the Bankruptcy Code disallows "claim[s] ... for unmatured interest." We have interpreted that provision to disallow the "economic equivalent of 'unmatured interest' " as well. *In re Pengo Indus., Inc.*, 962 F.2d 543, 546 (5th Cir. 1992) (citation omitted); *accord* *In re Chateaugay Corp.*, 961 F.2d 378, 380–81 (2d Cir. 1992). [7] Otherwise, the Code's disallowance ***146** of unmatured interest would be susceptible to easy end-runs by canny creditors. *See* *Pengo*, 962 F.2d at 543 (refusing to allow an end-run around the Code's disallowance of unmatured interest by recharacterizing as "principal" what is essentially interest).

Contractual make-whole amounts, like the one at issue here, are expressly designed to liquidate fixed-rate lenders' damages flowing from debtor default while market interest rates are lower than their contractual rates. Lenders' damages equal the present value of all their future interest payments. In other words, a make-whole amount is nothing more than a lender's unmatured interest, rendered in today's dollars. *See* *In re Energy Future Holdings Corp.*, 842 F.3d 247, 251 (3d Cir. 2016) (referring to a make-whole as a "contractual substitute for interest lost on [n]otes redeemed before their expected due date"); *In re MPM Silicones, L.L.C.*, 874 F.3d 787, 801 n.13 (2d Cir. 2017) (same). It is—rather precisely—the "economic equivalent of 'unmatured interest.' " *Pengo*, 962 F.2d at 546 (citation omitted).

Because the Make-Whole Amount here is the "economic equivalent" of a lender's "unmatured interest," the Code—per our circuit's precedent—disallows it. *See* 11 U.S.C. § 501(b)(2); *Pengo*, 962 F.2d at 546. Against this straightforward syllogism, Creditors lodge an array of objections. None succeeds.

1.

Creditors first contend that the Make-Whole Amount is simply not unmatured interest: it is neither "interest" nor "unmatured" (if it were interest), they argue. Neither of these arguments has merit.

Creditors rely heavily on dictionary and case law definitions of the term "interest." Interest, they say, is "consideration for the *use or forbearance* of another's money accruing over time." Brief for Appellee Ad Hoc Committee of OpCo Unsecured Creditors at 37 (quoting *Ultra*, 624 B.R. at 184). And because the Make-Whole Amount does not compensate Creditors for any actual "use or forbearance," it therefore cannot be "interest."

This argument fails. Even on the terms of Creditors' own argument, the Make-Whole Amount *does* constitute compensation for "use or forbearance" of Creditors' principal —it compensates Creditors for the *future* use of their money, albeit use that will never actually occur because of Ultra's default. This is simply another way of saying that the interest is *unmatured.* And unmatured interest is still interest. [8]

***147** Assuming *arguendo* that the Make-Whole Amount is interest, Creditors next argue that it had matured—albeit at the very moment of Ultra's filing for bankruptcy. If that were so, the Make-Whole Amount would narrowly escape § 502(b)(2)'s gaping maw: it would be an allowable claim for (barely) matured interest. This argument also fails.

The bankruptcy court correctly rejected the argument, reasoning that the MNPA's acceleration provision was an *ipso facto* clause that is not to be considered in assessing whether the payment it triggered had matured. *Ultra*, 624 B.R. at 188 (citing *In re ICH Corp.*, 230 B.R. 88, 94 (N.D. Tex. 1999)). But, more to the point, a make-whole amount contractually triggered by a bankruptcy petition cannot antedate that same bankruptcy petition. First the petition is filed; then the make-whole amount becomes due—first the cause; then the effect. Thus, if it is indeed "interest," the make-whole amount is also "unmatured" as of the time of filing—and therefore subject to § 502(b)(2) disallowance.

Let us suppose, though, that Creditors' characterization of the Make-Whole Amount as something other than unmatured interest were correct. Their arguments would founder nonetheless. In our circuit, we evaluate whether a claim is disallowed under § 502(b)(2) based on whether the claim is for the "economic equivalent of unmatured interest"—not simply whether the claim is *itself* for "unmatured interest." *Pengo*, 962 F.2d at 546. What matters in this context is the underlying "economic reality" of the thing—not dictionary definitions or formalistic labels. *Id.* So, to the extent that Creditors argue, even successfully, that the Make-Whole Amount is not "unmatured interest," they are barking up the wrong tree.

2.

This brings us to Creditors' second chief contention: *Pengo* did not mean what it said when it interpreted § 502(b)(2) to disallow claims for the "economic equivalent of unmatured interest." Creditors attempt to cabin this controlling case to its facts. In *Pengo*, we held that a debt instrument with an "Original Issue Discount" (OID) constituted unmatured interest as a matter of "economic fact." *Id.* In essence, an OID security disguises interest as principal. [9] Recognizing this, we held that we must look through the labels assigned to claims to evaluate their underlying "economic realit[ies]." *Id.*; *accord* *Chateaugay*, 961 F.2d at 380 ("As a matter of economic definition, OID constitutes interest."). And when the reality of things—the economic fact of the matter—is that a particular claim is really just the functional equivalent of unmatured interest, § 502(b)(2) disallows it.

Creditors attempt to distinguish the Make-Whole Amount at issue here from *Pengo*'s OIDs on the basis that an OID is an "assured payment," whereas Creditors' Make-Whole Amount is "contingent." The relevance of this distinction, though, is hazy at best. At most, it shows that OIDs are not narrowly tailored liquidated damages that account for market conditions at the time of debtor breach. The Make-Whole Amount, meanwhile, *does* ***148** constitute well-tailored liquidated damages: it pays out only when and to the extent that the Creditors are actually harmed by Ultra's breach. Yet this distinction does nothing to mitigate the force of *Pengo*'s holding: If the claim in question is the "economic equivalent of unmatured interest," it is disallowed by § 502(b)(2). Whether the claim also happens to be denominated "liquidated damages" is beside the point. Like interest masquerading as "principal," interest labeled "liquidated damages" is still interest. [10]

3.

We thus arrive at Creditors' final set of arguments. Creditors broadly argue that the Make-Whole Amount is not the "economic equivalent of unmatured interest," but rather "liquidated damages," as a number of bankruptcy courts have held. *See, e.g.*, *In re Trico Marine Servs., Inc.*, 450 B.R. 474, 480 (Bankr. D. Del. 2011). They suggest that even though unmatured interest factors heavily into the Make-Whole Amount's calculation, the figure that the formula spits out is itself something different in kind. This argument is untenable.

Creditors acknowledge, as they must, that a key ingredient in the formula used to calculate the Make-Whole Amount is the sum of Ultra's unmatured interest (and principal) future payments. Creditors posit that the formula somehow transmogrifies its inputs, including the key input—unmatured interest—into something fundamentally different on the other side of the equals sign. To suggest otherwise, they say, "makes no more sense than saying that the area of a circle constitutes π because its formula is πr^2." Brief for Appellee Ad Hoc Committee of OpCo Unsecured Creditors at 40. This argument proves far too much. Consider this formula for a hypothetical 'Fake-Whole' Amount:

$$\text{Fake-Whole Amount} = (\Sigma\ [\text{all unmatured interest payments}] + \$1.00) \times 1$$

Of course, this Fake-Whole Amount is nothing more than unmatured interest plus one dollar (for good measure). Nothing transformative happened here. To determine whether a formula's output bears some identity with any of its inputs requires looking at the formula itself. And the Make-Whole formula, like the Fake-Whole formula, does nothing to its unmatured interest component to render the result different in kind.

In fact, the Make-Whole Amount's formula yields *precisely* the "economic equivalent" of Creditors' unmatured interest. The formula simply accounts for the time-value of money: A dollar today is worth more than a dollar tomorrow. The sum of unmatured interest payments today is worth more than that same set of payments paid out incrementally in the future. To create the "economic equivalent" of that unmatured interest *today*, the sum of those payments must be discounted by a factor representing the appropriate reinvestment rate—what the Creditors could earn on comparable securities in the present market. That is exactly what the ***149** Make-Whole formula does. The Make-Whole Amount is exactly the "economic equivalent of unmatured interest."

Creditors protest that the Make-Whole Amount functions more like ordinary damages to compensate them for the transaction costs involved in securing a comparable loan. Conceding that the dichotomy between "liquidated damages" and "unmatured interest" (or its "economic equivalent") is not so airtight as their briefs generally suggest, Creditors acknowledge that whether a given make-whole amount is allowable or disallowable liquidated damages turns "on the dynamics of the individual case." Brief for Appellee Ad Hoc Committee of OpCo Unsecured Creditors at 44, 46–47; Brief for Appellee OpCo Noteholders at 38–39; *see also* *Ultra*, 943 F.3d at 765. And Creditors insist that *this* Make-Whole Amount is *allowable* liquidated damages—not disallowed unmatured interest in the form of liquidated damages.

In making this argument, Creditors adopt by reference the bankruptcy court's chain of reasoning below. The bankruptcy court posed a hypothetical involving a three-party transaction: Borrower B prepays his Loan from Lender L, who turns to Broker K to identify a New Borrower N who will accept a New Loan identical to B's original Loan. But to find N and secure the loan at the same rate, K charges L a fee of 2%, which B must pay L in damages for prepayment. Would that 2% fee constitute unmatured interest? No, the court said, it is just the "negotiated cost to compensate the lender for making a new loan on comparable terms in a changed market." *Ultra*, 624 B.R. at 190. "The hypothetical is no different than the Make-Whole at issue here." *Id.*

But it *is* different. The relevant consideration is whether the make-whole amount merely compensates the borrower for the search and transaction costs of "seek[ing] to find someone else to use the capital," or goes further and compensates creditors for the loss of future interest "through the guise of a make-whole premium." Douglas G. Baird, Elements of Bankruptcy 84–85 (6th ed. 2014). [11] The bankruptcy court's helpful hypothetical illustrates the fact that there is non-overlapping space in the Venn Diagram between liquidated damages and unmatured interest. Liquidated damages certainly *can* compensate for anticipated transaction costs that are *not* unmatured interest. But the Make-Whole Amount, unlike the transaction-costs liquidated damages in the hypothetical, is *both* liquidated damages *and* the "economic equivalent of unmatured interest"—indeed, that is its whole point. [12]

***150** B.

Although we have concluded that Creditors' claim for the Make-Whole Amount is indeed a claim for unmatured interest or its economic equivalent as disallowed under 11 U.S.C. § 502(b)(2), we are not done. We must evaluate whether the solvent-debtor exception survived the Bankruptcy Code's enactment and applies to this case. We conclude that it does. For this reason, Ultra must pay the Make-Whole Amount.

In the ordinary case, the Bankruptcy Code would disallow a make-whole amount that functionally equates to unmatured interest. But this is not the ordinary case. Ultra became ultra solvent. And when a debtor is able to pay its valid contractual debts, traditional doctrine says it should—bankruptcy rules notwithstanding.

We begin with history, tracing the English provenance of the solvent-debtor exception, and its incorporation into American bankruptcy law. We then examine Ultra's contention that the 1978 Bankruptcy Code abrogated the traditional exception. Although it is a close call, the Supreme Court has instructed us not to infer abrogation of traditional bankruptcy practice. Because the Code's general bar on claims for unmatured interest does not specifically address the solvent-debtor scenario, for which traditional bankruptcy practice has always provided an exception, we conclude that the pre-Code doctrine concerning solvent debtors' obligations remains good law, and the exception operates in this case to suspend § 502(b)(2)'s disallowance of Creditors' Make-Whole Amount.

1.

For some three centuries of bankruptcy law, courts have held that an equitable exception to the usual rules applies in the unusual case of a solvent debtor. When a debtor proves solvent—that is, when the debtor's assets exceed its liabilities—bankruptcy's ordinary suspension of post-petition interest is itself suspended. When a debtor can pay its creditors interest on its unpaid obligations in keeping with the valid terms of their contract, it must. *Am. Iron & Steel Mfg. Co. v. Seaboard Air Line Ry.*, 233 U.S. 261, 266, 34 S.Ct. 502, 58 L.Ed. 949 (1914) ("[I]f, as a result of good fortune or good management, the [debtor's] estate prove[s] sufficient to discharge the claims in full, interest as well as principal should be paid."); *see also* *Debentureholders Protective Comm. of Cont'l Inv. Corp. v. Cont'l Inv. Corp.*, 679 F.2d 264, 269 (1st Cir. 1982) ("Where the debtor is solvent, the bankruptcy rule is that where there is a contractual provision, valid under state law, providing for interest on unpaid instalments of interest, the bankruptcy court will enforce the contractual provision with respect to both instalments due before *and* ... *after* the petition was filed." (emphasis added)).

As with many of our bankruptcy rules, this doctrine originated in eighteenth-century ***151** English practice. *See* 2 William Blackstone, Commentaries *488 ("[T]hough the usual rule is, that all interest on debts carrying interest shall cease from the time of issuing the commission, yet, in case of a surplus left after payment of every debt, such interest shall again revive, and be chargeable on the bankrupt ...."); *see also, e.g., Bromley v. Goodere* (1743) 26 Eng. Rep. 49, 52; 1 Atk. 75, 80 ("[S]uppos[ing] ... there should be a surplus, it would be absurd to say the creditors should not have interest ...."); *Ex parte Rooke* (1753) 26 Eng. Rep. 156, 157; 1 Atk. 244, 245 (ordering solvent bankruptcy petitioner "to pay the principal *and interest* ... to all his creditors" (emphasis added)). [13]

Our forebears adopted English practice in our nation's nascent nineteenth-century bankruptcy system. *See* *Sexton v. Dreyfus*, 219 U.S. 339, 344, 31 S.Ct. 256, 55 L.Ed. 244 (1911) (Holmes, J.) ("We take our bankruptcy system from England, and we naturally assume that the fundamental principles upon which it was administered were adopted by us when we copied the system ...."); [14] *see also* *Debentureholders*, 679 F.2d at 269 (referring to "the settled English and American law that when an alleged bankrupt is proved solvent, the creditors are entitled to receive post-petition interest before any surplus reverts to the debtor"). And as the Supreme Court has said, the English solvent-debtor exception "ha[s] been carried over into our system." *City of New York v. Saper*, 336 U.S. 328, 330 n.7, 69 S.Ct. 554, 93 L.Ed. 710 (1949); *see also* *United States v. Ron Pair Enters., Inc.*, 489 U.S. 235, 246, 109 S.Ct. 1026, 103 L.Ed.2d 290 (1989) (noting the solvent-debtor exception's "recogni[tion] under pre-Code [American] practice").

The reason for this traditional, judicially-crafted exception is straightforward: Solvent debtors are, by definition, able to pay their debts in full on their contractual terms, and absent a legitimate bankruptcy reason to the contrary, they should. Unlike the typical insolvent bankrupt, a solvent debtor's pie is large enough for every creditor to have his full slice. With an insolvent debtor, halting contractual interest from accruing serves the legitimate bankruptcy interest of equitably distributing a limited pie among competing creditors as of the time of the debtor's filing. *See* *Am. Iron & Steel*, 233 U.S. at 266, 34 S.Ct. 502. [15] With a solvent debtor, ***152** that legitimate bankruptcy interest is not present. [16] *See* *In re Chicago, Milwaukee, St. Paul & Pac. R.R. Co.*, 791 F.2d 524, 527–28 (7th Cir. 1986) (Posner, J.) ("The only good reason for refusing to give a creditor in reorganization all that he bargained for when he extended credit is to help other creditors, the debtor's assets being insufficient to pay all creditors in full .... [But] if the bankrupt is solvent the task for the bankruptcy court is simply to enforce creditors' rights according to the tenor of the contracts that created those rights ...."). Therefore, solvent debtors should be exempted from the general rule disallowing unmatured interest from accruing post-petition, and this "solvent-debtor exception" simply follows from the first principles of bankruptcy law.

2.

In the face of the solvent-debtor exception's historical provenance and comportment with bankruptcy's fundamental principles, Ultra argues that Congress nonetheless abrogated it in enacting the 1978 Bankruptcy Code. The Code's straightforward disallowance of claims for unmatured interest in § 502(b)(2) does not distinguish solvent and insolvent debtors. Ultra cites a string of bankruptcy court opinions and two circuit cases for the proposition that § 502(b)(2) applies regardless of debtor solvency. Brief for Appellants at 26 (citing, *inter alia, In re Gencarelli*, 501 F.3d 1 (1st Cir. 2007) and *In re Dow Corning Corp.*, 456 F.3d 668 (6th Cir. 2006)).[17] Ultra further urges the court to draw negative implications from the Code's provision for impaired creditors to receive interest at "the legal rate" when a debtor proves sufficiently solvent. *See* 11 U.S.C. §§ 726(a)(5), 1129(a)(7)(A)(ii). If Congress provided for interest in this circumstance but said nothing else about solvent debtors generally, no broader exception should be inferred —*expressio unius est exclusio alterius.*

Creditors respond with equal and opposite force. Under American bankruptcy statutes in place from the late nineteenth century through much of the twentieth century, claims for unmatured interest were expressly disallowed; nevertheless, courts regularly applied the solvent-debtor exception. *See* Bankruptcy Act of 1898, ***153** Pub. L. No. 55-541, § 63, 30 Stat. 544, 563 (1898) (limiting interest on provable claims to interest "which would have been recoverable" when the petition was filed, and subtracting "interests accrued *after* the filing of the petition" (emphasis added)); Bankruptcy Act of 1938 (Chandler Act), Pub. L. No. 75-696, § 63, 52 Stat. 840, 873 (1938) (same); *see, e.g., Johnson v. Norris*, 190 F. 459, 461–65 (5th Cir. 1911) (concluding that § 63 of the Bankruptcy Act "was not intended to be applied to a solvent estate"); *Ruskin v. Griffiths*, 269 F.2d 827, 829–32 (2d Cir. 1959) (awarding post-default interest on overdue interest and accelerated principal at a heightened contractual rate because the debtor was solvent, despite the then-applicable bankruptcy acts' preclusion of unmatured interest); *cf. Saper*, 336 U.S. at 330–32, 330 n.7, 69 S.Ct. 554 (acknowledging American adoption and retention of the solvent-debtor exception in our nation's bankruptcy practice, even after the Bankruptcy Act of 1898 and the 1938 Chandler Amendments codified the "long-standing rule against post-bankruptcy interest").[18]

This historical bankruptcy practice, Creditors argue, demonstrates that Congressional recodification of the Bankruptcy Act's § 63 disallowance of unmatured interest in § 502(b)(2) of the 1978 Bankruptcy Code did not expressly abrogate the solvent-debtor exception. If Congress legislated cognizant of courts' practice of excepting solvent debtors from the generally applicable statutory disallowance of § 63, one would expect it to have *expressly* abrogated the judicial exception if it intended to do so.

3.

The parties' competing arguments center on how we expect Congress to draft statutes and, specifically, what we are to make of congressional silence. Ultra assumes, not unreasonably, that Congress means what it says and that, when Congress says one thing but not another, it means to exclude what it did not say. Creditors, meanwhile, assume that Congress legislates against a historical backdrop, and that when courts historically have fashioned an exception to a clear statutory provision, Congress is presumed to accept that practice unless it expressly says otherwise. These equally sensible presumptions are at loggerheads.

The Supreme Court breaks the tie. We must defer to prior bankruptcy practice unless expressly abrogated. The Court has endorsed a substantive canon of interpretation regarding the Bankruptcy Code vis-à-vis preexisting bankruptcy doctrine. Namely, abrogation of a prior bankruptcy practice generally requires an "unmistakably ***154** clear" statement on the part of Congress; any ambiguity will be construed in favor of prior practice. *Cohen v. de la Cruz*, 523 U.S. 213, 221–22, 118 S.Ct. 1212, 140 L.Ed.2d 341 (1998) (stating that courts should "not read the Bankruptcy Code to erode past bankruptcy practice absent a clear indication that Congress intended such a departure" (quoting *Pa. Dep't of Pub. Welfare v. Davenport*, 495 U.S. 552, 563, 110 S.Ct. 2126, 109 L.Ed.2d 588 (1990))); *Midlantic Nat'l Bank v. N.J. Dep't of Envt'l Prot.*, 474 U.S. 494, 501, 106 S.Ct. 755, 88 L.Ed.2d 859 (1986) (indicating that the "normal rule of statutory construction" that courts "follow[ ] with particular care" in interpreting the Code is that "if Congress intends for legislation to change the interpretation of a judicially created concept, it makes that intent specific"); *Kelly v. Robinson*, 479 U.S. 36, 46, 53, 107 S.Ct. 353, 93 L.Ed.2d 216 (1986) (noting that "Congress enacted the Code in 1978 against the background of an established judicial exception ... created in the face of a statute drafted with considerable care and specificity" and finding no "significant evidence that Congress intended to change the law"); *see also* *Dewsnup v. Timm*, 502 U.S. 410, 419–20, 112 S.Ct. 773, 116 L.Ed.2d 903 (1992) (concluding that it is "not plausible" "to attribute to Congress the intention" to act "contrary to basic bankruptcy principles" "without ... mention[ing] [it] somewhere in the Code itself"). [19]

The provisions of the 1978 Bankruptcy Code do not clear this high hurdle. As the bankruptcy court explained, "Absent *clear* Congressional intent, provisions of the Bankruptcy Code did not abrogate universally recognized legal principles under the Bankruptcy Act. Nothing ... suggests that Congress intended to defang the solvent-debtor exception." *Ultra*, 624 B.R. at 198 (citation omitted) (emphasis added). We agree.

The Code's most relevant section, § 502(b)(2), tersely recodified § 63 of the preceding Chandler Act (and the 1898 Bankruptcy Act before it): It simply states that bankruptcy courts "shall allow [a] claim ... except to the extent that," among other things, "such claim is for unmatured interest." But this affords no greater clarity than the 1898 and 1938 Acts, which similarly limited claims for interest to what "would have been recoverable at" the date the bankruptcy petition was filed—*i.e.*, matured interest. § 63, 30 Stat. at 562–63; § 63, 52 Stat. at 873; [20] *see also* *Ultra*, 624 B.R. at 197 ("The Bankruptcy Act's treatment of unmatured interest was nearly identical to § 502(b)(2).").

Importantly, the text of these pre-Code bankruptcy acts did not stop courts from applying the traditional solvent-debtor exception. [21] In 1911, our court was called ***155** upon to determine whether the solvent-debtor exception survived enactment of the original Bankruptcy Act of 1898. *Johnson*, 190 F. at 461. The debtors in that case, like the debtors here, were solvent. Pointing to the Bankruptcy Act's bar against claims for interest other than what "could have been recoverable" on the date the bankruptcy petition was filed, the debtors argued that they were shielded from claims for unmatured interest despite their solvency. *Id.* at 461. In rejecting the debtors' argument, we cited longstanding bankruptcy law principles to conclude that the Bankruptcy Act's bar on unmatured interest simply "was not intended to be applied to the case of a solvent estate." [22] *Id.* at 462. *See also* *Ultra*, 624 B.R. at 196–98 (noting that this court "squarely held [in *Johnson*] that creditors of a solvent debtor may recover post-petition interest, *notwithstanding the plain text of § 63 of the Bankruptcy Act*," and that our sister circuits did likewise (emphasis added)); *supra* n.18.

The problem for the debtors in *Johnson* was not, as the dissenting opinion suggests, that the Bankruptcy Act was insufficiently explicit in its exclusion of claims for unmatured interest. The problem was that the Bankruptcy Act was insufficiently explicit about applying this general exclusion in solvent-debtor cases. *Cf.* *United States v. Texas*, 507 U.S. 529, 534, 113 S.Ct. 1631, 123 L.Ed.2d 245 (1993) ("In order to abrogate a common law principle, the statute must 'speak directly' to the question addressed by the common law."(citation omitted)). That is why *Johnson* held that the traditional rule would continue to apply absent an "express provision ... allowing interest that accrues after the filing of the petition to be paid out of a surplus ... to the bankrupt." 190 F. at 463. The Bankruptcy Code, like its predecessors, did not give us that.

Ultra complains that this manner of statutory interpretation, which allows judicial practice to override otherwise clear statutory text, is taken from a "time capsule." But as the Creditor Committee Appellees have pointed out, this mode of statutory interpretation is alive and well. Indeed, the Supreme Court very recently applied an analogous interpretive approach in the patent law context. *See* *Minerva Surgical, Inc. v. Hologic, Inc.*, ––– U.S. ––––, 141 S. Ct. 2298, 2307–08, 210 L.Ed.2d 689 (2021) (noting that the Patent Act of 1952 has "similar language" to its precursor statute against which the judicial exception of assignor estoppel developed, thus suggesting that that language did not evince sufficiently plain Congressional intent to abrogate the doctrine). We are at no greater liberty to disregard the Supreme Court's instructions in the bankruptcy context than we are in the patent domain. We remain bound by the substantive canon of Bankruptcy Code interpretation embraced in *Cohen*, *Midlantic*, and *Kelly*.

Congress has not explicitly addressed claims for unmatured interest owed by solvent debtors. Nonetheless, statutory language may carry crucial context. *See generally* Antonin Scalia, *Common-Law Courts in a Civil-Law System: The Role of United States Federal Courts in Interpreting the Constitution and* ***156** *Laws, in* A MATTER OF INTERPRETATION: FEDERAL COURTS AND THE LAW

3, 24 (new ed. 2018) (explaining why "the good textualist is not a literalist"). And here, that context is the backdrop of traditional bankruptcy practice. The Supreme Court has dictated that we presume Congress did not mean to abrogate traditional bankruptcy practice "absent a clear indication that Congress intended such a departure." *Cohen*, 523 U.S. at 221, 118 S.Ct. 1212. Considered in the context of what came before, the text of § 502(b)(2) hardly constitutes an unambiguous—let alone explicit—change in bankruptcy practice. [23] *See* *Dewsnup*, 502 U.S. at 419–20, 112 S.Ct. 773; *Bodenheimer*, 592 F.3d at 673–74. Accordingly, we hold that the Code did not abrogate the longstanding judicial exception for cases involving solvent debtors. We thus hold that the solvent-debtor exception is alive and well. The 1978 Code's disallowance of unmatured interest did not abrogate the exception with "unmistakable" clarity. *Cohen*, 523 U.S. at 221–22, 118 S.Ct. 1212. Because Ultra was solvent—indeed, "massively" solvent—the solvent-debtor exception plainly applies in this case. For that reason, Ultra must pay Creditors the contractual Make-Whole Amount—even though, as we have already determined, *see supra* section II.A., it is indeed otherwise disallowed unmatured interest.

C.

We are not done quite yet. We have determined that the Make-Whole Amount is unmatured interest, and therefore, that it is disallowed under the Code. We have also determined, however, that the solvent-debtor exception survived the Code's enactment and applies to this case. But the solvent-debtor exception *only* ensures that solvent debtors make good on their *valid* contractual obligations. So Ultra argues, in the alternative, that the Make-Whole Amount is an unenforceable penalty under governing state law. If that were so, the Bankruptcy Code would still disallow it—the solvent-debtor exception notwithstanding. We conclude, though, that the Make-Whole Amount constitutes enforceable liquidated damages under New York law. Therefore, the solvent-debtor exception continues to apply, and Ultra must keep its contractual promise.

***157** Section 502(b)(1) of the Bankruptcy Code disallows "claim[s] [that are] unenforceable against the debtor ... under any agreement or applicable law." The MNPA is governed by New York law. If New York law would prohibit enforcement of the Make-Whole Amount as an unenforceable penalty, the Code would not allow it as a claim, and the solvent-debtor exception could not resuscitate it.

We turn then to New York contract law. As the "party seeking to avoid liquidated damages," Ultra bears the burden of showing that the Make-Whole Amount is "in fact, a penalty." *JMD Holding Corp. v. Cong. Fin. Corp.*, 4 N.Y.3d 373, 795 N.Y.S.2d 502, 828 N.E.2d 604, 609 (2005). To do so, Ultra must show that the "amount fixed is plainly or grossly disproportionate to the probable loss" incurred by Noteholder Creditors as a result of default. *Id.* (quoting *Truck Rent-A-Ctr., Inc. v. Puritan Farms 2nd, Inc.*, 41 N.Y.2d 420, 393 N.Y.S.2d 365, 361 N.E.2d 1015, 1018 (1977)). Showing that the Make-Whole Amount effectively grants double recovery would meet that test under New York law. *See, e.g.,* *172 Van Duzer Realty Corp. v. Globe Alumni Student Assistance Ass'n Inc.*, 24 N.Y.3d 528, 25 N.E.3d 952, 957 (2014).

Ultra asserts the Make-Whole Amount to be unreasonably disproportionate and thus an unenforceable penalty because it allows for double recovery. The alleged double recovery stems from the fact that the MNPA "allows the Noteholders to charge ongoing interest on the accelerated principal at a 'default' rate." Brief for Appellants at 34. Since Creditors already get contractual interest on the accelerated principal, the argument goes, the Make-Whole Amount, which compensates Noteholder Creditors for the future interest payments that would have been made on the *same* accelerated principal, gives Creditors double recovery.

This argument withers under scrutiny. The Make-Whole Amount and the post-petition interest address two different harms. *Ultra*, 575 B.R. at 370–71. [24] The Make-Whole Amount serves as liquidated damages for Ultra's breach; the post-petition interest compensates for Ultra's lag in paying the accelerated principal (and the Make-Whole itself), which were already due and payable for the duration of the bankruptcy. Separate harms warrant separate recoveries; accordingly, the Make-Whole Amount is not unenforceable on this theory.

Absent any other alternative theory to show that the Make-Whole Amount is unreasonably disproportionate, Ultra fails to meet its burden. *JMD Holding*, 795 N.Y.S.2d 502, 828 N.E.2d at 609. The Make-Whole Amount is enforceable under New York law; therefore, § 502(b)(1) does not stand in the way of the solvent-debtor exception.

D.

We turn, finally, to post-petition interest. Ultra concedes that Creditors are entitled to *some* post-petition interest on their claims to compensate for the duration of the bankruptcy proceedings. But Ultra insists that the appropriate rate is the Federal Judgment Rate specified at 28 U.S.C. § 1961(a)—not the parties' much higher contractual default rate. [25] And Ultra ***158** reiterates that the solvent-debtor exception does not apply to suspend that rule's application here. We conclude that the contractual default rate is appropriate here.

Ultra recognizes, as it must, that unsecured creditors of solvent debtors are entitled to post-petition interest on their claims if they are to be deemed unimpaired. *See* *In re New Valley Corp.*, 168 B.R. 73, 81 (Bankr. D.N.J. 1994) (holding that "a solvent debtor is not required to pay postpetition interest on claims of unsecured creditors who are unimpaired"); Bankruptcy Reform Act of 1994, Pub. L. No. 103-394, § 213(d), 108 Stat. 4106, 4125–26 (overruling *New Valley* by repealing 11 U.S.C. § 1124(3) (1988), and, in effect, requiring payment of post-petition interest in order for unsecured creditors to be unimpaired); *see also* *In re PPI Enterprises (U.S.), Inc.*, 324 F.3d 197, 205–07 (3d Cir. 2003) (recognizing and explaining *New Valley*'s statutory abrogation). Ultra asserts, though, that post-petition interest is to be calculated at the Federal Judgment Rate, "no more and no less." Brief for Appellants at 43.

Ultra's argument depends on a series of statutory inferences. For a plan to be confirmed, creditors must either be unimpaired (and therefore "conclusively presumed to have accepted the plan," 11 U.S.C. § 1126(f)), or impaired but either (1) voting in favor of the plan, *see id.* § 1129(a)(7)(A)(i), or (2) no worse off than they would be in a chapter 7 liquidation, *see id.* § 1129(a)(7)(A)(ii). Creditors are presumed "impaired under a plan unless ... the plan leaves unaltered the[ir] legal, equitable, and contractual rights." *Id.* § 1124(1). If, therefore, creditors are deemed "unimpaired," § 1124 necessarily requires that their "legal, equitable, and contractual rights" remain "unaltered." And per Congress's statutory overruling of *New Valley* noted above, that entails provision for post-petition interest.

The question remains: how much? As to *unimpaired* creditors, the Code does not itself say. So Ultra turns to what it says about *impaired* creditors. It is reasonable, after all, to infer that creditors who are *unimpaired* (as Creditors here are stipulated to be) cannot be treated any worse than *impaired* creditors, who at least get to vote on the plan.

The Code provides that a bankruptcy court can "cram down" a plan on impaired creditors, over their objection, if they "will receive or retain under the plan ... not less than the amount that [they] would so receive or retain if the debtor were liquidated under chapter 7." *Id.* § 1129(a)(7)(A)(ii). In turn, what the creditors would get if the debtor were liquidated is specified in § 726(a). Section 726(a) provides a waterfall for the distribution of a debtor's assets in a Chapter 7 liquidation. Before a solvent debtor's equity holders get any of the estate's leftovers, § 726(a)(5) says that creditors are to be paid interest on their claims "at the legal rate" from the petition date.

Ultra hangs its hat on these words. The "legal rate," it insists, must be the Federal Judgment Rate. Ultra cites and deploys many of the same arguments propounded in a Ninth Circuit case, *In re Cardelucci*, 285 F.3d 1231 (9th Cir. 2002). For instance, the definite article "the" that precedes "legal rate" in § 726(a)(5) indicates that the rate is singular and not variable—and the only reasonable single rate under federal law is the Federal Judgment Rate. *Id.* at 1234. And, as our sister circuit suggests, ***159** "the commonly understood meaning of 'at the legal rate' at the time the Bankruptcy Code was enacted was a rate fixed by statute"—and the Federal Judgment Rate is the most likely candidate. *Id.* at 1234–35. This conclusion, Ultra and the *Cardelucci* court continue, advances the bankruptcy system's interests in "ensur[ing] equitable treatment of creditors" by compensating them all at the same rate for the same duration of bankruptcy proceedings, and, happily, it is eminently administrable. *Id.* at 1235–36. [26]

We do not quarrel with the *Cardelucci* court's sensible reasoning, but neither must we decide the matter. The precise referent of "the legal rate" is not dispositive here. Why? Because Ultra overlooks the logically prior textual fact that "the legal rate" only sets a *floor*—not a ceiling—for what an impaired (and by implication, unimpaired) creditor is to receive in a cram-down scenario. Specifically, the Code provides that objecting, impaired creditors must receive "*not less* than" what they would receive in a Chapter 7 liquidation—including "interest at the legal rate" per § 726(a)(5)—in order for the plan to be "crammed down" on them. *See id.* § 1129(a)(7)(A)(ii) (emphasis added).

So, even if "the legal rate" is the Federal Judgment Rate, the Code does not preclude unimpaired creditors from receiving default-rate post-petition interest in excess of the Federal Judgment Rate in solvent-debtor Chapter 11 cases. *See* Shelley & Noh, *supra* note 16, at 368–69 (arguing that "§ 1129(a)(7) should not be interpreted to *require* the application of the federal judgment rate" and that "the fair and equitable test [of § 1129(b)] will, in many instances, permit the payment of interest at a higher rate, particularly when the higher rate is set forth in a contract"). Recall that under § 1124(1), *unimpaired* creditors' "legal, equitable, and contractual rights" must remain "unaltered." And as a matter of equity, creditors are entitled to contractually specified rates of interest "on" their claims when a solvent debtor is fully capable of paying up. [27] As the bankruptcy court rightly noted below, "[t]his equitable right is the root of the solvent-debtor exception." *Ultra*, 624 B.R. at 203. [28] And as we have explained, the solvent-debtor exception survived the Bankruptcy Code's enactment. *See supra* Section II.B.

The requirements of § 1129(b) for plan confirmation buttress our conclusion. That section states that the bankruptcy ***160** court shall only confirm a plan if it is "fair and equitable"—a test long understood to mean the "absolute priority rule." *See* 11 U.S.C. § 1129(b)(2)(B)(ii); *In re Linn Energy, L.L.C.*, 936 F.3d 334, 341 n.1 (5th Cir. 2019) ("The absolute priority rule requires that certain classes of claimants be paid in full before any member of a subordinate class is paid." (quoting *In re Seaquest Diving, LP*, 579 F.3d 411, 420 n.5 (5th Cir. 2009))). As the bankruptcy court explained well, unsecured creditors vying against each other for shares of a "limited pot of assets" have no equitable rights vis-à-vis each other to contractual rates of interest on their claims: they must be treated equally; but "[w]hen the struggle is between creditors *and equity holders*, as opposed to creditors and creditors, [creditors'] equitable right [to contractual post-petition interest rates] is critical." *Ultra*, 624 B.R. at 203 (emphasis added). And per the absolute priority rule, creditors' rights prevail.

III.

To sum up, Ultra is right about one thing: Creditors' Make-Whole Amount is disallowed "unmatured interest" under the Bankruptcy Code. But the traditional solvent-debtor exception compels payment of the Make-Whole Amount because it is a valid contractual debt under applicable state law. For similar reasons, Ultra cannot avoid payment of contractual default-rate interest in favor of the much-lower Federal Judgment Rate: Creditors are entitled to what they bargained for with this solvent debtor, and the Code does not preclude the contractual interest rate. The judgment of the bankruptcy court is AFFIRMED.

Andrew S. Oldham, Circuit Judge, dissenting:

The majority correctly concludes that the Make-Whole Amount is unmatured interest in disguise. And it acknowledges that the Bankruptcy Code bars all unmatured interest. *See* 11 U.S.C. § 502(b)(2). In my view, it necessarily follows that the Code bars the Make-Whole Amount.

The majority nevertheless holds that an unwritten solvent-debtor exception "operates in this case to suspend § 502(b)(2)'s disallowance of [the] Make-Whole Amount." *Ante*, at 150. I recognize that the majority is attempting to faithfully apply confusing Supreme Court precedent in a difficult case. But the clear statutory text governing this issue compels me to respectfully dissent.

I.

In my view, the solvent-debtor exception didn't survive the adoption of the Bankruptcy Code. Premise one: If it's "unmistakably clear" that a Code provision is incompatible with a prior bankruptcy practice, then the Code overrides that prior practice. [1] *Cohen v. de la Cruz*, 523 U.S. 213, 221–22, 118 S.Ct. 1212, 140 L.Ed.2d 341 (1998); *see also ante*, at 154 (collecting cases). Premise two: It's unmistakably clear that 11 U.S.C. § 502(b)(2), which allows a given claim "except to the extent that ... (2) such claim is for unmatured interest," is incompatible with the preexisting solvent-debtor exception. Conclusion: The Code overrides the solvent-debtor exception.

I take the first premise to be uncontroversial, *see ante*, at 154, but I should elaborate on the second. The Code provides that all claims for unmatured interest ***161** are disallowed. The solvent-debtor exception provides that not all claims for unmatured interest are disallowed. That's a stark contradiction. And the statutory text offers no alternative interpretation to avoid it, as the majority appears to recognize. *See ante*, at 250 ("[W]e conclude that the pre-Code doctrine concerning solvent debtors' obligations remains good law, *and the exception operates in this case to suspend § 502(b)(2)'s disallowance* of Creditors' Make-Whole Amount." (emphasis added)); *see generally id.* at 150-56 (majority's analysis, contending the statutory text isn't clear enough but not explaining what else the text could mean).

II.

The majority nonetheless disputes the second premise, maintaining it's *not* unmistakably clear that 11 U.S.C. § 502(b)(2) is incompatible with the solvent-debtor exception. Its analysis begins with the Bankruptcy Acts of 1898 and 1938. *See ante*, at 152-53 (citing Bankruptcy Act of 1898, 30 Stat. 544; Bankruptcy Act of 1938, 52 Stat. 840). For reference, here's the relevant text:

> Debts of the bankrupt may be proved and allowed against his estate which are (1) a fixed liability, as evidenced by a judgment or an instrument in writing, absolutely owing at the time of the filing of the petition against him, whether then payable or not, *with any interest thereon which would have been recoverable at that date* or with a rebate of interest upon such as were not then payable and did not bear interest; (2) due as costs taxable against an involuntary bankrupt who was at the time of the filing of the petition against him plaintiff in a cause of action which would pass to the trustee and which the trustee declines to prosecute after notice; (3) founded upon a claim for taxable costs incurred in good faith by a creditor before the filing of the petition in an action to recover a provable debt; (4) founded upon an open account, or upon a contract express or implied; and (5) founded upon provable debts reduced to judgments after the filing of the petition and before the consideration of the bankrupt's application for a discharge, less costs incurred and interests accrued after the filing of the petition and up to the time of the entry of such judgments.
>
> ...
>
> A claimant shall not be entitled to collect from a bankrupt estate any greater amount than shall accrue pursuant to the provisions of this Act.

Act of 1898, §§ 63(a), 65(e), 30 Stat. at 562–63, 564 (emphasis added). The 1938 Act has almost identical wording —none of the slight differences are relevant here. *See* Act of 1938, § 63(a), 65(e), 52 Stat. at 873, 875.

The majority points to the italicized text, contending it amounts to a rather obvious bar on unmatured interest. *See ante*, at 154-55. At the least, the majority says, this antique unmatured-interest bar is just as clear as 11 U.S.C. § 502(b)(2)'s current bar. *See ibid.* (quoting the latter provision and saying, "this affords no greater clarity than the 1898 and 1938 Acts, which similarly limited claims for interest to what 'would have been recoverable at' the date the bankruptcy petition was filed—*i.e.*, matured interest" (citation omitted)).

The majority then cites a handful of old cases that read the 1898 and 1938 Acts not to foreclose the solvent-debtor exception. *Ante*, at 152-53 (collecting cases). One of the cases cited is even binding precedent in this circuit. *See Johnson v. Norris*, 190 F. 459 (5th Cir. 1911). If the old statutory bar on unmatured interest was just as clear as the Code's current bar, aren't we obligated to follow these precedents? Put ***162** differently, 11 U.S.C. § 502(b)(2) can't possibly be an "unmistakably clear" indication that Congress wanted to deviate from courts' longstanding interpretation of the 1898 and 1938 Acts. *See Cohen*, 523 U.S. at 221–22, 118 S.Ct. 1212. So goes the argument.

The problem, in my view, is that the old statutes *weren't* just as clear as 11 U.S.C. § 502(b)(2) is. It's simply not true that the 1898 and 1938 Acts precluded unmatured interest, full stop. Rather, the language quoted by the majority—"with any interest thereon which would have been recoverable at that date"—comes from a clause (which is offset by a comma) in one item in a five-item list (whose entries are separated by semicolons). *See Ante*, at 154-55 (quoting Act of 1898 § 63(a)(1), 30 Stat. at 562–63; Act of 1938, § 63(a)(1), 52 Stat. at 873). The quoted text therefore modifies *only* that first item, as the block quote above makes clear. That first item, in turn, concerns a specific subset of claims: "a fixed liability, as evidenced by a judgment *or an instrument in writing*, absolutely *owing at the time of the filing of the petition.*" Act of 1898, § 63(a)(1), 30 Stat. at 562–63 (emphasis added); Act of 1938, § 63(a)(1), 52 Stat. at 873 (emphasis added). Contrast that with the category of claims discussed in the last listed item: "provable debts *reduced to judgments after the filing of the petition* and before the consideration of the bankrupt's application for a discharge." Act of 1898, § 63(a)(5), 30 Stat. at 563 (emphasis added); Act of 1938, § 63(a)(5), 52 Stat. at 873 (emphasis added). (The Make-Whole Amount at issue in this case, which seems never to have been reduced to judgment, is itself a good example of a debt that doesn't fit into the latter category but does fit into the former.) The upshot: Though § 63(a)(1) of the Acts expressly prohibits *some* unmatured interest, it *does not* contain a blanket bar on all unmatured interest—unlike 11 U.S.C. § 502(b)(2).

It also bears emphasis that the old § 63(a)(1) operates differently and less directly to bar unmatured interest than does § 502(b)(2). To see the old bar, we need to read § 63(a) together with § 65(e). The former gives a five-item list of allowed claims—claims upon which a creditor could recover in bankruptcy. Act of 1898, § 63(a), 30 Stat. at 562–63 (beginning with, "[d]ebts of the bankrupt may be proved and allowed against his estate which are ..." and going on to provide five categories of recoverable debts); Act of 1938, § 63(a), 52 Stat. at 873 (nearly identical). As we've seen, that list contains some qualifications, but it mainly serves the *positive* function of listing *what is permissible.* And the first permissible claims is "a fixed liability, as evidenced by a judgment or an instrument in writing, absolutely owing at the time of the filing of the petition against him, whether then payable or not, *with any interest thereon which would have been recoverable at that date* or with a rebate of interest upon such as were not then payable and did not bear interest." Act of 1898, § 63(a)(1), 30 Stat. at 562–63 (emphasis added); Act of 1938, § 63(a), 52 Stat. at 873 (emphasis added). Thus, claims for *matured* interest are allowed. [2]

Section 65(e) is a sort of zipper clause. It provides that "[a] claimant shall not be entitled to collect from a bankrupt estate ***163** any greater amount than shall accrue pursuant to the provisions of this Act." Act of 1898, § 65(e), 30 Stat. at 564; Act of 1938, § 65(e), 52 Stat. at 875. That provision serves the *negative* function of stipulating that every claim not listed as permissible *is not permissible.* But because § 63(a)(1) allows matured interest without allowing unmatured interest, and because no *other* provision allows unmatured interest, it follows that unmatured interest is barred by the combination and implication of §§ 63(a)(1) and 65(e).

The very first of the majority's old cases, *Johnson v. Norris*, interpreted the Act of 1898 in just this way. First, our court noted that § 63(a)(1) allows claims for matured interest. *Johnson*, 190 F. at 461. Second, we pointed out that § 65(e) disallows any claims not allowed. *Ibid.* Third, we *inferred* that "[o]rdinarily, no question as to subsequently accruing interest can arise," *i.e.*, that unmatured interest is generally barred. *Ibid.* We then went on to hold that this bar didn't apply in solvent-debtor cases. *Id.* at 461–65. The important point for present purposes, however, is that the *Johnson* court *did not* (a) hold that the Acts expressly barred the unmatured interest and (b) then hold the express bar inapplicable in solvent-debtor cases. Rather, the court (a) held (correctly) that the Acts *implicitly* barred unmatured interest and (b) then held the implicit bar inapplicable in solvent-debtor cases.

So the *Johnson* court saw more ambiguity in the Acts than today's majority does. And that's doubly important because *Johnson* proved to be the seminal case on the topic. Three years after the decision, the Supreme Court reached the same conclusion, citing only two sources in support: Blackstone and *Johnson. See* *Am. Iron & Steel Mfg. Co. v. Seaboard Air Line Ry.*, 233 U.S. 261, 266, 34 S.Ct. 502, 58 L.Ed. 949 (1914) (explaining that the general rule against unmatured interest "did not prevent the running of interest during the Receivership; and if as a result of good fortune or good management, the estate proved sufficient to discharge the claims in full, interest as well as principal should be paid"). Three of the majority's cited cases relied on *Johnson* in similar fashion. *See* *Brown v. Leo*, 34 F.2d 127, 128 (2d Cir. 1929); *Littleton v. Kincaid*, 179 F.2d 848, 852 (4th Cir. 1950); *In re Magnus Harmonica Corp.*, 159 F. Supp. 778, 780 (D.N.J. 1958). This widespread reliance suggests that courts allowed the solvent-debtor exception to persist, not because they thought the exception could override an *explicit* congressional prohibition on unmatured interest, but because they thought any such prohibition was *implicit* at best under the old Code. As the Supreme Court put it in 1949, "[t]he long-standing rule against post-bankruptcy interest thus appears *implicit* in our current Bankruptcy Act." *City of New York v. Saper*, 336 U.S. 328, 332, 69 S.Ct. 554, 93 L.Ed. 710.

If all of that sounds convoluted, that's precisely the point. The majority's argument rests on the premise that the 1898 and 1938 Acts barred unmatured interest just as clearly as does 11 U.S.C. § 502(b)(2). *See ante*, at 154-55. But that premise is, with deepest respect, false. The old statutes *did* bar unmatured interest—but the reader has to stitch together two separate provisions and make an inference from them to see it. The current Code, in sharp contrast, goes for the jugular by flatly disallowing "claim[s] for unmatured interest." 11 U.S.C. § 502(b)(2). The majority protests that "Congress has not explicitly addressed claims for unmatured interest owed by solvent debtors," *ante*, at 155, but I am not sure what Congress should have done to make the point more lucid short of saying, "and the solvent-debtor exception doesn't apply." Congress need ***164** not speak superfluously to speak "unmistakably." *See* *Cohen*, 523 U.S. at 221–22, 118 S.Ct. 1212; *BFP v. Resol. Tr. Corp.*, 511 U.S. 531, 546, 114 S.Ct. 1757, 128 L.Ed.2d 556 (1994) ("The Bankruptcy Code can of course override by implication when the implication is unambiguous.").

* * *

We all agree that the Make-Whole Amount is unmatured interest. And we all agree that 11 U.S.C. § 502(b)(2) bars unmatured interest. I would leave it at that. The Make-Whole Amount should be barred, and the creditors should recover post-petition interest only at the federal judgment rate. Neither the solvent-debtor exception's historical pedigree nor its policy underpinnings—no matter how compelling—can overcome Congress's clear, and clearer-than-ever, command on this point.

I respectfully dissent.

All Citations

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Footnotes

1 Unless otherwise indicated, "Creditors" will generally refer to both groups of creditor–appellees: (1) OpCo Noteholders (a group of over forty insurance companies, hedge funds, and other institutional investors); and (2) the Ad Hoc Committee of OpCo Unsecured Creditors, which represents both note and revolver creditors (a similar group of twenty investors).

2 The Federal Judgement Rate as of April 29, 2016, the date of Ultra's bankruptcy petition (the applicable rate for the confirmed plan) was 54 basis points (0.54%), which is materially lower than the contractual rate, defined as the greater of 2% over either of two benchmark rates. 28 U.S.C. § 1961; Post-Judgment Interest Rates – 2016, (Week Ending April 22, 2016), United States District & Bankruptcy Court, Southern District of Texas, https://www.txs.uscourts.gov/page/post-judgment-interest-rates-2016.

3 Here is the nitty-gritty: The MNPA defines the Make-Whole Amount as "the excess, if any, of the Discounted Value of the Remaining Scheduled Payments with respect to the Called Principal of such fixed rate Note over the amount of such Called Principal." The "Remaining Scheduled Payments" are the payments of interest and principal that would have occurred absent OpCo's default. These payments are summed and discounted to their present value using a discount factor 50 basis points over the yield to maturity of Treasury securities comparable in risk profile to the OpCo Notes. From this figure is subtracted the "Called Principal"—the unpaid balance of the Notes' principal that was accelerated on default. The Make-Whole Amount is any resultant positive number.

4 Both instruments defined the rate as the greater of two percent over the Notes' usual rate or two percent over the JPMorgan Chase prime rate.

5 As noted above, the applicable Federal Judgment Rate as of Ultra's petition date would have been 54 basis points (0.54%), which is materially less than the contractual default rate of over 2%. *See supra* n.2.

6 The bankruptcy court granted Ultra's motion for certification of direct appeal, and this court granted Ultra's petition for direct appeal. We therefore have jurisdiction over this appeal under 28 U.S.C. § 158(d)(2).

7 *See also* *In re Doctors Hosp. of Hyde Park, Inc.*, 508 B.R. 697, 705 (Bankr. N.D. Ill. 2014) (noting that "courts look to the *economic substance* of the transaction to determine what counts as interest" and holding that a "Yield Maintenance Premium" is subject to § 502(b)(2) disallowance because it "serves the purpose of interest *in economic reality*" (emphases added)); *In re Ridgewood Apartments of DeKalb Cnty., Ltd.*, 174 B.R. 712, 720–21 (Bankr. S.D. Ohio 1994) (holding the "clear purpose [of] a prepayment penalty" to be to "compensate the lender for anticipated interest," and therefore disallowing a claim for such); *In re Pub. Serv. Co. of N.H.*, 114 B.R. 800, 803 (Bankr. D.N.H. 1990) (holding that, "in economic fact," an original issue discount "is interest" subject to § 502(b)(2)); *cf.* *Thrifty Oil Co. v. Bank of Am. Nat'l Tr. & Sav. Ass'n*, 322 F.3d 1039, 1048–49 (9th Cir. 2003) (holding that damages stemming from default on interest-rate swap cannot constitute "interest" under § 502(b)(2) because "[a] fundamental characteristic of an interest rate swap is that the counterparties never actually loan or advance the notional amount"); *In re Hertz Corp.*, 637 B.R. 781, 791 (Bankr. D. Del. 2021) (adopting the "economic equivalent of unmatured interest" interpretation of § 502(b)(2)).

8 If we accepted Creditors' contention that the Make-Whole Amount could not be "interest" because it does not compensate for the (prior) use of another's money, then the term "unmatured interest" in 11 U.S.C. § 502(b)(2) would be vacuous: Until it matures, *no* "interest" compensates for the use of another's money —it is "interest" only in an anticipatory sense (*i.e.*, it *will* compensate for the use of another's money when it becomes due). Interest is only "interest" when it matures. On Creditors' argument, therefore, "unmatured interest" would be a paradox.

Creditors also recharacterize the Make-Whole Amount as "compensat[ion] ... for Ultra's decision *not* to use their money." Brief for Ad Hoc Committee of OpCo Unsecured Creditors at 38 (quoting *Ultra*, 624 B.R. at 188). But this, again, is just another way of saying that the Make-Whole Amount *is* interest—albeit *future* interest that will never mature because of Ultra's default.

9 Here is a simple example of how an OID works: Lender L issues Debtor D a loan in return for a Security S with a face value of $100. But, instead of handing over $100, L gives D only $90. Still, S's principal is $100 and must be repaid over the term of the loan. The $10 difference between face-value principal and actual credit extended, while denominated "principal," serves exactly the same purpose as interest: it compensates L for extending the loan.

10 Creditors also unpersuasively urge that *Pengo* was really just about OIDs, pointing to our icing-on-the-cake argument from legislative history: the Code's drafters mentioned OIDs as examples of claims disallowed under § 502(b)(2). But in *Pengo*, we prefaced our mention of this fact with: "*Moreover*, the legislative history *verifies* our [conclusion] ...." 962 F.2d at 546 (emphases added). We certainly did *not* suggest that legislative history was dispositive in *Pengo*, let alone that legislative history could narrow the scope of a statutory provision. And regardless, as we have recently said, also in interpreting the Bankruptcy Code, "We

are reluctant to rely on legislative history for the simple reason that it's not law." *In re DeBerry*, 945 F.3d 943, 949 (5th Cir. 2019).

11 *See Hertz*, 637 B.R. at 791 ("If it were enough to just label a make-whole claim liquidated damages ... , then a contract providing that on default or redemption 'all unmatured interest' would be immediately due and payable could avoid the effect of section 502(b)(2) completely.").

12 *But see generally* Douglas G. Baird, *Making Sense of Make-Wholes*, 94 Am. Bankr. L.J. 567, 580 (2020) ("When a make-whole clause represents the parties' good faith estimate of the loss of a favorable rate of interest, it is merely serving as a liquidated damages clause, and bankruptcy judges should enforce it for the same reason judges enforce such clauses outside of bankruptcy."). Professor Baird eloquently argues that a claim for the difference between a fixed and floating interest rate does not *necessarily* constitute unmatured interest. *Id.* at 579–580 ("An obligation owed on a bad bet—involving changes in the rate of interest or anything else—is not in and of itself an obligation to pay unmatured interest."); *but cf.* *Thrifty Oil Co.*, 322 F.3d at 1048–49 (implying, in a case involving interest-rate swaps, that such a claim is not "interest" only when "no advance of money has occurred between the ... counterparties" with respect to that claim—*i.e.*, when there is no principal). Professor Baird makes the case that make-whole amounts in a variable interest-rate environment are different in kind than sums of unmatured fixed-rate interest in a stable interest-rate market. He concludes that it comports with longstanding bankruptcy principles and policy to allow claims for make-whole amounts.

Be that as it may, the Code as interpreted by this circuit's binding precedent disallows the "economic equivalent of unmatured interest." *Pengo*, 962 F.2d at 546. And, as discussed above, Creditors' Make-Whole Amount represents the economic equivalent of interest that had not matured as of the petition date, even though it *also* constitutes liquidated damages. The conclusion inexorably follows that the Make-Whole Amount must be disallowed under current law, even though policy considerations may favor allowance.

13 *See also, e.g., Ex parte Mills* (1793) 30 Eng. Rep. 640, 644; 2 Ves. Jun. 294, 303 (ordering payment of "interest upon [the solvent bankrupt's] debts, as either upon the face of the security or by force of the contract between the parties carry interest"); Bankruptcy Act of 1825, 6 Geo. 4 c. 16, § 132 (codifying the doctrine that "all Creditors whose Debts are now by Law entitled to carry Interest, in the Event of a Surplus, shall first receive Interest on such Debts ...."); *cf. Ex parte Marlar* (1746) 26 Eng. Rep. 97, 98; 1 Atk. 150, 152 (stating the rule in solvent-debtor cases "that note-creditors have no right to prove interest upon them, *unless it is expressed in the body of the notes*"); *Ex parte Williams.—In the Matter of Wilcocks*, 1 Cases in Bankruptcy 399, 399 (George Rose ed. 1813) ("Where there is a Surplus of the Bankrupt's Estate, Creditors are not entitled to Interest upon Debts, *unless it has been provided for by Contract*, either express, or implied ...." (emphasis added)).

14 *But see* *Sloan v. Lewis*, 89 U.S. 150, 157, 22 Wall. 150, 22 L.Ed. 832 (1874) ("The English cases referred to in the argument, in our opinion, have no application here. They are founded upon the English statutes and the established practice under them. Our statute is different in its provisions and requires, as we think, a different practice.")

15 *See also* Thomas H. Jackson & Robert E. Scott, *On the Nature of Bankruptcy: An Essay on Bankruptcy Sharing and the Creditors' Bargain*, 75 Va. L. Rev. 155, 155 (1989) ("[P]rebankruptcy entitlements should be impaired in bankruptcy only when necessary to maximize net asset distributions to the creditors as a group ...."); Ginsburg & Martin on Bankruptcy § 1.01 (6th ed. 2022) (noting that the primary goal of United States bankruptcy law is to "promote equality of distribution among similarly situated creditors" from a limited estate).

16 There exists a gray area, however, where a debtor is solvent enough to pay in full all allowed claims, but the surplus is not enough to cover all creditors' otherwise disallowed interest. In such a case, legitimate bankruptcy interests may well warrant a more nuanced application of the solvent-debtor exception. *See* Scott C. Shelley & Solomon J. Noh, *Show Me the Money: Another Look at Postpetition Interest in Solvent Debtor Chapter 11 Cases*, 24 Emory Bankr. Dev. J. 361, 370–71 (2008). But that situation is not present here, so we need not address it.

17 *See also* *In re Ancona*, No. 14-10532, 2016 WL 828099, at *6 (Bankr. S.D.N.Y. Mar. 2, 2016) (rejecting "the proposition that a court must first find a debtor to be insolvent or determine all other claims against a debtor before analyzing a [§ 502(b)(6)] claim"); *In re Flanigan*, 374 B.R. 568, 575 (Bankr. W.D. Pa. 2007) (same); *In re Farley, Inc.*, 146 B.R. 739, 747–48 (Bankr. N.D. Ill. 1992) (same); *In re Federated Dep't Stores, Inc.*, 131 B.R. 808, 817 (S.D. Ohio 1991) (same); *In re PPI Enters. (U.S.), Inc.*, 228 B.R. 339, 345–46 (Bankr. D. Del. 1998); *HSBC Bank USA, Nat'l Ass'n v. Calpine Corp.*, No. 07-CIV-3088, 2010 WL 3835200, at *5, *10 (S.D.N.Y. Sept. 15, 2010) (applying § 502(b)(2) in a "very solvent" debtor case).

18 *See also, e.g.,* *Brown v. Leo*, 34 F.2d 127, 127 (2d Cir. 1929) (recognizing that § 63 of the 1898 Bankruptcy Act fixes "the time when interest stops ... as the date of the filing of the petition," but noting that the estate at issue there was solvent, so "neither the rule nor the reason for stopping interest at the date of the filing of the petition applies"); *Sword Line, Inc. v. Indus. Comm'r of N.Y.*, 212 F.2d 865, 870 (2d Cir. 1954) ("[I]nterest ceases upon bankruptcy in the general and usual instances noted ... unless the bankruptcy bar proves eventually nonexistent by reason of the actual solvency of the debtor."); *Littleton v. Kincaid*, 179 F.2d 848, 852 (4th Cir. 1950) ("[W]hen this unusual event [*i.e.*, debtor solvency in bankruptcy] occurs interest is payable out of this surplus to the date of payment."); *In re Magnus Harmonica Corp.*, 159 F. Supp. 778, 780 (D.N.J. 1958) (enumerating as an explicit, judicially devised exception to § 63 of the Bankruptcy Act that "[w]here the estate of the debtor is sufficient to pay all of his debts, including interest, interest may be allowed to the date of payment"), *aff'd*, 262 F.2d 515 (3d Cir. 1959); *In re Int'l Hydro-Elec. Sys.*, 101 F. Supp. 222, 224 (D. Mass. 1951) (holding a debtor's solvency dispositive in awarding creditors contractual default-rate interest).

19 We have followed the Supreme Court's lead and held similarly. *See* *In re Bodenheimer, Jones, Szwak, & Winchell L.L.P.*, 592 F.3d 664, 673–74 (5th Cir. 2009) (stating the rule that pre-Code bankruptcy doctrines "remain controlling unless *explicitly* superseded" (emphasis added)); *In re Laymon*, 958 F.2d 72, 74–75 (5th Cir. 1992) (similar). These precedents also bind us.

20 The Chandler Act reenacted this provision verbatim.

21 For this reason, this is not a case in which "the language of the Code leaves no room for clarification by pre-Code practice." *Hartford Underwriters Ins. Co. v. Union Planters Bank, N.A.*, 530 U.S. 1, 11, 120 S.Ct. 1942, 147 L.Ed.2d 1 (2000). This is not a case in which pre-Code practice *comported* with prior acts' text or clarified an open-ended ambiguity therein; this is a case involving a plain judicial *exception* to the prior acts. *Cf.* *id.* at 9–11, 120 S.Ct. 1942. Because Congress was not writing upon a clean slate, we are to assume that the legislature was aware of courts' equitable exception to the prior acts' text. Had Congress intended to do away with this practice, it would have said so directly.

22 Discussing *Johnson*, the bankruptcy court persuasively observed that unchanged "[e]quitable considerations support the solvent-debtor exception." *Ultra*, 624 B.R. at 198. "There is no reason why Congress would

allow solvent debtors to wield bankruptcy as a sword to slash valid debts"—an "observation [that] applies as persuasively to Congress['s] deliberation of the Bankruptcy Code as it did to deliberations of the Bankruptcy Act." *Id.* at 199.

23 Ultra also argues that the Code's reticulated scheme already contemplates solvent-debtor scenarios but declines to embrace the full scope of the traditional solvent-debtor exception. This, we are told, gives rise to the negative implication that Congress did not intend the broad solvent-debtor exception to survive the Code's enactment. Specifically, because the Code provides that impaired creditors of solvent debtors are to receive interest at least "at the legal rate" under the best-interests-of-creditors test, *see* 11 U.S.C. §§ 726(a)(5), 1129(a)(7)(A)(ii), we are to infer that Congress intended to abrogate the traditional solvent-debtor exception and replace it with a narrower version that requires payment of post-petition interest only at the Federal Judgment Rate. Thus, Ultra tells us, we should not overstep Congress's specific instructions and apply the solvent-debtor exception to award default-rate contractual interest, despite Ultra's solvency.

We are not persuaded. Sections 726(a)(5) and 1129(a)(7)(A)(ii) do not *unambiguously* abrogate or constrict the traditional solvent-debtor exception. Indeed, authorizing "[post-petition] interest at the legal rate ... *on any claim*" in solvent-debtor cases does not constitute any sort of exception to the Code's disallowance of "unmatured interest" as *part of a claim, see* *id.* § 726(a)(5) (emphasis added), § 502(b)(2), so those provisions cannot be said to supplant the traditional solvent-debtor exception. If anything, § 726(a)(5) arguably *expands* the scope of the traditional English solvent-debtor exception, which seems to have allowed for ongoing interest just *as part of* (rather than "on") creditors' claims in solvent-debtor scenarios. *See, e.g., Rooke*, 26 Eng. Rep. at 157; *Marlar*, 26 Eng. Rep. at 98; *supra* n.13 and accompanying text.

24 The bankruptcy court's first opinion in this case also provides a nice illustration that mathematically demonstrates how charging default-rate interest on the unpaid Make-Whole Amount does not result in any double recovery. *Ultra*, 575 B.R. at 371–72.

25 Recall that the difference is rather material: the applicable Federal Judgment Rate would be only 54 basis points; the contractual default rate, meanwhile, would be *the greater* of 2% *over* either of two benchmark rates. *See supra* note 2.

26 Still, one might well wonder why Congress did not simply cross-reference the statutory provision designating the Federal Judgment Rate, 28 U.S.C. § 1961, if indeed it meant for that to be that single rate applied. Indeed, in antitrust legislation passed just a few years after the Bankruptcy Code's enactment, Congress did just that. *See* Pub. L. No. 98-462, § 4(a), 98 Stat. 1815 (1984) (providing for "interest calculated at the rate specified in section 1961 of title 28, United States Code"); *see also, e.g.*, 28 U.S.C. § 2412(f) ("[I]nterest shall be computed at the rate determined under section 1961(a) of this title ...."); 15 U.S.C. § 4303(a)–(c) (similar).

27 This is consistent with our prior holding that the Code's disallowance provisions do not operate to "impair" creditors. *Ultra*, 943 F.3d at 765. Section 502(b)(2) operates to disallow "unmatured interest" that is *part of* a claim—not interest *on* a claim, which is what the contractual default rates here specify. A broader reading of § 502(b)(2) to disallow *all* post-petition interest, whether as *part of* a claim or *on* a claim, would plainly conflict with § 1129(a)(7)(A)(ii) and § 726(a)(5), which expressly operate to *allow* post-petition interest *on* claims.

28 *See also* *Ultra*, 624 B.R. at 203 ("The solvent-debtor exception has existed throughout the history of bankruptcy law and § 1124 provides a means to implement the exception within the plan confirmation framework of the Bankruptcy Code.").

1 The other side of the coin: If the Code is *not* unmistakably clear, then the prior practice survives. *See ante*, at 154 (discussing and collecting cases). That proposition is orthogonal to my argument because, of course, I think the Code *is* unmistakably clear.

2 The clause "or with a rebate of interest upon such as were not then payable and did not bear interest" is not a standalone bar on unmatured interest. That's because its "rebate" applies only to "interest upon such [claims] *as were not then payable* and did not bear interest." (Emphasis added.) That means the rebate doesn't apply to unmatured interest on claims that *were* payable at the time of filing. That is, it could be that the *claim itself* was payable at the time of filing and yet the interest didn't mature until after filing. The rebate clause doesn't say anything about that kind of unmatured interest.

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55 F.4th 377
United States Court of Appeals, Second Circuit.

IN RE: LATAM AIRLINES GROUP S.A., Debtor.
TLA Claimholders Group, Appellant,
v.
LATAM Airlines Group S.A., Debtor-Appellee,
Parent Ad Hoc Claimant Group, Banco del Estado de Chile, Official Committee of Unsecured Creditors, Ad Hoc Group of LATAM Bondholders, Intervenors-Appellees.

Docket No. 22-1940
|
August Term, 2022
|
Argued: October 12, 2022
|
Decided: December 14, 2022

Synopsis

Background: Unsecured creditors objected to confirmation of Chapter 11 plan of reorganization which classified them as unimpaired and did not provide for payment of postpetition interest to which they would have been entitled in the absence of any bankruptcy proceeding. The United States Bankruptcy Court for the Southern District of New York, James L. Garrity, Jr., J., 2022 WL 2206829 and 2022 WL 2541298, confirmed plan and, following unsecured creditors' appeal, denied stay pending appeal, 2022 WL 2657345, as well as motion to certify appeal, 2022 WL 2962948. The District Court, Denise L. Cote, J., 643 B.R. 741, affirmed. Unsecured creditors appealed.

Holdings: The Court of Appeals, Leval, Circuit Judge, held that:

as a matter of first impression for the court, a claim is "**impaired**" within the meaning of the Bankruptcy Code only when the plan of reorganization, rather than the Code, alters the creditor's legal, equitable, or contractual rights;

unsecured creditors' claims were not "**impaired**" simply because they did not receive postpetition interest;

as a matter of first impression for the court, the judicially-created solvent-debtor exception survived enactment of the Code; and

the Bankruptcy Court did not err in finding that debtor-affiliate was insolvent.

Affirmed.

See also 643 B.R. 756.

Procedural Posture(s): On Appeal; Objection to Confirmation of Plan.

***379** Appeal from an order of the United States District Court for the Southern District of New York (Denise L. Cote, *Judge*)

Attorneys and Law Firms

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Before: Leval, Chin, and Lee, Circuit Judges.

Opinion

LEVAL, Circuit Judge:

***380** The TLA Claimholders, who assert unsecured claims against Tam Linhas Aéreas S.A. ("TLA"), an affiliate of LATAM Airlines Group S.A. ("LATAM"), a large South American airline holding company, appeal from an August 31, 2022 order of the United States District Court for the Southern District of New York (Denise L. Cote, *Judge*), affirming a June 18, 2022 order of the United States Bankruptcy Court for the Southern District of New York (James L. Garrity, Jr., *Bankruptcy Judge*), confirming LATAM's reorganization plan.

The plan of reorganization provides that the Appellants' claims will be paid in full, except for any post-petition interest. The Bankruptcy Court determined that such treatment rendered the claims unimpaired under Section 1124(1) of the Bankruptcy Code, because Section 502(b)(2) of the Code provides that "unmatured interest" may be excluded from a claim. 11 U.S.C. §§ 502(b)(2), 1124(1). It also determined that the affiliate, TLA, was insolvent, so that the solvent-debtor exception—an equitable doctrine permitting the payment of post-petition interest by a solvent debtor in limited circumstances—did not apply.

On appeal, the TLA Claimholders contend that, unless they receive post-petition interest, their claims are "impaired" under Section 1124(1). They also argue that TLA is solvent and that its solvency makes the solvent debtor exception applicable. They further contend that the Bankruptcy Court's test for assessing solvency was legally flawed.

We hold that (1) a claim is not impaired under 11 U.S.C. § 1124(1) when it is altered by operation of the Bankruptcy Code, and (2) the Bankruptcy Court did not err in its assessment of TLA's solvency. Accordingly, we **AFFIRM**.

BACKGROUND

LATAM is a holding company, which owns numerous South American airlines. TLA, a Brazilian airline, is a subsidiary of LATAM.

***381** On May 26, 2020, LATAM and several of its affiliates filed for Chapter 11 bankruptcy protection in the U.S. Bankruptcy Court for the Southern District of New York. On July 9, 2020, TLA filed its own Chapter 11 voluntary petition. Pursuant to Fed. R. Bankr. P. 1015(b), the Bankruptcy Court procedurally consolidated LATAM's case with those of its affiliates, including TLA. We refer to LATAM, TLA, and the other affiliated businesses as the Debtors.

The Debtors proposed a plan of reorganization in late 2021 (the "Plan"). The Plan depends on raising $5.442 billion through a new equity offering in Chile (the "Chilean Offering"). To ensure that sufficient funds are raised through the Chilean Offering, several large claimholders and a group of LATAM's largest shareholders have committed to purchase up to $5.4 billion of shares.

Consistent with 11 U.S.C. § 1123, the Plan divided claims into different classes and designated each class as impaired or unimpaired. Class 6 contains all general unsecured claims against LATAM's affiliates, with limited exceptions not relevant here. The Plan designates this class as unimpaired. Unless members of Class 6 consent to other treatment, they will receive the full "allowed" value of their claim, *i.e.*, the amount recoverable under the Bankruptcy Code, or whatever other treatment is necessary to render the claims unimpaired. S. App'x at 96.

The TLA Claimholders assert unsecured claims against TLA, based on several debt instruments governed by Brazilian law. It is undisputed that TLA defaulted on these instruments, and that in the absence of any bankruptcy proceeding, the Claimholders would be entitled to substantial interest. Under the Plan, the Claimholders are classified as members of Class 6 and receive the full allowed amount of their claims: about $300 million. The Plan does not provide for a further $150 million of post-petition interest.

The Claimholders objected to confirmation, arguing that they could not be classified as unimpaired if they did not receive such postpetition interest. In support of this position, they cited the text of Section 1124(1) and the solvent-debtor exception. To demonstrate that TLA was solvent, the Claimholders submitted two analyses. The first, the "Waterfall Analysis," used figures submitted by the Debtors in support of a settlement made as part of the bankruptcy proceedings (the "Settlement Figures").[1] The Settlement Figures estimated LATAM's going-concern value, assuming that the Plan was confirmed and LATAM received a capital infusion through the Chilean Offering. These figures estimated the consolidated value of the debtors to be $14 billion, with about $3.446 billion of that value attributable to TLA. The Settlement Figures also identified about $1.080 billion worth of liabilities as associated with TLA, although other estimates proffered by the Debtors showed higher amounts of liabilities. The TLA Claimholders' expert took the Settlement Figures and subtracted TLA's share of the estimated liabilities from its share of the estimated overall value, yielding a surplus of $2.336 billion.

The Claimholders' second analysis, the "Discounted Cash Flow Analysis," assessed TLA's value as a going concern based on the present value of its future cash flow. Both the Discounted Cash Flow ***382** Analysis and the Waterfall Analysis supported the view that TLA was solvent.

The Debtors opposed the objection and submitted two additional analyses of TLA's solvency. The first, the "Liquidation Analysis," compared the amount that TLA would obtain through sales of its assets against the amount of its liabilities. This analysis estimated the amount that could be obtained through quick, foreclosure style-sales, as well as through sales occurring over an eighteen-month period. The second, the "Balance Sheet Test," compared the book value of TLA's assets against the book value of its liabilities. Both analyses submitted by the Debtors indicated that TLA was insolvent.

The Debtors also criticized the Claimholders' methodology, arguing that it was improper to use the Settlement Figures in this context. They also argued that both analyses understated TLA's liabilities by a significant amount.

The Bankruptcy Court agreed with the Debtors, rejected the Claimholders' objection, and confirmed the Plan. *See generally* *In re LATAM Airlines Grp. S.A.*, No. 20-11254 (JLG), 2022 WL 2206829 (Bankr. S.D.N.Y. June 18, 2022), *as amended*, 2022 WL 2541298 (Bankr. S.D.N.Y. July 7, 2022) ("*LATAM I*").

First, the Bankruptcy Court held that **Section 1124**(**1**) did not speak to post-petition interest and thus did not supersede the limitation on post-petition interest contained in **Section** 502(b)(2). Second, it determined that TLA was insolvent, so that the solvent-debtor exception did not apply. Specifically, the Bankruptcy Court found that the analyses submitted by the Debtors were credible, supported by evidence, and consistent with the statutory definition of "insolvent," *i.e.*, that "the sum of such entity's debts is greater than all of such entity's property, at a fair valuation." 11 U.S.C. **§** 101(32)(A).

As to the Waterfall Analysis and the Discounted Cash Flow Analysis, the Bankruptcy Court found that neither comported with **Section** 101(32). As to the Waterfall Analysis, the Bankruptcy Court agreed with the Debtors that it significantly understated TLA's liabilities. The Bankruptcy Court concluded that when the corrected figure was used, the Waterfall Analysis also demonstrated that TLA was insolvent. As to the Discounted Cash Flow Analysis, the Bankruptcy Court determined that it was too speculative to support a finding of solvency.

The District Court affirmed. *In re LATAM Airlines Grp. S.A.*, 643 B.R. 741 (S.D.N.Y. 2022) ("*LATAM II*"). The TLA Claimholders then appealed to this Court.

STANDARD OF REVIEW

"In an appeal from a district court's review of a decision of a bankruptcy court, we conduct an independent and plenary review of the bankruptcy court's decision, accepting the bankruptcy court's findings of fact unless they are clearly erroneous and reviewing its conclusions of law de novo." *In re Teligent, Inc.*, 640 F.3d 53, 57 (2d Cir. 2011).

DISCUSSION

A. Applicable Law

(i) The Rule Against Post-Petition Interest and the Solvent-Debtor Exception

Before the Bankruptcy Code was enacted in 1978, the Supreme Court recognized a "general rule" in bankruptcy: "interest on the debtors' obligations ceases to accrue at the beginning of proceedings." *Vanston Bondholders Protective Comm. v. Green*, 329 U.S. 156, 163, 67 S.Ct. 237, 91 L.Ed. 162 (1946). The Court also recognized that English courts had developed an exception ***383** to this rule: "if the alleged 'bankrupt' proved solvent, creditors received post-bankruptcy interest before any surplus reverted to the debtor." *City of New York v. Saper*, 336 U.S. 328, 330 n.7, 69 S.Ct. 554, 93 L.Ed. 710 (1949) (collecting English authorities). Like other circuit courts, we applied this "solvent-debtor" exception in cases arising under pre-Code bankruptcy laws. *See, e.g.*, *Ruskin v. Griffiths*, 269 F.2d 827, 831 (2d Cir. 1959); *see also* *Debentureholders Protective Comm. of Cont'l Inv. Corp. v. Cont'l Inv. Corp.*, 679 F.2d 264, 269 (1st

Cir. 1982); *In re Beverly Hills Bancorp*, 752 F.2d 1334, 1339 (9th Cir. 1984).

Under the Bankruptcy Code, the rule against post-petition interest is codified at 11 U.S.C. § 502(b)(2). *See United Sav. Ass'n of Texas v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 372-73, 108 S.Ct. 626, 98 L.Ed.2d 740 (1988). Section 502 defines what portions of a claim may be "allowed," *i.e.*, recoverable in bankruptcy. 11 U.S.C. § 502(a). It contains several specific limitations, including that an allowed claim cannot include "unmatured interest." 11 U.S.C. § 502(b)(2).

We have not yet addressed whether the solvent-debtor exception survived the enactment of the Code. The Fifth and Ninth Circuits have recently concluded that it did. *See In re Ultra Petroleum Corp.*, 51 F.4th 138, 156 (5th Cir. 2022) ("*Ultra Petroleum II*"); *In re PG&E Corp.*, 46 F.4th 1047, 1061 (9th Cir. 2022).

(ii) Impairment Under Chapter 11

"A Chapter 11 bankruptcy is implemented according to a 'plan,' typically proposed by the debtor, which divides claims against the debtor into separate 'classes' and specifies the treatment each class will receive." *RadLAX Gateway Hotel, LLC v. Amalgamated Bank*, 566 U.S. 639, 641, 132 S.Ct. 2065, 182 L.Ed.2d 967 (2012) (citing 11 U.S.C. § 1123). The plan must designate each class as impaired or not impaired. *See* 11 U.S.C. §§ 1123(a)(2)–(3). Classes with "impaired" claims may vote to accept or reject the plan. *See* 11 U.S.C. §§ 1126, 1129(a)(8). If a class of impaired creditors dissents, the debtor must resort to the "cramdown" process for the plan to be confirmed. *See Bank of America Nat'l Tr. and Sav. Ass'n v. 203 North LaSalle St. P'ship*, 526 U.S. 434, 441, 119 S.Ct. 1411, 143 L.Ed.2d 607 (1999). An unimpaired class is "conclusively presumed to have accepted the plan" and thus gets no vote. 11 U.S.C. § 1126(f).

Section 1124 of the Bankruptcy Code determines when a claim is impaired. It provides that:

> [A] class of claims or interests is impaired under a plan unless, with respect to each claim or interest of such class, the plan—
>
> (1) leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest; or
>
> (2) notwithstanding any contractual provision or applicable law that entitles the holder of such claim or interest to demand or receive accelerated payment of such claim or interest after the occurrence of a default—
>
> (A) cures any such default that occurred before or after the commencement of the case under this title, other than a default of a kind specified in section 365(b)(2) of this title or of a kind that section 365(b)(2) expressly does not require to be cured;
>
> (B) reinstates the maturity of such claim or interest as such maturity existed before such default;
>
> (C) compensates the holder of such claim or interest for any damages ***384** incurred as a result of any reasonable reliance by such holder on such contractual provision or such applicable law;
>
> (D) if such claim or such interest arises from any failure to perform a nonmonetary obligation, other than a default arising from failure to operate a nonresidential real property lease subject to section 365(b)(1)(A), compensates the holder of such claim or such interest (other than the debtor or an insider) for any actual pecuniary loss incurred by such holder as a result of such failure; and
>
> (E) does not otherwise alter the legal, equitable, or contractual rights to which such claim or interest entitles the holder of such claim or interest.

11 U.S.C. § 1124.

B. Application

(i) Whether Section 1124(1) Requires the Payment of Post-Petition Interest to Render a Claim Unimpaired

The TLA Claimholders first argue that to be unimpaired under Section 1124(1) of the Bankruptcy Code, a creditor must receive postpetition interest on its claim, regardless of the debtor's solvency. [2]

We have stated that Section 1124(1) "define[s] impairment in the broadest possible terms," so that "any change in legal, equitable or contractual rights creates impairment." In re Taddeo, 685 F.2d 24, 28 (2d Cir. 1982). Although other circuits agree that Section 1124(1) sweeps broadly, [3] the Third, Fifth, and Ninth Circuits have noted a significant caveat: Because Section 1124(1) refers to impairment imposed by a "plan," these circuits have held it inapplicable to modifications which occur by operation of the Code. "In other words, a creditor's claim outside of bankruptcy is not the relevant barometer for impairment; [courts] must examine whether the plan itself is a source of limitation on a creditor's legal, equitable, or contractual rights." *PPI Enters.*, 324 F.3d at 204. *See also* *In re Ultra Petroleum Corp.*, 943 F.3d 758, 763 (5th Cir. 2019) ("*Ultra Petroleum I*") ("The plain text of § 1124(1) requires that '*the plan*' do the altering. We therefore hold a creditor is impaired under § 1124(1) only if 'the plan' itself alters a claimant's 'legal, equitable, [or] contractual rights.' " (alteration in original)); *PG&E*, 46 F.4th at 1063 n.11 ("[A]n alteration of pre-bankruptcy rights that occurs by operation of the Code does not result in impairment.").

We find these authorities persuasive. We therefore join the Third, Fifth, and Ninth Circuits and hold that a claim is impaired under Section 1124(1) only when the plan of reorganization, rather than the ***385** Code, alters the creditor's legal, equitable, or contractual rights. [4]

Under this interpretation of Section 1124(1), Appellants' claims are not impaired simply because they did not receive post-petition interest. Although they had a contractual right to such interest, "this contractual right, as applied to postpetition debts, was superseded by the Code—specifically, by § 502(b)(2)'s prohibition on the inclusion of 'unmatured interest' as part of a claim." *PG&E*, 46 F.4th at 1063 (citing *Ultra Petroleum I*, 943 F.3d at 763); *see also* *PPI Enters.*, 324 F.3d at 205 ("Because the Bankruptcy Code, not the Plan, is the only source of limitation on those rights here, [the creditor's] claim is not impaired under § 1124(1)."). This determination does not necessarily mean that Appellants' claims are unimpaired; we must still determine whether they have any "equitable" right to post-petition interest under the solvent-debtor exception, which Section 1124(1) would protect. *See* *PG&E*, 46 F.4th at 1064; *Ultra Petroleum I*, 943 F.3d at 765-66. However, we reject the argument that post-petition interest must be paid regardless of solvency.

The TLA Claimholders raise three further objections to this conclusion. We find each unpersuasive.

First, they argue that because Section 1124(1) refers to "claims" rather than "allowed claims," Section 502(b)(2)'s limitation on postpetition interest does not apply. We agree with the Fifth Circuit that the "broader statutory context" undermines this argument. *Ultra Petroleum I*, 943 F.3d at 764. Section 1124(1) does not state that the "claims" themselves will be left unaltered; instead, it protects "the legal, equitable, and contractual *rights* to which such claim or interest entitles the holder of such claim or interest." 11 U.S.C. § 1124(1) (emphasis added). Thus, "we judge impairment after considering everything that defines the scope of the right or entitlement," including the Bankruptcy Code. *Ultra Petroleum I*, 943 F.3d at 764. The Third Circuit agrees that the language of Section 1124(1) "does not address a creditor's claim 'under nonbankruptcy law,' and that its use of the present-tense suggests a creditor's rights must be ascertained with regard to applicable statutes[.]" *PPI*, 324 F.3d at 204 (quotation marks omitted).

Second, the TLA Claimholders point to Section 1124(2), the "cure" provision. This subsection applies where the creditor has a right to "demand or receive accelerated payment ... after the occurrence of a default." 11 U.S.C. § 1124(2). It permits the debtor to treat the defaulted claim as unimpaired without providing that accelerated payment, so long as other conditions ***386** are satisfied: the creditor must cure the default, reinstate the maturity of the claim, and compensate the creditor for damages resulting from reliance on the prospect of receiving accelerated payment. *See* 11 U.S.C. §§ 1124(2)(A)–(C). The Claimholders correctly note that courts considering Section 1124(2) have required debtors to pay post-petition interest to render a claim unimpaired. However, each case identified by the Claimholders reasoned that the right to postpetition interest in a Section 1124(2) case follows from 11 U.S.C. § 1123(d), which provides how much must be paid to cure a default. [5] Unlike Section 1124(1), which, as discussed above, refers to all applicable law, including the Code, Section 1123(d) provides that the amount necessary to cure a default shall be determined by "applicable nonbankruptcy law." Because Section 1124(1) does not refer to cure and reinstatement, we find no guidance in these authorities considering the interaction of **Sections** 1124(2) and 1123(d).

Third, the TLA Claimholders make an argument from statutory history. Prior to 1994, **Section** 1124(3) permitted a debtor to render a claim "unimpaired" by paying the allowed amount of a claim in cash. *See* 11 U.S.C. **§** 1124(3) (1992). It is not disputed that this subsection would have also permitted the Debtors to treat the claims of TLA Claimholders as unimpaired without post-petition interest. The Claimholders thus argue that, for the repeal of **Section** 1124(3) to have had any meaning, **Section 1124**(**1**) cannot be read to authorize treating claims as unimpaired when excluding post-petition interest.

We are not convinced that the 1994 repeal can be given such sweeping effect. The Supreme Court "has been reluctant to accept arguments that would interpret the Code, however vague the particular language under consideration might be, to effect a major change in pre-Code practice that is not the subject of at least some discussion in the legislative history." *Dewsnup v. Timm*, 502 U.S. 410, 419, 112 S.Ct. 773, 116 L.Ed.2d 903 (1992). While the TLA Claimholders' proposed interpretation would nullify the longstanding rule barring post-petition interest, the legislative history regarding the 1994 repeal demonstrates more modest intentions. That history shows that Congress acted in response to *In re New Valley Corp.*, 168 B.R. 73 (Bankr. D.N.J. 1994). *See* H.R. Rep. No. 103-835, **§** 214 at 47–48 (1994); *see also* *PG&E*, 46 F.4th at 1060, 1062 (discussing legislative history). In *New Valley*, a solvent debtor argued that it need not pay post-petition interest to unsecured creditors to render them unimpaired, relying on **Sections** 502(b)(2) and 1124(3). *See* 168 B.R. at 75-76. The bankruptcy court agreed, ruling that "a plain reading of the pertinent Bankruptcy Code **sections** demonstrates that in a Chapter 11 context solvency alone is an insufficient basis to require payment of postpetition interest to unsecured creditors." *Id.* at 77. ***387** The House Report explained that the repeal of **Section** 1124(3) was meant to prohibit this outcome, describing *New Valley* as an "unfair result." H.R. Rep. No. 103-835, **§** 214 at 48.

Based on this legislative history, the Fifth Circuit has held that, in repealing **Section** 1124(3), Congress meant only to ensure that solvent debtors pay post-petition interest on their claims. *See* *Ultra Petroleum I*, 943 F.3d at 764-65. The Third and Ninth Circuits have likewise described **Section** 1124(3)'**s** repeal as targeted at the "anomalous result" created by the *New Valley* decision. *PPI Enters.*, 324 F.3d at 206-07; *see* *PG&E*, 46 F.4th at 1060 (emphasizing that the *New Valley* repeal applies to "creditors of a solvent debtor"). We agree with this interpretation.

The TLA Claimholders argue that these decisions are wrong, and that we should instead follow the approach taken by several bankruptcy courts. *See* *In re Seasons Apartments, Ltd. P'ship*, 215 B.R. 953, 960 (Bankr. W.D. La. 1997); *In re Atlanta-Stewart Partners*, 193 B.R. 79, 81–82 (Bankr. N.D. Ga. 1996). These courts have reasoned that, even though Congress may have been spurred to action by the *New Valley* decision, the repeal of **Section** 1124(3) applies to all debtors. They base this conclusion on **Section** 1124'**s** purported failure to distinguish between solvent and insolvent debtors. *See* *Seasons Apartments*, 215 B.R. at 960; *Atlanta-Stewart*, 193 B.R. at 82.

We are not persuaded. Although **Section 1124**(**1**) does not expressly refer to solvency, it does protect a creditor's "equitable rights." That includes whatever survives of the solvent-debtor exception. *See* *PG&E*, 46 F.4th at 1060 ("While, as discussed, no Code provision legally entitles supposedly unimpaired creditors to postpetition interest, pre-Code practice conclusively establishes creditors' equitable entitlement to contractual postpetition interest when a debtor is solvent, subject to any other countervailing equities."). So interpreted, **Section 1124**(**1**) does distinguish between solvent and insolvent debtors. The textual hurdle identified by the *Seasons Apartments* and *Atlanta-Stewart* courts thus does not foreclose our interpretation. We therefore do not believe that the repeal of **Section** 1124(3) carries the weight the TLA Claimholders ascribe to it.

(ii) Whether the Solvent-Debtor Exception Was Satisfied

The Claimholders also raise two legal objections to the Bankruptcy Court's solvency analysis.[6] First, they argue that the solvent-debtor exception arises from the absolute priority rule, a doctrine which forbids a debtor's equity holders from recovering value from the estate before all creditors are paid. *See* *In re DBSD N. Am., Inc.*, 634 F.3d 79, 94 (2d Cir. 2011). Thus, the solvent-debtor exception is triggered—and creditors must receive post-petition interest—whenever a plan will return value to equity.

Second, the Claimholders argue that the Bankruptcy Court should have looked to a discounted cash-flow analysis to assess solvency. They primarily rely on *Consolidated Rock Products Company v. Du Bois*, 312 U.S. 510, 520, 61 S.Ct. 675, 85 L.Ed. 982 (1941), in which the Supreme Court held that a plan of reorganization could not be confirmed under the 1898 Bankruptcy Act. [7] The barriers to confirmation included the lower court's failure "to value the whole enterprise by a capitalization of prospective ***388** earnings." *Id.* at 525, 61 S.Ct. 675. The Court further explained that "[f]indings as to the earning capacity of an enterprise are essential to a determination of the feasibility as well as the fairness of a plan of reorganization." *Id.*

Although raised as a separate objection, the *Consolidated Rock* argument also follows from the absolute priority rule. The reason a prospective earnings analysis was "essential," as Justice Douglas explained, was to ensure that "indefensible participation of junior securities in plans of reorganization" did not result. *Id.* at 525-26, 61 S.Ct. 675; *see also* John D. Ayer, *Rethinking Absolute Priority After Ahlers*, 87 Mich. L. Rev. 963, 975–76 (1989). Thus, to the extent the Claimholders argue that *Consolidated Rock* requires a prospective earnings analysis in this context, such a requirement likewise follows from the common-law absolute priority rule. *See* Appellant's Br. at 65; Reply Br. at 21. We therefore consider these objections together.

As we have explained, the Code's treatment of absolute priority "is so different from the prior Bankruptcy Act that the old practice simply cannot be imported *in toto* into practice under the new Code." *In re Coltex Loop Cent. Three Partners, L.P.*, 138 F.3d 39, 43 (2d Cir. 1998); *accord* *203 North Lasalle*, 526 U.S. at 448, 119 S.Ct. 1411 ("[T]he Code does not codify any authoritative pre-Code version of the absolute priority rule."). Accordingly, even assuming the TLA Claimholders correctly describe the solvent-debtor exception's relationship to the common-law absolute priority rule, [8] we cannot assume that the Code guarantees the same result.

Under the Code, the absolute priority rule comes into effect only when a class of **impaired** creditors votes to reject a plan, and the debtor resorts to the "cramdown" procedure. *DBSD*, 634 F.3d at 105. For unsecured creditors such as the TLA Claimholders, the absolute priority rule is codified at **Section** 1129(b)(2)(B). The plan must satisfy one of two conditions:

> (i) the plan provides that each holder of a claim of such class receive or retain on account of such claim property of a value, as of the effective date of the plan, equal to the allowed amount of such claim; or
>
> (ii) the holder of any claim or interest that is junior to the claims of such class will not receive or retain under the plan on account of such junior claim or interest any property ....

11 U.S.C. §§ 1129(b)(2)(B)(i)–(ii).

Under the statute, unsecured creditors such as the Claimholders—who ***389** will be paid the full allowed amount of their claim—cannot insist on compliance with the absolute priority rule. Because such a plan satisfies **Section** 1129(b)(2)(B)(i), there is no need for it to satisfy **Section** 1129(b)(2)(B)(ii). *Cf.* *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 201 n.1, 108 S.Ct. 963, 99 L.Ed.2d 169 (1988).

The Claimholders' understanding of the solvent-debtor exception is not consistent with this statutory scheme. Under their interpretation, they are effectively entitled to insist on compliance with the absolute priority rule, unless they are paid more than what they could recover under full compliance with the rule as codified. [9] Appellant's Br. at 40; Ad Hoc Claimant Brief at 14. We therefore do not believe that the absolute priority rule provides the relevant test for solvency. We accordingly reject the argument that the Bankruptcy Court was required, as a matter of law, to apply the solvent debtor exception under these circumstances. We likewise reject the contention that the Bankruptcy Court was required to credit the Discounted Cash Flow Analysis because of *Consolidated Rock*'**s** gloss on the absolute priority rule.

The Claimholders do not identify any other rule of law which would require the Bankruptcy Court to rule that the solvent-debtor exception applied. We have held that bankruptcy courts have "broad discretion when considering evidence to support a finding of insolvency." *In re Roblin Indus., Inc.*, 78 F.3d 30, 35 (2d Cir. 1996). The district court did not abuse that discretion in determining that the Debtors' analyses and the corrected Waterfall Analysis were more probative on the question of TLA's solvency than the Discounted Cash Flow Analysis. We accordingly affirm the Bankruptcy Court's finding that TLA was insolvent. [10]

CONCLUSION

We have considered the TLA Claimholders' remaining arguments and determined that they are without merit. In sum, we hold that: 1) a claim is not "**impaired**" under 11 U.S.C. § **1124**(**1**) unless the plan, rather than other provisions of the Bankruptcy Code, alters the claim, and 2) the Bankruptcy Court did not err in its assessment of TLA's solvency. We therefore **AFFIRM**.

All Citations

55 F.4th 377

Footnotes

1 The settlement pertains to the treatment of Class 4 claims, which are based on LATAM's 2024 and 2026 bonds. Class 4 claimholders will receive, in cash, the full allowed amount of their claim. The Debtors proffered the Settlement Figures to show that, with the infusion of funds from the Chilean Offering, LATAM would be able to pay the Class 4 claims and continue as a going concern.

2 The District Court held that this argument had not been raised in the Bankruptcy Court and was therefore forfeited. Based on our review of the transcript of the confirmation hearing and the TLA Claimholders' demonstrative slides, we find that the argument was raised before the Bankruptcy Court. In any event, we may exercise our discretion to consider the issue on appeal. *See* *In re Nortel Networks Corp.* ***Sec****. Litig.*, 539 F.3d 129, 133 (2d Cir. 2008) ("[O]ur waiver doctrine is entirely prudential.").

3 *See, e.g.*, *In re PPI Enters. (U.S.), Inc.*, 324 F.3d 197, 202 (3d Cir. 2003) ("If the debtor's Chapter 11 reorganization plan does not leave the creditor's rights entirely 'unaltered,' the creditor's claim will be labeled as **impaired** under **§** **1124**(**1**) of the Bankruptcy Code."); *In re L&J Anaheim Assocs.*, 995 F.2d 940, 942 (9th Cir. 1993) (adopting *Taddeo*'s formulation).

4 The TLA Claimholders argue that we should instead follow *In re Monclova Care Center, Inc.*, 59 F. App'x 660, 664 (6th Cir. 2003), where the Sixth Circuit determined that the Internal Revenue Service's ("IRS") claim against a debtor would be **impaired** under **Section** **1124**(**1**) unless the IRS received postpetition interest. We do not regard *Monclova* as persuasive authority for two reasons. First, unlike the disputed interest here, the IRS's right to interest in *Monclova* is conferred by federal statute. *Id.* at 663 (citing 26 U.S.C. §§ 6601(a), (e), 6621, 6622). Second, in reaching its conclusion that the IRS is owed postpetition interest, the Sixth Circuit treated the dispute as concerning the language of a bankruptcy plan, rather than the Code. *Id.* at 663-64. Although the definitions given in the plan tracked those in the Code, the Sixth Circuit did not appear to treat the dispute as an issue of law subject to de novo review, and instead stated that it gave "full deference" to the bankruptcy court's "reasonabl[e]" interpretation of the plan in favor of the IRS. *Id.* at

661, 662, 664. We are thus uncertain whether the Sixth Circuit definitively adopted an interpretation of the Code contrary to the one held by the Third, Fifth, and Ninth Circuits, and which we adopt today. For these reasons, we do not rely on *Monclova*.

5 *See, e.g.*, *In re Depietto*, No. 20-CV-8043 (KMK), 2021 WL 3287416, at *6 (S.D.N.Y. Aug. 2, 2021) ("A number of courts, including several within the Second Circuit, have concluded that **§** 1123(d) may require the debtor to pay a default interest rate in order to cure a default."); *In re New Inv., Inc.*, 840 F.3d 1137, 1142 (9th Cir. 2016) ("The parties bargained for a higher interest rate on the note in the event of default, and Pacifica is entitled to the benefit of that bargain under the terms of **§** 1123(d)."); *In re Moshe*, 567 B.R. 438, 444 (Bankr. E.D.N.Y. 2017) ("Courts interpreting **Section** 1123(d) have held that the underlying loan agreement and state law determine whether a debtor must cure using the default rate of interest in a Chapter 11 plan."); *In re Gen. Growth Properties, Inc.*, 451 B.R. 323, 327 (Bankr. S.D.N.Y. 2011) (holding that **§** 1123(d) compelled the payment of default interest at the contractual rate).

6 Although the Claimholders raised limited factual objections to the solvency analysis before the District Court, *see LATAM II*, 643 B.R. at 752, they have not done so on this appeal.

7 The TLA Claimholders also argue that *Associates Commercial Corporation v. Rash*, 520 U.S. 953, 117 S.Ct. 1879, 138 L.Ed.2d 148 (1997), required the Bankruptcy Court to look to TLA's value as a going concern. But *Rash* does not provide a general standard for valuation: it interpreted specific statutory language in 11 U.S.C. **§** 506(a). *See Rash*, 520 U.S. at 961–62, 117 S.Ct. 1879 (holding that **Section** 506(a)'**s** second sentence "expressly addresses how 'value shall be determined' " in the context of secured claims). Because that provision of the Code does not apply here, neither does *Rash*'**s** interpretation of that provision.

8 In support of their position, the TLA Claimholders primarily rely on *PG&E* and *Ultra Petroleum II*. Although both cases stated that the solvent-debtor exception has roots in the absolute priority rule, neither addressed the proper standard for determining solvency. There was no need to do so, as each debtor's solvency was obvious and consequently undisputed. *See PG&E*, 46 F.4th at 1051 ("...PG&E was, and has remained, solvent. Its assets at the time of the bankruptcy filing exceeded its known liabilities by nearly $20 billion."); *Ultra Petroleum II*, 51 F.4th at 143 ("During the bankruptcy proceedings, the same volatile commodity prices that hurled Ultra into insolvency propelled the debtors back into solvency. Indeed, Ultra became 'massively solvent.' "). We therefore do not understand either court's discussion of history to bear on the proper test for solvency.

9 The Claimholders mention in passing that a plan cannot be crammed down if it does not comply with the best-interest-of-creditors test, 11 U.S.C. **§** 1129(a)(7), which requires **impaired**, dissenting creditors to receive as much as they would have in a Chapter 7 liquidation. Appellant's Br. 7. We do not understand them to argue that the Plan would have failed this test. **Section** 1129(a)(7) "essentially requires every plan proponent to perform a liquidation analysis of the estate," which "will often be proved through the testimony of auctioneers or other liquidators as to what the assets will yield under more or less 'firesale' conditions." 7 Collier on Bankruptcy ¶ 1129.02[7][b][iii] (16th ed. 2022); *see also Toibb v. Radloff*, 501 U.S. 157, 164, 111 S.Ct. 2197, 115 L.Ed.2d 145 (1991) (describing this process as assuming "an immediate liquidation of

the debtor's assets”). Given the analyses proffered by the Debtors, we have no basis to assume that the Claimholders would be better off in a Chapter 7 liquidation.

10 Under these circumstances, it is unnecessary to consider whether the Bankruptcy Court correctly put the burden on the Claimholders to prove TLA's insolvency. The Debtors did provide affirmative evidence of TLA's insolvency, which the Bankruptcy Court determined to be reliable.

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II. UNITED STATES TRUSTEE FEES

Siegel v. Fitzgerald, 142 S.Ct. 1770 (2022)

142 S.Ct. 1770
Supreme Court of the United States.

Alfred H. SIEGEL, Trustee of the Circuit City Stores, Inc. Liquidating Trust, Petitioner
v.
John P. FITZGERALD, III, Acting United States Trustee for Region 4

No. 21-441
|
Argued April 18, 2022
|
Decided June 6, 2022

Synopsis
Background: Trustee of liquidating trust established under debtors' confirmed Chapter 11 plan filed motion to determine extent of liability for post-confirmation quarterly United States Trustee (UST) fees, asking the court to order that, notwithstanding amendment of governing statute by the Bankruptcy Judgeship Act of 2017, the amount of such fees be determined based on statutory rates in effect as of petition date in this case. UST moved for summary judgment. The United States Bankruptcy Court for the Eastern District of Virginia, No. 3:08-bk-35653, Kevin R. Huennekens, J., 606 B.R. 260, granted motion to determine and denied motion for summary judgment, and parties sought leave to appeal directly to the Court of Appeals, which was granted. The United States Court of Appeals for the Fourth Circuit, King, Circuit Judge, 996 F.3d 156, reversed in relevant part and remanded. Certiorari was granted.

Holdings: The Supreme Court, Justice Sotomayor, held that:

statutory amendment which imposed a temporary, significant increase in the bankruptcy fees applicable to large Chapter 11 cases in United States Trustee (UST) program districts, but not to cases in Bankruptcy Administrator (BA) districts, was a law "on the subject of Bankruptcies" to which the uniformity requirement of the Bankruptcy Clause applied, and

the amendment in question violated the uniformity requirement of the Bankruptcy Clause, abrogating *In re Mosaic Management Group, Inc.*, 22 F.4th 1291, and *Matter of Buffets, L.L.C.*, 979 F.3d 366.

Reversed and remanded.

Procedural Posture(s): Petition for Writ of Certiorari; On Appeal; Application for Bankruptcy Trustee Fees; Motion for Summary Judgment.

West Codenotes

Prior Version Held Unconstitutional
28 U.S.C.A. § 1930(a)(6)(B).

***1772** *Syllabus* [*]

Congress created the United States Trustee Program (Trustee Program) as a mechanism to transfer administrative functions previously handled by bankruptcy judges to U. S. Trustees, a component of the Department of Justice. Congress permitted the six judicial districts in North Carolina and Alabama to opt out of the Trustee Program. In these six districts, bankruptcy courts continue to appoint bankruptcy administrators under a system called the Administrator Program. The Trustee Program and the Administrator Program handle the same core administrative functions, but have different funding sources. Congress requires that the Trustee Program be funded in its entirety by user fees paid to the United States Trustee System Fund (UST Fund), largely paid by debtors who file cases under Chapter 11 of the Bankruptcy Code. 28 U.S.C. § 589a(b)(5). Those debtors pay a fee in each quarter of the year that their case remains pending at a rate set by Congress and determined by the amount of disbursements the debtor's estate made that quarter. See § 1930(a). In contrast, the Administrator Program is funded by the Judiciary's general budget. While initially Congress did not require Administrator Program district debtors to pay user fees at all, Congress permitted the Judicial Conference of the United States to require Chapter 11 debtors in Administrator Program districts to pay fees equal to those imposed in Trustee Program districts. See § 1930(a)(7). Pursuant to a 2001 standing order of the Judicial Conference, from 2001 to 2017 all districts nationwide charged similarly situated debtors uniform fees.

In 2017, Congress enacted a temporary increase in the fee rates applicable to large Chapter 11 cases to address a shortfall in the UST Fund. See 131 Stat. 1229 (2017 Act). The 2017

Act provided that the fee raise would become effective in the first quarter of 2018, would last only through 2022, and would be applicable to currently pending and newly filed cases. The Judicial Conference adopted the 2017 fee increase for the six Administrator Program districts, effective October 1, 2018, and applicable only to newly filed cases.

In 2008, Circuit City Stores, Inc., filed for Chapter 11 bankruptcy in the Eastern District of Virginia, a Trustee Program district. In 2010, the Bankruptcy Court confirmed a joint-liquidation plan, overseen by a trustee (petitioner here), to collect, administer, distribute, and liquidate all of Circuit City's assets. The liquidation plan required petitioner to pay quarterly fees to the U. S. Trustee while the Chapter 11 case was pending. Circuit City's bankruptcy was still pending when Congress increased the fees for Chapter 11 debtors in Trustee Program districts through the 2017 Act. Across the first three quarters of 2018, petitioner paid $632,542 in total fees, significantly more than the $56,400 petitioner would have paid absent the fee increase in the 2017 Act. Petitioner filed for relief against the Acting U. S. Trustee for Region 4 (respondent here) contending that the fee increase was nonuniform across Trustee Program districts and Administrator Program districts, in violation of the Constitution's Bankruptcy Clause. The Bankruptcy Court agreed, and directed that for the fees due from January 1, 2018, onward, the Circuit City trustee pay the rate in effect prior to the 2017 Act. The Bankruptcy Court reserved the question whether the trustee could recover any "overpayments" made under the 2017 Act. The Fourth Circuit reversed, holding that the fee increase did not violate the uniformity requirement of the Bankruptcy Clause because the increase applied only to debtors in Trustee Program districts in order to bolster the dwindling UST Fund, which funded the Trustee Program alone.

Held: Congress' enactment of a significant fee increase that exempted debtors in two States violated the uniformity requirement of the Bankruptcy Clause. Pp. 1778 - 1783.

(a) The Bankruptcy Clause's uniformity requirement—which empowers Congress to establish "uniform Laws on the subject of Bankruptcies throughout the United States," U. S. Const., Art. I, § 8, cl. 4—applies to the 2017 Act. Respondent contends that the 2017 Act was not a law "on the subject of Bankruptcies" to which the uniformity requirement applies, but instead a law enacted pursuant to the Necessary and Proper Clause, U. S. Const., Art. I, § 8, cl. 18, meant to help administer substantive bankruptcy law. Nothing in the language of the Bankruptcy Clause suggests a distinction between substantive and administrative laws, however, and this Court has repeatedly emphasized that the Bankruptcy Clause's language, embracing "laws on the subject of Bankruptcies," is broad. This Court has never distinguished between substantive and administrative bankruptcy laws or suggested that the uniformity requirement would not apply to both. Further, the Court has never suggested that all administrative bankruptcy laws are enacted pursuant to the Necessary and Proper Clause, nor that the Necessary and Proper Clause permits Congress to circumvent the limitations set by the Bankruptcy Clause. To the contrary, Congress cannot evade the "affirmative limitation" of the uniformity requirement by enacting legislation pursuant to other grants of authority. See *Railway Labor Executives' Assn. v. Gibbons*, 455 U.S. 457, 468–469, 102 S.Ct. 1169, 71 L.Ed.2d 335. In any event, the 2017 fee provision fits comfortably under the scope of the Bankruptcy Clause: The provision amended a statute titled "Bankruptcy fees," § 1930, and the only "subject" of the 2017 Act is bankruptcy. Moreover, the 2017 Act does affect the "substance of debtor-creditor relations" because increasing mandatory fees paid out of the debtor's estate decreases the funds available for payment to creditors. Respondent points to purported historic analogues to argue that the uniformity requirement does not apply where Congress sets different fee structures with different funding mechanisms for debtors in different bankruptcy districts. But the fee increase at issue here is materially different from the examples cited by respondent. Unlike respondent's examples, the 2017 Act does not confer discretion on bankruptcy districts to set regional policies based on regional needs. Rather, Congress exempted debtors in only 2 States from a fee increase that applied to debtors in 48 States, without identifying any material difference between debtors across those States. Pp. 1778 - 1780.

(b) The 2017 Act violated the uniformity requirement of the Bankruptcy Clause. The Bankruptcy Clause confers broad authority on Congress with the limitation that the laws enacted be "uniform." The Court's three decisions addressing the uniformity requirement together stand for the proposition that the Bankruptcy Clause does not permit arbitrary geographically disparate treatment of debtors. In *Moyses* v. *Hanover Nat'l Bank*, 186 U.S. 181, 22 S.Ct. 857, 46 L.Ed. 1113, the Court rejected a challenge to the constitutionality of the Bankruptcy Act of 1898, which permitted individual debtor exemptions under different state laws, explaining that the "general operation of the law is uniform although it may result in certain particulars differently in different States." *Id.,* at 190, 22 S.Ct. 857. In the *Regional Rail Reorganization Act Cases,* 419 U.S. 102, 95 S.Ct. 335, 42 L.Ed.2d 320, the Court affirmed the constitutionality of legislation which applied only to rail carriers operating within a defined region of the country, noting the "flexibility inherent" in the Bankruptcy Clause, *id.,* at 158, 95 S.Ct. 335, permits Congress to enact geographically limited bankruptcy laws consistent with the uniformity requirement in response to a geographically limited problem. In *Gibbons*, 455 U.S. 457, 102 S.Ct. 1169, 71 L.Ed.2d 335, the Court struck down legislation in which Congress altered the priority of claimants in a single railroad's bankruptcy proceedings, holding that "[t]o survive scrutiny under the Bankruptcy Clause, a law must at least apply uniformly to a defined class of debtors." *Id.*, at 473, 102 S.Ct. 1169.

Here, all agree that the 2017 Act's fee increase was not geographically uniform because the fee increase applied differently to Chapter 11 debtors in different regions. That geographical disparity meant that petitioner paid over $500,000 more in fees compared to an identical debtor in North Carolina or Alabama. While respondent contends that such disparities were a permissible effort to solve the budgetary shortfall in the UST Fund, an arguably geographical problem, that shortfall stemmed not from an external and geographically isolated need, but from Congress' creation of a dual bankruptcy system which allowed certain districts to opt into a system more favorable for debtors. The Clause does not permit Congress to treat identical debtors differently based on artificial distinctions Congress itself created. Pp. 1780 - 1783.

(c) The Court remands for the Fourth Circuit to consider in the first instance the proper remedy. Pp. 1782 - 1783.

996 F.3d 156, reversed and remanded.

SOTOMAYOR, J., delivered the opinion for a unanimous Court.

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Opinion

Justice SOTOMAYOR delivered the opinion of the Court.

The Bankruptcy Clause empowers Congress to establish "uniform Laws on the subject of Bankruptcies throughout the United States." U. S. Const., Art. I, § 8, cl. 4. The Clause's requirement that bankruptcy laws be "uniform" is not a straitjacket: Congress retains flexibility to craft legislation that responds to different regional circumstances that arise in the bankruptcy system. Nor, however, is this uniformity requirement toothless. The question in this case is whether Congress' enactment of a significant fee increase that exempted debtors in two States violated the uniformity requirement. Here, it did.

I

A

Bankruptcy cases involve both traditional judicial responsibilities and extensive administrative ones. Until 1978, bankruptcy judges handled both. This meant that, in addition to their traditional judicial function of ruling on disputed matters in adversarial proceedings, bankruptcy judges dealt with an array of administrative tasks, such as appointing private trustees where appropriate; organizing creditors' committees; supervising the filing of required reports, schedules, and taxes; and monitoring cases for signs of abuse and fraud. See H. R. Rep. No. 99–764, p. 17 (1986).

***1776** Concerned that these dual roles were overloading bankruptcy judges and creating an appearance of bias, particularly because judges were responsible for supervising trustees that they themselves had appointed, Congress in 1978 piloted the United States Trustee Program (Trustee Program) in 18 of the 94 federal judicial districts. See *id.*, at 17–18; Bankruptcy Reform Act of 1978, 92 Stat. 2549. To "rende[r] the separation of administrative and judicial functions complete," the pilot program transferred the administrative functions previously handled by the bankruptcy courts to newly created U. S. Trustees, housed within the Department of Justice rather than the Administrative Office of the U. S. Courts. H. R. Rep. No. 95–595, p. 115 (1977).

In 1986, Congress sought to make the pilot Trustee Program permanent and to expand it nationwide, but met resistance from stakeholders in North Carolina and Alabama. See The United States Trustee System: Hearing on S. 1961 before the Subcommittee on Courts of the Senate Committee on the Judiciary, 99th Cong., 2d Sess., 129 (1986). As a result, Congress opted to expand mandatorily the Trustee Program to all federal judicial districts except for the six judicial districts in North Carolina and Alabama. Congress permitted only those six districts to continue judicial appointment of bankruptcy administrators, referring to that system as the Administrator Program. §§ 111–115, 302(d)(3), 100 Stat. 3090–3095, 3121–3123. The Administrator Program was scheduled to phase out in 1992, but Congress extended it by 10 years. § 317(a), 104 Stat. 5115. At the end of those 10 years, however, Congress did not phase out the Administrator Program. Instead, it eliminated the sunset period and permanently exempted the six districts from the requirement to transition to the Trustee Program, while providing that each district could individually elect to do so. § 501, 114 Stat. 2421–2422 (2000 Act); § 302(d)(3), 100 Stat. 3121–3123. Each of the six districts continues to participate in the Administrator Program.

The Trustee Program and the Administrator Program handle the same core administrative functions, but have different funding sources. Congress requires that the Trustee Program be funded in its entirety by user fees paid to the United States Trustee System Fund (UST Fund), the bulk of which are paid by debtors who file cases under Chapter 11 of the Bankruptcy Code. 28 U.S.C. § 589a(b)(5). Those debtors pay a fee in each quarter of the year that their case remains pending at a rate set by Congress. The fee varies according to the amount of funds paid out ("disbursed") from the bankruptcy estate to creditors, suppliers, and other parties during that quarter. See § 1930(a).

In contrast, Congress does not require the Administrator Program to fund itself. Instead, the Administrator Program is funded by the Judiciary's general budget. *In re Circuit City Stores, Inc.*, 996 F.3d 156, 160 (CA4 2021). Initially, Congress did not require Administrator Program district debtors to pay user fees at all. After the Ninth Circuit held that system unconstitutional, see *St. Angelo v. Victoria Farms, Inc.*, 38 F.3d 1525, 1532–1533 (1994), amended, 46 F.3d 969 (1995), Congress provided that " 'the Judicial Conference of the United States may require the debtor in a case under chapter 11 [filed in an Administrator Program district] to pay fees equal to those imposed' " in Trustee Program districts, 2000 Act § 105, 114 Stat. 2412 (enacting 28 U.S.C. § 1930(a)(7)). Congress directed that any such fees be deposited into a fund that offsets appropriations to the Judicial Branch. *Ibid.* The Judicial Conference adopted a standing order in 2001 directing ***1777** Administrator Program districts to charge fees "in the amounts specified in 28 U.S.C. § 1930, as those amounts may be amended from time to time." Report of the Proceedings of the Judicial Conference of the United States 46 (Sept./Oct. 2001). Under this standing order, for the next 17 years, the Judicial Conference matched all Trustee Program fee increases with equivalent Administrator Program fee increases, meaning that all districts nationwide charged similarly situated debtors uniform fees.

In 2017, concerned with a shortfall in the UST Fund, Congress enacted a temporary, but significant, increase in the fee rates applicable to large Chapter 11 cases. See Pub. L. 115–72, Div. B, 131 Stat. 1229 (2017 Act). The increase was set to take effect only if the UST Fund balance dropped below $200 million as of September 30 of the most recent fiscal year. If that condition was met, the increase applied on a quarterly basis to any debtors with a disbursement of $1 million or more during that quarter, regardless of whether their case was newly filed or already pending when the increase took effect. For those debtors, the maximum fee was increased from $30,000 a quarter to $250,000 a quarter. § 1004(a), *id.*, at 1232. The statute provided that the fee raise would become effective in the first quarter of 2018 and would last only through 2022.

Despite the Judicial Conference's standing order, and unlike with previous fee increases, the six districts in the two States participating in the Administrator Program did not immediately adopt the 2017 fee increase. Only in September 2018 did the Judicial Conference order Administrator Program districts to implement the amended fee schedule. Even then, however, two key differences remained between the fee increase faced by debtors in Trustee Program districts as opposed to those faced by debtors in Administrator Program districts. First, the fee increase took effect for the six Administrator Program districts as of October 1, 2018, while the increase took effect for the Trustee Program districts as of the first quarter of 2018. Second, in Administrator Program districts, the fee increase applied only to newly filed cases, while in Trustee Program districts, the increase applied to all pending cases.

In 2021, Congress amended the statute governing parity of fees between Trustee Program and Administrator Program districts, § 1930(a)(7), to replace the word "may" with "shall." See Pub. L. 116–325, 134 Stat. 5088. As a result, the statute now provides that the Judicial Conference "shall require" imposition of fees in Administrator Program districts that are equal to those imposed in Trustee Program districts. § 1930(a)(7). This change "confirm[ed] the longstanding intention of Congress that quarterly fee requirements remain consistent across all Federal judicial districts." *Id.*, at 5086.

B

In 2008, Circuit City Stores, Inc., filed for Chapter 11 bankruptcy in the Eastern District of Virginia, a Trustee Program district. In 2010, the Bankruptcy Court confirmed a joint-liquidation plan, overseen by a trustee (petitioner here), to collect, administer, distribute, and liquidate all of Circuit City's assets. The liquidation plan required petitioner to " 'pay quarterly fees to the U. S. Trustee until the Chapter 11 Cases are closed or converted.' " *In re Circuit City Stores*, 606 B.R. 260, 263 (2019). In 2010, when the plan was confirmed, the maximum quarterly fee was $30,000.

Circuit City's bankruptcy was still pending when Congress raised the fees for Chapter 11 debtors in Trustee Program ***1778** districts through the 2017 Act. Across the first three quarters after the fee increase took effect, petitioner paid $632,542 in total fees. *Id.*, at 267, n. 20. Had Congress not increased fees, petitioner would have paid $56,400 over that same period. *Ibid.*

Petitioner filed for relief against the Acting U. S. Trustee for Region 4 (respondent here, represented by the Solicitor General) in the Bankruptcy Court of the Eastern District of Virginia. Petitioner objected that the fee increase under the 2017 Act was nonuniform across Trustee Program districts and Administrator Program districts, in violation of the Constitution's Bankruptcy Clause. The Bankruptcy Court agreed, and directed that for the fees due from January 1, 2018, onward, the trustee pay the rate in effect prior to the 2017 Act. *Id.*, at 270–271. The court reserved the question whether the trustee could recover any "overpayments" made under the 2017 Act. *Ibid.*

A divided panel of the Fourth Circuit reversed. The court agreed that the uniformity requirement of the Bankruptcy Clause applied to the 2017 Act, but it interpreted the Clause as forbidding "only 'arbitrary' geographic differences." 996 F.3d at 166. In the court's view, the fee increase permissibly applied only to Trustee Program districts because the UST Fund, which funded that program alone, was dwindling. Therefore, the court reasoned, Congress' effort to remedy that problem was not arbitrary. Judge Quattlebaum dissented in relevant part, interpreting the Bankruptcy Clause to preclude disparate treatment of bankruptcy districts unless the treatment was "aimed at addressing issues that are geographical in nature." *Id.*, at 175. In Judge Quattlebaum's view, the difference between Trustee Program districts and Administrator Program districts was arbitrary, as there was nothing "geographically distinct about Alabama or North Carolina that justified a different approach in those states." *Ibid.*

This Court granted certiorari, 595 U. S. ——, 142 S.Ct. 752, 211 L.Ed.2d 471 (2022), to resolve a split that had developed in the lower courts over the constitutionality of the 2017 Act. [1]

II

A

The Bankruptcy Clause empowers Congress to establish "uniform Laws on the subject of Bankruptcies throughout the United States." U. S. Const., Art. I, § 8, cl. 4. The first question before the Court is whether the 2017 Act is subject to the Bankruptcy Clause's uniformity requirement at all.

Respondent contends that the 2017 Act was not a law "on the subject of Bankruptcies" to which the uniformity requirement applies, but, rather, a law meant to help administer substantive bankruptcy law. Respondent interprets the Bankruptcy Clause as extending only to laws that "alter the substance of debtor-creditor relations," such as laws that set priorities for claims or exempt property from an estate. Brief for Respondent 25. In respondent's view, the Necessary and Proper Clause, U. S. Const., Art. I, § 8, cl. 18, supplies the authority for Congress to pass a law auxiliary to a substantive bankruptcy law.

Nothing in the language of the Bankruptcy Clause itself, however, suggests ***1779** a distinction between substantive and administrative laws. This Court has repeatedly emphasized that the Bankruptcy Clause's language, embracing "laws on the subject of Bankruptcies," is broad. For example, the Court has recognized that the "subject of bankruptcies is incapable of final definition," and includes "nothing less than 'the subject of the relations between [a] debtor and his creditors.' " *Wright v. Union Central Life Ins. Co.*, 304 U.S. 502, 513–514, 58 S.Ct. 1025, 82 L.Ed. 1490 (1938). Without purporting to define the full scope of the Clause, the Court has interpreted the Clause to have "granted plenary power to Congress over the whole subject of 'bankruptcies,' " and observed that the "language used" did not "limit" the scope of Congress' authority. *Hanover Nat. Bank v. Moyses*, 186 U.S. 181, 187, 22 S.Ct. 857, 46 L.Ed. 1113 (1902).

Nor has this Court ever distinguished between substantive and administrative bankruptcy laws or suggested that the uniformity requirement would not apply to both. Respondent argues that each of this Court's prior cases on the uniformity requirement has addressed what he terms "substantive bankruptcy laws," Brief for Respondent 24, but these cases do not establish that the uniformity requirement only applies to such "substantive" laws. This Court has stated that "the powers of the general grant" of the Necessary and Proper Clause must be added to the Bankruptcy Clause's "specific grant" of power to Congress to legislate on the subject of bankruptcies. *Wright*, 304 U.S. at 513, 58 S.Ct. 1025. The Court has never suggested, however, that all "administrative" bankruptcy laws, Brief for Respondent 13, are enacted pursuant to the Necessary and Proper Clause, nor that the Necessary and Proper Clause permits Congress to circumvent the limitations set by the Bankruptcy Clause. To the contrary, the Court has held that Congress cannot evade the "affirmative limitation" of the uniformity requirement by enacting legislation pursuant to other grants of authority. *Railway Labor Executives' Assn. v. Gibbons*, 455 U.S. 457, 468–469, 102 S.Ct. 1169, 71 L.Ed.2d 335 (1982) (rejecting the contention that Congress could "enact nonuniform bankruptcy laws pursuant to the Commerce Clause," because doing so "would eradicate from the Constitution a limitation on the power of Congress to enact bankruptcy laws").

Not surprisingly, all courts to have considered this question to date (even those that have found the 2017 Act constitutional) have accepted that the statute is subject to the Bankruptcy Clause's uniformity requirement. See *In re Clinton Nurseries, Inc.*, 998 F.3d 56, 64, and n. 6 (CA2 2021) (collecting cases). The 2017 fee provision amended a statute titled "Bankruptcy fees." 28 U.S.C. § 1930. The provision's effect is to set fees that must be paid by a bankruptcy trustee from the debtor's estate in a bankruptcy proceeding. The only "subject" of the 2017 Act is bankruptcy. Moreover, and importantly, the 2017 Act does affect the "substance of debtor-creditor relations": Increasing mandatory fees paid out of the debtor's estate decreases the funds available for payment to creditors. As a result, the obligations between creditors and debtors are changed.

Respondent also argues that historic and modern congressional practice support the notion that bankruptcy fees are wholly exempt from the uniformity requirement. This argument glosses over the nature of the practices at issue. The historic examples respondent cites concern uniform federal laws allowing for local variation by delegating discretion to districts to establish their own procedures for certain bankruptcy matters, including fees, in view of local needs and conditions. See An Act to ***1780** Establish an Uniform System of Bankruptcy Throughout the United States, § 47, 2 Stat. 33 (1800) (providing "[t]hat the district judges, in each district respectively, shall fix a rate of allowance to be made to the commissioners of bankruptcy"); An Act to Establish a Uniform System of Bankruptcy Throughout the United States, § 6, 5 Stat. 446 (1841) (establishing that district courts may "prescribe a tariff or table of fees and charges"). Similarly, the contemporary laws respondent cites are uniform laws allowing for local determination of governing rules. See, *e.g.,* 28 U.S.C. §§ 158(b)(1), (6) (providing that district courts may, but need not, participate in the bankruptcy appellate panel for its circuit if the circuit has created one). As discussed below, see *infra*, at 1780 - 1781, the uniformity requirement does not demand that Congress forbid or eliminate such local variation or choice.

The fee increase at issue here is materially different from these laws. It does not confer discretion on bankruptcy districts to set regional policies based on regional needs. Rather, Congress exempted debtors in only 2 States from a fee increase that applied to debtors in 48 States, without identifying any material difference between debtors across those States. The only difference between the States in which the fee increase applied and the States in which it was not required was the desire of those two States not to participate in the Trustee Program. The historical record therefore provides no support for respondent's argument that the uniformity requirement does not apply where Congress sets different fee structures with different funding mechanisms for debtors in different bankruptcy districts.

B

Having determined that the 2017 Act falls within the ambit of the Bankruptcy Clause, the Court must now decide whether the Act was a permissible exercise of that Clause.

1

Although the Bankruptcy Clause confers broad authority on Congress, the Clause also imposes a limitation on that authority: the requirement that the laws enacted be "uniform." The Court has addressed the uniformity requirement on three occasions. Taken together, they stand for the proposition that the Bankruptcy Clause offers Congress flexibility, but does not permit arbitrary geographically disparate treatment of debtors.

The Court first addressed the uniformity requirement in rejecting a challenge to the constitutionality of the Bankruptcy Act of 1898, which permitted individual debtor exemptions, including homestead and wage exemptions under state laws. *Moyses*, 186 U.S. 181, 22 S.Ct. 857, 46 L.Ed. 1113. The Court in *Moyses* held that the Bankruptcy Clause's uniformity principle does not require Congress to eliminate existing state exemptions in bankruptcy laws. *Id.*, at 188, 22 S.Ct. 857. The Court explained that the "general operation of the law is uniform although it may result in certain particulars differently in different States." *Id.*, at 190, 22 S.Ct. 857.

Next, in the *Regional Rail Reorganization Act Cases*, 419 U.S. 102, 95 S.Ct. 335, 42 L.Ed.2d 320 (1974), the Court affirmed the constitutionality of the Regional Rail Reorganization Act of 1973, which applied only to rail carriers operating within a defined region of the country, where "[n]o railroad reorganization ... was pending outside that defined region." *Id.,* at 159–160, 95 S.Ct. 335. The Court described the "flexibility inherent" in the Bankruptcy Clause, *id.,* at 158, 95 S.Ct. 335, which "does not deny Congress power ***1781** to take into account differences that exist between different parts of the country, and to fashion legislation to resolve geographically isolated problems," *id.,* at 159, 95 S.Ct. 335. Because the Regional Rail Reorganization Act "operate[d] uniformly upon all bankrupt railroads then operating in the United States," it was consistent with the Bankruptcy Act's uniformity principle. *Id.,* at 160, 95 S.Ct. 335. Put simply, Congress may enact geographically limited bankruptcy laws consistent with the uniformity requirement if it is responding to a geographically limited problem.

While the uniformity requirement allows Congress to account for "differences that exist between different parts of the country," *id.,* at 159, 95 S.Ct. 335, it does not give Congress free rein to subject similarly situated debtors in different States to different fees because it chooses to pay the costs for some, but not others. In *Gibbons*, 455 U.S. 457, 102 S.Ct. 1169, 71 L.Ed.2d 335, the Court struck down the Rock Island Railroad Transition and Employee Assistance Act (RITA), in which Congress altered the order of priority of claimants in a single railroad's bankruptcy proceedings. The Court recognized that the Bankruptcy Clause "contains an affirmative limitation or restriction upon Congress' power," namely, the uniformity requirement. *Id.,* at 468, 102 S.Ct. 1169. RITA exceeded this limitation, the Court explained, because it singled out one railroad and did not apply to other similarly situated railroads that were engaged in bankruptcy proceedings. *Id.,* at 470, 102 S.Ct. 1169. The Court reasoned that unlike the Regional Rail Reorganization Act, RITA was "not a response either to the particular problems of major railroad bankruptcies or to any geographically isolated problem: it is a response to the problems caused by the bankruptcy of *one* railroad." *Ibid.* For that reason, RITA "cannot be said to apply uniformly even to major railroads in bankruptcy proceedings throughout the United States." *Id.*, at 471, 102 S.Ct. 1169. The Court emphasized that its "holding ... does not impair Congress' ability under the Bankruptcy Clause to define classes of debtors and to structure relief accordingly" and summarized that "[t]o survive scrutiny under the Bankruptcy Clause, a law must at least apply uniformly to a defined class of debtors." *Id.*, at 473, 102 S.Ct. 1169.

In sum, our precedent provides that the Bankruptcy Clause offers Congress flexibility, but does not permit the arbitrary, disparate treatment of similarly situated debtors based on geography.

2

Here, there is no dispute that the 2017 Act's fee increase was not geographically uniform. The only remaining question is whether Congress permissibly imposed nonuniform fees because it was responding to a funding deficit limited to the Trustee Program districts. Under the specific circumstances present here, the nonuniform fee increase violated the uniformity requirement.

All agree that the fee increase applied differently to Chapter 11 debtors in different regions. Debtors in Alabama and North Carolina, unlike debtors in the remainder of the country, paid no fee increases for the first three quarters of 2018. Moreover, the fee increase only applied to newly filed cases, and not pending cases, in those two States. That geographical disparity meant that petitioner paid over $500,000 more in fees compared to an identical debtor in North Carolina or Alabama.

Recognizing that the 2017 Act caused such disparities, respondent contends that those disparities were a permissible effort to solve a particular geographical problem: the budgetary shortfall that befell ***1782** the UST Fund, which supports the Trustee Program but not the Administrator Program. Respondent argues that this problem justified Congress' imposition of fee increases specific to Trustee Program districts in order to replenish the UST Fund's coffers. It is true that Congress' stated goal in raising fees in Trustee Program districts was to address this budgetary shortfall. That shortfall, however, existed only because Congress itself had arbitrarily separated the districts into two different systems with different cost funding mechanisms, requiring Trustee Program districts to fund the Program through user fees while enabling Administrator Program districts to draw on taxpayer funds by way of the Judiciary's general budget.

The problem Congress sought to address here is thus different from the problem facing the debtors in the *Regional Rail Reorganization Act Cases*. There, a "national rail transportation crisis" prompted Congress to respond with the Regional Rail Reorganization Act of 1973. 419 U.S. at 159, 95 S.Ct. 335. That crisis arose when eight major railroads located in the Northeast and the Midwest entered reorganization proceedings. *Id.*, at 108, 95 S.Ct. 335. Congress responded accordingly with legislation tailored to those regions. *Id.*, at 108–109, 95 S.Ct. 335. The problems prompting Congress' disparate treatment in this case, however, stem not from an external and geographically isolated need, but from Congress' own decision to create a dual bankruptcy system funded through different mechanisms in which only districts in two States could opt into the more favorable fee system for debtors.

The Bankruptcy Clause affords Congress flexibility to "fashion legislation to resolve geographically isolated problems," *id.*, at 159, 95 S.Ct. 335, but as precedent instructs, the Clause does not permit Congress to treat identical debtors differently based on an artificial funding distinction that Congress itself created. The Clause, after all, would clearly prohibit Congress from arbitrarily dividing States into two categories and charging different fees to States in different categories unrelated to the needs of, or conditions in, those States. The Clause does not allow Congress to accomplish in two steps what it forbids in one. [2]

A few observations on the limits of this decision are in order. The Court does not today address the constitutionality of the dual scheme of the bankruptcy system itself, only Congress' decision to impose different fee arrangements in those two systems. The Court's holding today also should not be understood to impair Congress' authority to structure relief differently for different classes of debtors or to respond to geographically isolated problems. The Court holds only that the uniformity requirement of the Bankruptcy Clause prohibits Congress from arbitrarily burdening only one set of debtors with a more onerous funding mechanism than ***1783** that which applies to debtors in other States.

C

The parties dispute the appropriate remedy. Petitioner seeks a full refund of fees that it paid during the nonuniform period. Respondent argues that any remedy should apply only prospectively, or should result in a fee increase for debtors who paid less in the Administrator Program districts. The parties raise a host of legal and administrative concerns with each of the remedies proposed, including the practicality, feasibility, and equities of each proposal; their costs; and potential waivers by nonobjecting debtors. The court below, however, has not yet had an opportunity to address these issues or their relevancy to the proper remedy. "[M]indful that we are a court of review, not of first view," *Cutter v. Wilkinson*, 544 U.S. 709, 718, n. 7, 125 S.Ct. 2113, 161 L.Ed.2d 1020 (2005), this Court remands for the Fourth Circuit to consider these questions in the first instance.

* * *

For these reasons, the judgment of the Court of Appeals for the Fourth Circuit is reversed, and the case is remanded for further proceedings consistent with this opinion.

It is so ordered.

All Citations

142 S.Ct. 1770, 213 L.Ed.2d 39, 71 Bankr.Ct.Dec. 155, Bankr. L. Rep. P 83,753, 22 Cal. Daily Op. Serv. 5553, 2022 Daily Journal D.A.R. 5613, 29 Fla. L. Weekly Fed. S 305

Footnotes

* The syllabus constitutes no part of the opinion of the Court but has been prepared by the Reporter of Decisions for the convenience of the reader. See *United States v. Detroit Timber & Lumber Co.*, 200 U.S. 321, 337, 26 S.Ct. 282, 50 L.Ed. 499.

1 Compare *In re John Q. Hammons Fall 2006, LLC*, 15 F.4th 1011 (CA10 2021) (2017 Act is unconstitutional); *In re Clinton Nurseries, Inc.*, 998 F.3d 56 (CA2 2021) (same), with *In re Mosaic Mgmt. Group, Inc.*, 22 F.4th 1291 (CA11 2022) (2017 Act is constitutional); *In re Circuit City Stores, Inc.*, 996 F.3d 156 (CA4 2021) (same); *In re Buffets, LLC*, 979 F.3d 366 (CA5 2020) (same).

2 Respondent further argues that any uniformity violation should be attributed to the Judicial Conference and not to Congress, because Congress expected the Judicial Conference to implement the 2017 Act's fee increase in Administrator Program districts. As respondent sees it, it is the Judicial Conference's failure to implement the fee increase that is responsible for the disparate fees, not the 2017 Act itself. Respondent provides ample evidence that Congress likely understood, when it passed the 2017 Act, that the Judicial Conference would impose the same fee increase. That said, prior to the 2021 amendment, the fee statute did not *require* the Judicial Conference to impose an equivalent increase. It is that congressional decision that led to the disparities at issue here.

860 Fed.Appx. 544
This case was not selected for publication in West's Federal Reporter.
See Fed. Rule of Appellate Procedure 32.1 generally governing citation of judicial decisions issued on or after Jan. 1, 2007. See also U.S.Ct. of App. 9th Cir. Rule 36-3.
United States Court of Appeals, Ninth Circuit.

IN RE: David William BARTENWERFER; Kate Marie Bartenwerfer, Debtors,
Kieran Buckley, Appellant,
v.
David William Bartenwerfer; Kate Marie Bartenwerfer, Appellees.
In re: David William Bartenwerfer; Kate Marie Bartenwerfer, Debtors,
Kieran Buckley, Appellant,
v.
David William Bartenwerfer; Kate Marie Bartenwerfer, Appellees.
In re: David William Bartenwerfer; Kate Marie Bartenwerfer, Debtors,
David William Bartenwerfer; Kate Marie Bartenwerfer, Appellants,
v.
Kieran Buckley, Appellee.

No. 20-60021, No. 20-60023, No. 20-60024
|
Argued and Submitted July 29, 2021 San Francisco, California
|
FILED August 12, 2021

Synopsis
Background: Judgment creditor filed adversary complaint, seeking determination that debt was excepted from discharge because Chapter 7 debtors fraudulently concealed material defects plaguing renovated house that they sold to him prepetition. Following trial, the United States Bankruptcy Court for the Northern District of California, Hannah L. Blumenstiel, J., 549 B.R. 222, ruled that debt was nondischargeable, and appeals were taken. The Bankruptcy Appellate Panel, 2017 WL 6553392, affirmed judgment as to debtor-husband, but vacated and remanded as to debtor-wife. On remand, the Bankruptcy Court, Blumenstiel, J., 596 B.R. 675, entered judgment in favor of debtor-wife. Judgment creditor appealed. The Bankruptcy Appellate Panel, 2020 WL 1970506, affirmed. Cross-appeals were taken.

Holdings: The Court of Appeals held that:

[1] collateral estoppel did not bar judgment creditor's nondischargeability claim, and

[2] in ruling that debtor-husband's fraud was not imputed to debtor-wife, the Bankruptcy Court applied the incorrect legal standard for imputed liability in a partnership relationship.

Affirmed in part, reversed in part, and remanded with instructions.

Procedural Posture(s): On Appeal; Judgment.

West Headnotes (2)

[1] **Judgment** Bankruptcy
Collateral estoppel did not bar judgment creditor's nondischargeability claim against Chapter 7 debtors; in judgment creditor's prepetition state-court action against debtors, jury's findings in favor of judgment creditor on his claim for debtors' alleged nondisclosure of material facts, but not on his claim for intentional misrepresentation, were conflicting, or at least ambiguous. 11 U.S.C.A. § 523(a)(2)(A).

[2] **Bankruptcy** Fraud committed by agent or one other than debtor
In judgment creditor's adversary proceeding against Chapter 7 debtors under the fraud discharge exception, in connection with debtors' alleged fraudulent concealment of material defects in renovated house that they sold to him prepetition, the Bankruptcy Court applied the incorrect "knew or should have known" legal standard for imputed liability in a partnership relationship to conclude that debtor-husband's fraud was not imputed to his partner, debtor-

wife; under the correct standard, debtor-wife's debt was nondischargeable regardless of her knowledge of the fraud. 11 U.S.C.A. § 523(a)(2)(A).

2 Cases that cite this headnote

***545** Appeal from the Ninth Circuit Bankruptcy Appellate Panel, Brand, Jury, and Faris, Bankruptcy Judges, Presiding, Taylor, Faris, and Brand, Bankruptcy Judges, Presiding, BAP No. 16-1277, BAP No. 19-1016

Attorneys and Law Firms

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Reno F.R. Fernandez, III, Daniel Vaknin, BKC, Macdonald Fernandez LLP, San Francisco, CA, Iain A. Macdonald, Macdonald & Associates, San Francisco, CA, for Appellees.

Before: McKEOWN and NGUYEN, Circuit Judges, and HUCK, [*] District Judge.

MEMORANDUM [**]

As partners, David and Kate Bartenwerfer renovated a house in San Francisco, California and sold it to Kieran Buckley. Shortly after the sale, Buckley alleged defects in the house and sued the Bartenwerfers in California state court for (1) breach of contract, (2) negligence, (3) nondisclosure of material facts, (4) negligent misrepresentation, and (5) intentional misrepresentation. The jury found in Buckley's favor on his breach of contract, negligence, and nondisclosure of material facts claims and against him on his remaining claims and awarded him damages. The Bartenwerfers filed for bankruptcy.

In the bankruptcy court, Buckley initiated an adversary proceeding against the Bartenwerfers, arguing that the state court judgment against the Bartenwerfers could not be discharged in bankruptcy under 11 U.S.C. § 523(a)(2)(A), which provides ***546** that a debtor cannot discharge debt that was obtained through fraud. The bankruptcy court agreed and held that the portion of the state court judgment that was traceable to Buckley's nondisclosure claim was nondischargable. The bankruptcy court found that the Bartenwerfers intended to deceive Buckley and held that Mr. Bartenwerfer had actual knowledge of the false representations made to Buckley and that Mr. Bartenwerfer's fraudulent conduct could be imputed onto Mrs. Bartenwerfer because of their partnership relationship. Additionally, the bankruptcy court declined to apply collateral estoppel in favor of the Bartenwerfers based on the jury's findings of no intentional fraud. On appeal, the Ninth Circuit Bankruptcy Appellate Panel ("BAP") affirmed the bankruptcy court's collateral estoppel ruling, but, adopting the Eight Circuit's "knew or should have known" standard from *Walker v. Citizens State Bank*, 726 F.2d 452 (8th Cir. 1984), remanded the imputed liability finding and instructed the bankruptcy court to determine whether Mrs. Bartenwerfer "knew or should have known" of Mr. Bartenwerfer's fraud. On remand, after an evidentiary hearing, the bankruptcy court held that Mr. Bartenwerfer's fraud could not be imputed onto Mrs. Bartenwerfer because she did not know of the fraud. The BAP affirmed.

Buckley appeals the BAP's decision affirming the bankruptcy court's nondischargeability judgment in favor of Mrs. Bartenwerfer. On cross-appeal, the Bartenwerfers argue that collateral estoppel should apply to bar Buckley's § 523(a)(2)(A) claim. We have jurisdiction under 28 U.S.C. § 158(d), and we affirm in part and reverse in part.

[1] We begin with the Bartenwerfers' cross-appeal. The Bartenwerfers argue that collateral estoppel applies because the state court jury found in their favor on Buckley's intentional misrepresentation claim. The jury found in favor of Buckley on his nondisclosure of material facts claim against the Bartenwerfers, but not on his intentional misrepresentation claim. These two findings are conflicting, or at least ambiguous, which weigh against applying collateral estoppel. *See* *In re Kelly*, 182 B.R. 255, 258 (9th Cir. BAP 1995) ("Any reasonable doubt as to what was decided by a prior judgment should be resolved against allowing the collateral estoppel effect."), *aff'd*, 100 F.3d 110 (9th Cir. 1996). We affirm on this issue.

[2] In his appeal, Buckley argues that the bankruptcy court erred by failing to apply binding Supreme Court and Ninth Circuit precedent to the question of whether to impute Mr. Bartenwerfer's fraud onto his partner, Mrs. Bartenwerfer, and by holding that the fraud was not imputed. Buckley is correct. Applying basic partnership principles,

> if, in the conduct of partnership business, ... one partner makes false or fraudulent misrepresentations of fact to the injury of innocent persons, ... his partners cannot escape pecuniary responsibility therefor upon the ground that such misrepresentations were made without their knowledge. This is especially so when ... the partners, who were not themselves guilty of wrong, received and appropriated the fruits of the fraudulent conduct of their associate in business.

Strang v. Bradner, 114 U.S. 555, 561, 5 S.Ct. 1038, 29 L.Ed. 248 (1885); *see also* *In re Cecchini*, 780 F.2d 1440, 1444 (9th Cir. 1986) (holding a partner responsible for a tortfeasor/partner's fraud when the fraud was performed "on behalf of the partnership and in the ordinary course of the business of the partnership"), *overruled in other part by* *Kawaauhau v. Geiger*, 523 U.S. 57, 118 S.Ct. 974, 140 L.Ed.2d 90 (1998). Mrs. Bartenwerfer's debt is nondischargeable ***547** regardless of her knowledge of the fraud. By rejecting *Strang* and *Cecchini*, in favor of the "knew or should have known" standard, the bankruptcy court applied the incorrect legal standard for imputed liability in a partnership relationship. We reverse the bankruptcy court's judgment regarding imputed liability against Mrs. Bartenwerfer under § 523(a)(2)(A), and we remand to the bankruptcy court with instructions to enter judgment in favor of Buckley and against Mrs. Bartenwerfer.

We need not address the remaining issues raised on Buckley's direct appeal.

AFFIRMED IN PART; REVERSED IN PART AND REMANDED.

All Citations

860 Fed.Appx. 544

Footnotes

* The Honorable Paul C. Huck, United States District Judge for the U.S. District Court for Southern Florida, sitting by designation.

** This disposition is not appropriate for publication and is not precedent except as provided by Ninth Circuit Rule 36-3.

KeyCite Yellow Flag - Negative Treatment
Disagreed With by In re GFS Industries, LLC, Bankr.W.D.Tex., November 10, 2022

36 F.4th 509
United States Court of Appeals, Fourth Circuit.

IN RE: CLEARY PACKAGING, LLC, Debtor.
Cantwell-Cleary Co., Inc., Plaintiff - Appellant,
v.
Cleary Packaging, LLC, Defendant - Appellee.
Public Justice Center; Legal Aid Justice Center; Mountain State Justice; North Carolina Justice Center; Casa; Centro de los Derechos del Migrante; National Black Worker Center; National Employment Law Project; Farm Labor Organizing Committee, AFL-CIO; United States of America, Amici Supporting Appellant.

No. 21-1981
|
Argued: March 10, 2022
|
Decided: June 7, 2022

Synopsis
Background: Judgment creditor filed adversary complaint against debtor, a limited liability company (LLC) that had elected to proceed under Subchapter V of Chapter 11 as a "small business debtor," seeking declaration that $4.7 million debt arising from its state-court judgment for intentional interference with contracts and tortious interference with business relations was nondischargeable as a debt for "willful and malicious injury." Debtor moved to dismiss for failure to state a claim. The United States Bankruptcy Court for the District of Maryland, Michelle M. Harner, J., 630 B.R. 466, granted motion. Judgment creditor appealed, and its appeal was certified for direct appeal to the Fourth Circuit.

[Holding:] Addressing a matter of apparent first impression for the court, the Court of Appeals, Niemeyer, Circuit Judge, held that the discharge exceptions in Subchapter V of Chapter 11 apply to both individual debtors and corporate debtors.

Reversed and remanded with instructions.

Procedural Posture(s): On Appeal; Motion to Dismiss for Failure to State a Claim; Motion for Summary Judgment; Request for Declaratory Judgment.

West Headnotes (16)

[1] **Bankruptcy** Construction and Operation

A limited liability company (LLC) is a "corporation" within the meaning of the Bankruptcy Code. 11 U.S.C.A. § 101(9)(A).

[2] **Bankruptcy** Debts and Liabilities Discharged

Section of the Bankruptcy Code setting forth the general exceptions to discharge applies to a range of Code discharge provisions and provides that discharges in those specified provisions do not discharge an "individual debtor" from a list of 21 types of debt. 11 U.S.C.A. § 523(a).

[3] **Bankruptcy** Effect as discharge

Section of Bankruptcy Code governing Subchapter V discharge applies to individual and corporate debtors alike, Code provides for court to grant Subchapter V debtor a discharge of all debts except "any debt" "of the kind specified in" section of Code setting forth the general exceptions to discharge, and although introductory language in that general provision limits its discharge exceptions to "individual" debtors, implying that corporations are not subject to the discharge exceptions, combination of terms "debt" and "of the kind" in Subchapter V discharge provision indicates that Congress intended to reference only the list of nondischargeable debts found in Code's general exception-to-discharge provision, not the class of debtors addressed therein, and to the extent there is tension between the two provisions, Subchapter V provision, as the more specific, governs. 11 U.S.C.A. §§ 101(41), 523(a), 1182(1), 1192(2).

2 Cases that cite this headnote

[4] **Bankruptcy** Fairness and Equity; "Cram Down."

In a traditional Chapter 11 proceeding, debtor submits and the court approves a plan of reorganization for distribution of debtor's estate; if creditors withhold their consent, any such plan must be fair and equitable in that it must comply with priority rules that establish a hierarchy of creditor classes for the order in which each class of creditor is to be paid.

1 Case that cites this headnote

[5] **Bankruptcy** Preservation of priority

Pursuant to the absolute priority rule, under any Chapter 11 plan to which creditors have not consented, higher priority creditors are to be paid in full before payment is made to lower priority creditors. 11 U.S.C.A. § 1129(b)(2)(B)(ii).

[6] **Bankruptcy** Preservation of priority

As a general matter, any non-consensual Chapter 11 plan violating the absolute priority rule may not be approved, nor may a discharge of debts be granted. 11 U.S.C.A. § 1129(b)(2)(B)(ii).

[7] **Bankruptcy** In general; nature and purpose

Congress enacted Subchapter V of Chapter 11 in the Small Business Reorganization Act of 2019 in order to streamline reorganizations for small business debtors. Pub. L. No. 116-54, 133 Stat. 1079.

1 Case that cites this headnote

[8] **Bankruptcy** Feasibility in general

One of the main features of a proceeding under Subchapter V of Chapter 11 is its authorization of plans that are not consented to by creditors and that depart from the Bankruptcy Code's absolute priority rule; instead, under the governing rules of a Subchapter V proceeding, the bankruptcy court need only find that such a plan provide that all of the debtor's projected disposable income is paid to creditors for a three-to-five-year period and that it be feasible, thus enabling the owners of a Subchapter V debtor to retain their equity in the bankruptcy estate despite creditors' objections. 11 U.S.C.A. §§ 1129(b), 1191(c)(2)(A) and (3).

1 Case that cites this headnote

[9] **Bankruptcy** Effect as discharge

Under the specific rules for discharge provided in Subchapter V of Chapter 11, a court is required to grant discharge of all debts after approval of the plan except (1) any debt payable after the three-to-five-year period specified for payment, and (2) any debt "of the kind specified in" the section of the Bankruptcy Code setting forth the general exceptions to discharge. 11 U.S.C.A. §§ 523(a), 1192.

[10] **Bankruptcy** Effect as discharge

Subchapter V of Chapter 11 of the Bankruptcy Code provides for the discharge of debts for both individual and corporate debtors. 11 U.S.C.A. § 1192(2).

3 Cases that cite this headnote

[11] **Statutes** General and specific terms and provisions; ejusdem generis

To the extent that tension exists between two statutory provisions, the more specific provision should govern over the more general.

[12] **Bankruptcy** Discharge

In establishing the different Bankruptcy Code chapters, Congress conscientiously defined and distinguished the kinds of debtors covered by each provision; for example, Chapter 7 discharges are explicitly limited to individuals, as are Chapter 13 discharges. 11 U.S.C.A. §§ 109(e), 727(a)(1), 1328.

[13] **Bankruptcy** Effect as discharge

With respect to traditional Chapter 11 proceedings, Congress explicitly distinguished the discharges of individual debtors from the discharges of corporate debtors, excluding a different array of debts from discharge for each. 11 U.S.C.A. § 1141(d).

2 Cases that cite this headnote

[14] **Bankruptcy** Farmers

Under the Bankruptcy Code, Chapter 12 proceedings are limited to family farmers and family fishermen, whether they be individuals or corporations. 11 U.S.C.A. §§ 101(18), 101(19A).

[15] **Bankruptcy** In general; nature and purpose

Congress enacted Subchapter V of the Bankruptcy Code with the primary goal of simplifying Chapter 11 reorganizations for small businesses and reducing the administrative costs for those businesses. Pub. L. No. 116-54, 133 Stat. 1079.

1 Case that cites this headnote

[16] **Bankruptcy** Preservation of priority

Bankruptcy Fairness and Equity; "Cram Down."

Subchapter V proceeding involves a non-consensual plan, that is, a "cram-down" proceeding, in which stakeholders in the bankruptcy estate are treated differently than they would be in traditional Chapter 11 proceedings under the absolute priority rule. 11 U.S.C.A. §§ 1129(b), 1191(c).

***511** Appeal from the United States Bankruptcy Court for the District of Maryland, at Baltimore. Michelle W. Harner, Bankruptcy Judge. (21-10765; 21-00056)

Attorneys and Law Firms

ARGUED: Justin Philip Fasano, MCNAMEE HOSEA, P.A., Greenbelt, Maryland, for Appellant. Robert Joel Branman, UNITED STATES DEPARTMENT OF JUSTICE, Washington, D.C., for Amicus United States. Paul Sweeney, YUMKAS, VIDMAR, SWEENEY & MULRENIN, LLC, Columbia, Maryland, for Appellee. ON BRIEF: Steven L. Goldberg, MCNAMEE HOSEA, P.A., Greenbelt, Maryland, for Appellant. James R. Schraf, YUMKAS, VIDMAR, SWEENEY & MULRENIN, LLC, Columbia, Maryland, for Appellee. Michael R. Abrams, Murnaghan Appellate Advocacy Fellow, PUBLIC JUSTICE CENTER, Baltimore, Maryland, for Amici The Public Justice Center; The Legal Aid Justice Center; Mountain State Justice; The North Carolina Justice Center; CASA; Centro de los Derechos del Migrante; The Farm Labor Organizing Committee, AFL-CIO; The National Black Worker Center; and The National Employment Law Project. David A. Hubbert, Deputy Assistant Attorney General, Joan I. Oppenheimer, Tax Division, UNITED STATES DEPARTMENT OF JUSTICE, Washington, D.C.; Erek L. Barron, United States Attorney, OFFICE OF THE UNITED STATES ATTORNEY, Baltimore, Maryland, for Amicus United States.

Before NIEMEYER, MOTZ, and KING, Circuit Judges.

Opinion

Reversed and remanded with instructions by published opinion. Judge Niemeyer wrote the opinion, in which Judge Motz and Judge King joined.

NIEMEYER, Circuit Judge:

[1] When Cleary Packaging, LLC, filed a petition in bankruptcy under Subchapter V of Chapter 11 as a "small business debtor," seeking to discharge a $4.7 million judgment that Cantwell-Cleary Co., Inc. had obtained against it for intentional interference with contracts and tortious interference with business relations, Cantwell-Cleary opposed the effort. It argued that 11 U.S.C. § 1192(2), which falls within Subchapter V, provides that small business ***512** debtors are not entitled to discharge "any debt ... of the kind specified in section 523(a) of this title," *id.* §

1192(2), and that § 523(a) in turn lists 21 categories of debt that are non-dischargeable, including debts "for willful and malicious injury by the debtor to another entity or to the property of another entity," *id.* § 523(a)(6). Cleary Packaging argued, however, that because § 523(a)'s list of exceptions to dischargeability is applicable only to "individual debtor[s]," its $4.7 million debt as the debt of a corporation was not covered by the exception contained in § 1192(2) and therefore was indeed dischargeable. [1] Cantwell-Cleary responded that because the language of § 1192(2) incorporates *only the list* of debts — debts "*of the kind* specified in section 523(a)" — and *not the class of debtors* addressed by § 523(a), the $4.7 million debt is non-dischargeable as a debt for willful and malicious injury.

The bankruptcy court, in a nicely crafted opinion, agreed with Cleary Packaging and concluded that its $4.7 million debt was indeed dischargeable, reasoning that the exceptions to dischargeability that were incorporated into § 1192(2) from § 523(a) applied only to *individual* debtors. The court relied heavily on the reasoning of *Gaske v. Satellite Restaurants Inc. Crabcake Factory USA (In re Satellite Restaurants Inc. Crabcake Factory USA)*, 626 B.R. 871 (Bankr. D. Md. 2021), which was dismissed on appeal. While the question is a close one, we nonetheless disagree with the bankruptcy court, as explained herein. Accordingly, we reverse the court's ruling and remand.

I

Cantwell-Cleary is a Maryland corporation engaged as a wholesaler of office-related products, particularly packaging supplies, janitorial and sanitation supplies, and paper products. Vincent Cleary Jr., who was on the board of directors of Cantwell-Cleary and its former president and CEO, left the company in June 2018 following a long-running family dispute involving divorce proceedings and internal disagreements over control of the company. He thereafter formed Cleary Packaging, LLC. He took with him numerous employees covered by noncompetition agreements and sensitive customer information and began the new business in competition with Cantwell-Cleary. Shortly thereafter, Cantwell-Cleary commenced an action in the Circuit Court for Anne Arundel County, Maryland, for intentional interference with contracts, tortious interference with business relations, and related claims. On the jury's verdict in favor of Cantwell-Cleary, the state court entered judgment in January 2021 against Cleary Packaging and Vincent Cleary Jr. in the aggregate amount of $4,715,764.98.

Cleary Packaging thereafter filed a petition under Chapter 11 of the Bankruptcy Code, electing to proceed under Subchapter V as a small business enterprise. In its plan for reorganization, it proposed to pay Cantwell-Cleary 2.98 percent of its judgment in biannual installments over a period of five years, for a total of $140,489.77. If the plan were to be approved, the remainder of Cleary Packaging's debt to Cantwell-Cleary would be discharged.

Cantwell-Cleary filed a complaint in the bankruptcy court, seeking a declaratory judgment that the $4.7 million judgment is not dischargeable under ***513** 11 U.S.C. §§ 1192(2) and 523(a). It also sought, by motion for summary judgment, a judgment giving preclusive effect in the bankruptcy court to its state judgment. On Cleary Packaging's motion, the bankruptcy court dismissed Cantwell-Cleary's declaratory judgment action, finding that the discharge exceptions in § 1192(2) and § 523(a) do not apply to *corporate* debtors because of limiting language in § 523(a). Specifically, it held that the § 523(a) list of exceptions to dischargeability applies only to *individual* debtors. Because Cleary Packaging was not an individual, but rather a corporation (in this case, a limited liability company), its debt was therefore not excepted from discharge under § 523(a). Consequently, the court also dismissed Cantwell-Cleary's motion for summary judgment as moot.

On Cantwell-Cleary's motion, the bankruptcy court certified a direct appeal to this court of its "Section 523 Opinion and Order," pursuant to 28 U.S.C. § 158(d)(2)(A)(i), and we authorized the appeal by order dated September 8, 2021. The sole question on appeal, therefore, is whether Cleary Packaging, as a Subchapter V corporate debtor, can discharge its $4.7 million debt to Cantwell-Cleary "for willful and malicious injury."

II

[2] In filing its Chapter 11 petition, Cleary Packaging elected to proceed under Subchapter V, and accordingly its discharge of debts is specifically governed by 11 U.S.C. § 1192(2). That section provides: "If the plan of the debtor is confirmed ...

the court shall grant the debtor a discharge of all debts ... except any debt ... of the kind specified in section 523(a) of this title." Section 523(a), which applies to a range of bankruptcy code discharge provisions, including § 1192, provides that discharges in those specified sections "do[ ] not discharge an *individual debtor* from" a list of 21 types of debt, including a debt "for willful and malicious injury," *implying* that such exceptions do not apply to corporate debtors. 11 U.S.C. § 523(a) (emphasis added).

The parties do not dispute that Cleary Packaging's $4.7 million debt created by entry of the state judgment was "for willful and malicious injury" and therefore would qualify as the type of debt that § 523(a) makes non-dischargeable. *See* 11 U.S.C. § 523(a)(6). Rather, the dispute centers on conflicting interpretations of the two relevant provisions — § 1192(2) and § 523(a) — relating to the *kind of debtor* subject to the discharge exceptions listed in § 523(a). Cleary Packaging, focusing on § 523(a), argues that it limits § 1192(2) discharges with respect to the 21 categories of debt only as to *individual debtors*, and therefore corporate debts of the kind listed remain dischargeable. Cantwell-Cleary, on the other hand, focuses on § 1192(2), which applies to both individual and corporate debtors, and argues that the section excludes from discharge *debts of the kind* listed in § 523(a), regardless of the *class of debtor*, whether individual or corporate. Because § 1192(2) is the specific provision governing discharges in Subchapter V proceedings, Cantwell-Cleary argues that if there is any inconsistency, we should give § 1192(2) precedence over the more general § 523(a) and thereby except Cleary Packaging's $4.7 million debt from a discharge, as it is a type of debt listed in § 523(a).

[3] While we recognize a certain lack of clarity in the relationship between § 1192(2) and § 523(a), we conclude, based on our textual review, the provisions' context in the Bankruptcy Code, and practical and equitable considerations, that Cantwell-Cleary makes the more persuasive argument.

***514** A

[4] **[5]** **[6]** First, by way of background, we note that in a traditional Chapter 11 proceeding, the debtor submits and the court approves a plan of reorganization for the distribution of the debtor's estate. And when the creditors withhold their consent, any such plan must be fair and equitable in that it must comply with priority rules that establish a hierarchy of creditor classes for the order in which each class of creditor is to be paid. Thus, higher priority creditors are paid in full before payment is made to lower priority creditors. The rule began with judicial construction and, beginning in 1978, was included in the Bankruptcy Code. *See* *Norwest Bank Worthington v. Ahlers*, 485 U.S. 197, 202, 108 S.Ct. 963, 99 L.Ed.2d 169 (1988). Known as the "absolute priority rule," it requires that any plan, to which creditors have not consented, must provide that "a dissenting class of unsecured creditors [be paid] in full before any junior class can receive [payment]." *Id.* (citation omitted); *In re Maharaj*, 681 F.3d 558, 562 (4th Cir. 2012); 11 U.S.C. § 1129(b)(2)(B)(ii). And, as a general matter, any non-consensual plan violating the absolute priority rule may not be approved, nor may a discharge of debts be granted. *See* 11 U.S.C. § 1129(b)(2)(B)(ii). It can be readily recognized, however, that this strict priority rule could preclude reorganizations in which continuing management of the bankruptcy estate by a business's owners would be essential to a successful reorganization because such owners' retention of estate property would violate the priority rule.

[7] **[8]** Apparently in response to the problem, at least in part, Congress enacted Subchapter V in the Small Business Reorganization Act of 2019, Pub. L. No. 116–54, 133 Stat. 1079, to streamline reorganizations for small business debtors — defined during the relevant time period as those debtors whose debt is not more than $7.5 million, *see* 11 U.S.C. § 1182(1) (2020). One of the main features of a Subchapter V proceeding is its authorization of plans that are not consented to by creditors and that depart from the absolute priority rule of § 1129(b). Under the governing rules of a Subchapter V proceeding, the bankruptcy court need only find that such a plan provide that all of the debtor's projected disposable income is paid to creditors for a 3-to 5-year period and that it be feasible. 11 U.S.C. § 1191(c)(2)(A) and (3). Thus, the owners of a Subchapter V debtor are able to retain their equity in the bankruptcy estate despite creditors' objections.

[9] Subchapter V also provides specific rules for discharge, requiring a court to grant discharge of all debts after approval of the plan except (1) any debt payable *after* the 3- to 5-year period specified for payment, and (2) any debt "of the kind specified in section 523(a)." 11 U.S.C. § 1192.

B

[10] We now turn to the text of § 1192(2), which specifically governs Cleary Packaging's discharge, to determine the debts dischargeable under Subchapter V. First, we point out that § 1192(2) provides for granting *debtors* a discharge of all debts, subject to stated exceptions. For the purpose of Subchapter V, the term "debtor" was defined during the relevant time period to mean "a *person* engaged in commercial or business activities" that has debt of not more than $7.5 million. 11 U.S.C. § 1182(1) (2020) (emphasis added). "[P]erson" is in turn defined to include both individuals and corporations, *see id.* § 101(41), and "corporation[s]" include limited liability companies, *id.* § 101(9)(A). We thus conclude that § 1192(2) provides for the discharge of ***515** debts for *both* individual and corporate debtors.

Still, even though § 1192(2) applies to both individual and corporate debtors, the question remains whether the exception to such discharges — based on § 1192(2)'s reference to § 523(a) — applies to both individuals and corporations or to only individuals. And that question arises because the introductory language in § 523(a) limits its discharge exceptions to *individual* debtors. Specifically, § 523(a) provides that § 1192, along with five other discharge sections of the Bankruptcy Code, "does not discharge *an individual debtor*" from a list of 21 specified debts, including "any debt ... for willful and malicious injury," 11 U.S.C. § 523(a)(6) (emphasis added), implying that corporations are not subject to the discharge exceptions.

To address the question, we begin by focusing on § 1192(2) as the provision specifically governing discharges in a Subchapter V proceeding and on the scope of its incorporation of § 523(a). Section 1192(2) excepts from discharge "any *debt ... of the kind* specified in section 523(a)." 11 U.S.C. § 1192(2) (emphasis added). The section's use of the word "debt" is, we believe, decisive, as it does not lend itself to encompass the "kind" of *debtors* discussed in the language of § 523(a). This is confirmed yet more clearly by the phrase modifying "debt"— i.e., "of the kind." Thus, the combination of the terms "debt" and "of the kind" indicates that Congress intended to reference only the *list of non-dischargeable debts* found in § 523(a). As the U.S. Government's amicus brief notes, this interpretation of "of the kind" is in line "with the ordinary meaning of the word 'kind' as 'category' or 'sort.' " (Citing American Heritage Dictionary of the English Language (online ed.) (" '[a] group of individuals or instances sharing common traits; a category or sort' "); Merriam-Webster Dictionary (online ed.) (" 'a group united by common traits or interests: CATEGORY' ")). In short, while § 523(a) does provide that discharges under various sections, including § 1192 discharges, do not "discharge *an individual debtor* from any debt" of the kind listed, § 1192(2)'s cross-reference to § 523(a) does not refer to any *kind of debtor* addressed by § 523(a) but rather to a *kind of debt* listed in § 523(a). By referring to the *kind of debt* listed in § 523(a), Congress used a shorthand to avoid listing all 21 types of debts, which would indeed have expanded the one-page section to add several additional pages to the U.S. Code. Thus, we conclude that *the debtors* covered by the discharge language of § 1192(2) — i.e., both individual and corporate debtors — remain subject to the 21 *kinds of debt* listed in § 523(a).

[11] We add — to the extent that one might find tension between the language of § 523(a) addressing individual debtors and the language of § 1192(2) addressing both individual and corporate debtors — that the more specific provision should govern over the more general. *See, e.g., S.W. Ga. Farm Credit, Aca v. Breezy Ridge Farms, Inc. (In re Breezy Ridge Farms, Inc.)*, No. 09-1011, 2009 WL 1514671, at *2 (Bankr. M.D. Ga. May 29, 2009) ("If the two provisions may not be harmonized, then the more specific will control over the general" (quoting *Universal Am. Mortg. Co. v. Bateman (In re Bateman)*, 331 F.3d 821, 825 (11th Cir. 2003))). Thus, while § 523(a) references numerous discharge provisions of the Bankruptcy Code, § 1192(2) is the more specific, addressing only Subchapter V discharges.

C

[12] **[13]** The context of § 1192(2) within the Bankruptcy Code and the Bankruptcy Code's structure further support our interpretation. ***516** It is readily apparent from a review of different Bankruptcy Code chapters that Congress conscientiously defined and distinguished the kinds of debtors covered by each provision. For example, Chapter 7 discharges are explicitly limited to individuals, *see* 11 U.S.C. § 727(a)(1), as are Chapter 13 discharges, *see id.* §§ 109(e), 1328. More tellingly, as to traditional Chapter 11 proceedings, Congress explicitly distinguished the discharges of individual debtors from the discharges of corporate debtors in § 1141(d), excluding a different array of debts from discharge for each. *Compare id.* § 1141(d)(2), (5) (addressing the scope of discharge for individuals) *with id.* § 1141(d)(6) (addressing the scope of discharge for corporations). Yet Congress purposefully addressed both individual and corporate debtors when defining the right of discharge in Subchapter V proceedings. *Id.* § 1192.

Cleary Packaging's interpretation would also create difficulty in reconciling § 523(a) with § 1141(d)(6). Section 523(a) includes in its scope § 1141, just as it includes § 1192 and several other sections, and therefore under Cleary Packaging's interpretation, the list of exceptions to discharge in a traditional Chapter 11 proceeding would govern only individuals by reason of § 523(a)'s limiting language. Yet, § 1141 incorporates specified debts listed in § 523(a) to apply *to corporate debtors*, excluding from discharge debts "of a kind specified in paragraph (2)(A) or (2)(B) of section 523(a)." 11 U.S.C. § 1141(d)(6)(A). Cleary Packaging has been unable to reconcile its method for applying § 523(a) to § 1192 with any consistency as to how it would apply § 523(a) to § 1141(d)(6).

[14] Yet more telling is Congress's importation of language into Subchapter V from the conceptually similar Chapter 12 proceedings, which are limited to family farmers and family fishermen, whether they be individuals or corporations. *See* 11 U.S.C. § 101(18), (19A); *see also, e.g., In re Trepetin*, 617 B.R. 841, 848 (Bankr. D. Md. 2020) (recognizing that "[s]everal aspects of Subchapter V are premised on the provisions of chapter 12 of the Code for family farmers and fishermen").

In addressing the scope of discharge, Chapter 12 provides, in relevant part, that "the court shall grant the debtor a discharge of all debts provided for by the plan ... except any debt ... *of a kind specified in section 523(a)* of this title." 11 U.S.C. § 1228(a) (emphasis added). This language in Chapter 12 is virtually identical to the language included in § 1192(2). [2] Moreover, § 523(a) specifically references § 1228(a) discharges, just as it does § 1192 discharges. Yet, the courts construing the scope of § 1228(a) have concluded that § 1228(a)'s discharge exceptions apply *to both individual debtors and corporate debtors. See, e.g., Breezy Ridge Farms*, 2009 WL 1514671, at *1–2; *New Venture P'ship v. JRB Consol., Inc. (In re JRB Consol., Inc.)*, 188 B.R. 373 (Bankr. W.D. Tex. 1995). Interpreting language virtually identical to that in § 1192(2), the bankruptcy court in *JRB Consolidated* stated that "[t]he wording in § 1228(a)(2) describing 'debts of the kind' specified in § 523(a) does not naturally lend itself to also incorporate the meaning 'for debtors of the kind' referenced in § 523(a)." 188 B.R. at 374. Instead, it stated, "[d]ebts of the kind easily seems to be limited to the subparagraphs of § 523(a) which identify the types of debts which are eligible to be excepted from discharge." *Id.*; *see also Breezy Ridge Farms*, 2009 WL 1514671, at *2 (finding that Congress used the reference to ***517** § 523(a) in § 1228 "as shorthand to define the scope of a Chapter 12 discharge for corporations as well as individuals"). Thus, prior interpretations of § 1228(a) support our interpretation of § 1192(2)'s virtually identical language. *See Hall v. United States*, 566 U.S. 506, 519, 132 S.Ct. 1882, 182 L.Ed.2d 840 (2012) ("[I]dentical words and phrases within the same statute should normally be given the same meaning" (citations omitted)). To give different interpretations to the same language in the same statute would ignore the rationality of using the same language in describing a different proceeding of the Bankruptcy Code, as was done with the adoption of Subchapter V.

[15] Finally, our interpretation of § 1192(2) in Subchapter V makes particular sense when considering that subchapter's juxtaposition in Chapter 11 with traditional Chapter 11 provisions, reflecting its distinctive purpose within that Chapter. Congress enacted Subchapter V as part of the Small Business Reorganization Act of 2019 with the primary goal of simplifying Chapter 11 reorganizations for small businesses and reducing the administrative costs for those businesses. To do so, Congress deliberately altered the general provisions of traditional Chapter 11 proceedings by, among other things, eliminating the absolute priority rule and limiting the applicability of § 1141(d) to Subchapter V proceedings. Section 1141(d), in particular, sets forth debts that are eligible for discharge in a traditional Chapter 11 proceeding, making distinctions between individual debtors and corporate debtors. *See* *Breezy Ridge Farms*, 2009 WL 1514671, at *2; *cf.* *JRB Consol.*, 188 B.R. at 374. In contrast, § 1192 provides benefits to small business debtors, regardless of whether they are individuals or corporations. Thus, an important purpose for Subchapter V would be frustrated were we to adopt Cleary Packaging's interpretation of §§ 1192(2) and 523(a), which would treat individuals and corporations differently.

[16] And as to fairness and equity, it should be recognized that a Subchapter V proceeding involves a non-consensual plan — i.e., a "cram-down" proceeding — in which stakeholders in the bankruptcy estate are treated differently than they would be in traditional Chapter 11 proceedings under the absolute priority rule. Under a Subchapter V plan, owners of a debtor can retain ownership interests to continue conducting the reorganization at the expense of and over the objection of creditors. Given the elimination of the absolute priority rule, Congress understandably applied limitations on the discharge of debts to provide an additional layer of fairness and equity to creditors to balance against the altered order of priority that favors the debtor. To this end, *all Subchapter V debtors* are textually subject to the discharge limitations described in § 523(a), not just *individual* Subchapter V debtors. To make a distinction between individuals and corporations for how Subchapter V is applied would not only undermine that balance, but would also make no sense and indeed would create perverse incentives. But most importantly, it would violate the text of § 1192(2).

III

At bottom, while we recognize that the relationship between § 523(a) and § 1192 might be a bit discordant — or perhaps more accurately, clumsy — we find more harmony from following a close textual analysis and contextual review of § 1192(2) and thus conclude that it provides discharges to small business debtors, *whether they are individuals or corporations*, except with respect to the 21 kinds of debts listed in § 523(a). We would find it difficult to conceive of giving § 523(a) the additional ***518** role of defining *the debtors* covered by § 1192(2) in conflict with § 1192(2)'s own language. That function is actually and better carried out by § 1192, which is the specific provision governing discharges in Subchapter V proceedings and which applies to individual and corporate debtors alike. Finally, we conclude that our interpretation serves fairness and equity in circumstances where *a small business corporate debtor* in particular is given greater priority over creditors than would ordinarily apply and thus should not especially benefit from the discharge of debts incurred in circumstances of fraud, willful and malicious injury, and the other violations of public policy reflected in § 523(a)'s list of exceptions.

* * *

Accordingly, we reverse the bankruptcy court's certified order and remand the case for further proceedings, including consideration of Cantwell-Cleary's motion for summary judgment.

REVERSED AND REMANDED

All Citations

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Footnotes

1 While, for convenience, we use the terms "individual debtor" and "corporate debtor" in a binary fashion, we recognize that Cleary Packaging is a limited liability company under Maryland law. The Bankruptcy Code,

however, includes within its definition of "corporation" limited liability companies. *See* 11 U.S.C. § 101(9)(A).

2 There is one inconsequential difference — § 1228(a) refers to debt "of *a* kind specified," while § 1192(2) refers to debt "of *the* kind specified."

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647 B.R. 337
United States Bankruptcy Court,
W.D. Texas, San Antonio Division.

IN RE: GFS INDUSTRIES, LLC, Debtor.
Avion Funding, LLC, Plaintiff,
v.
GFS Industries, LLC, Defendant.

CASE NO. 22-50403-cag
|
ADV. NO. 22-05052-cag
|
Signed November 10, 2022

Synopsis
Background: Creditor filed complaint for determination of dischargeability of Chapter 11 debtor's debt. Debtor moved to dismiss.

Holdings: The Bankruptcy Court, Craig A. Gargotta, J., held that:

[1] on issue of first impression, exceptions to discharge in bankruptcy apply to discharge under Subchapter V, but only as to individual debtors;

[2] limits on dischargeability did not apply to Subchapter V debtor; and

[3] discharge exceptions did not apply to confirmed nonconsensual plan.

Motion granted.

Procedural Posture(s): Motion to Dismiss for Failure to State a Claim.

West Headnotes (12)

[1] **Bankruptcy** Pleading; dismissal

A claim for relief is plausible on its face when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged. Fed. R. Civ. P. 8; Fed. R. Bankr. P. 7008.

[2] **Bankruptcy** Pleading; dismissal

A motion to dismiss may be granted either because a legal remedy based on the alleged facts does not exist or because the facts as alleged, even if true, do not satisfy the legal requirements of the pleaded cause of action. Fed. R. Civ. P. 12(b)(6); Fed. R. Bankr. P. 7012.

[3] **Bankruptcy** Pleading; dismissal

The heightened pleading standard for cases in which fraud is alleged requires the plaintiff to plead the who, what, when, where, and why as to the fraudulent conduct. Fed. R. Civ. P. 9(b); Fed. R. Bankr. P. 7009.

[4] **Bankruptcy** Corporations

A corporate Subchapter V debtor may be granted a discharge of debts provided the debtor meets the statutory requirements. 11 U.S.C.A. § 1192.

[5] **Bankruptcy** Discharge

Exceptions to discharge in bankruptcy applied to discharge under Subchapter V, but only as to individual debtors. 11 U.S.C.A. §§ 523(a)(2)(A), 523(a)(2)(B), 1192.

[6] **Statutes** Superfluousness

When interpreting statutes, courts should lean in favor of construction which will render every word operative, rather than one which may make some idle and nugatory.

[7] **Bankruptcy** Debts and Liabilities Discharged

Exceptions to discharge applied only to individuals, not to corporations. 11 U.S.C.A. § 523.

[8] **Bankruptcy** Corporations

Limits on dischargeability did not apply to Chapter 11, Subchapter V, debtor, since debtor was not individual debtor. 11 U.S.C.A. §§ 523, 727.

[9] **Bankruptcy** Corporations

Corporate debtors proceeding under Subchapter V cannot be made defendants in dischargeability actions. 11 U.S.C.A. §§ 523, 1192.

[10] **Bankruptcy** Corporations

Chapter 11 Subchapter V case of business continuing to operate past confirmation of nonconsensual plan as means to fund plan that did not contemplate liquidating property of estate could not be treated as if it were Chapter 7 case to measure debtor's conduct against list of nondischargeable actions under Chapter 7. 11 U.S.C.A. §§ 1141, 1141(d)(3)(C), 1192.

[11] **Bankruptcy** Dischargeable Debtors

Conduct that would deny a debtor's discharge under Chapter 7 is incorporated into Chapter 11 cases; therefore, a court may treat a Subchapter V case as if it were a Chapter 7 case and measure the debtor's conduct against the list of nondischargeable actions under Chapter 7. 11 U.S.C.A. §§ 727, 1141(d)(3)(C).

[12] **Bankruptcy** Corporations

Non-individual debtors are excepted from discharge under Chapter 7. 11 U.S.C.A. § 727(a)(1).

Attorneys and Law Firms

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ORDER GRANTING DEFENDANT GFS INDUSTRIES, LLC'S FIRST AMENDED RULE 12(b)(6) MOTION TO DISMISS PLAINTIFF'S COMPLAINT (ECF NO. 6)

CRAIG A. GARGOTTA, CHIEF UNITED STATES BANKRUPTCY JUDGE

Came on to be considered Defendant GFS Industries, LLC's First Amended Rule 12(b)(6) Motion to Dismiss Plaintiff's Complaint ("Motion to Dismiss") (ECF No. 6) [1] . The Motion to Dismiss seeks to dismiss with prejudice Plaintiff's Original Complaint for Determination of Dischargeability of Debt Pursuant to 11 U.S.C. § 523(a)(2) & (4) ("Complaint") (ECF No. 1). In response, Plaintiff Avion Funding, LLC filed Plaintiff's Opposition to Defendant's First Amended Rule 12(b)(6) Motion to Dismiss Plaintiff's Complaint ("Response") (ECF #7). The Court took the matter under advisement without the necessity of a hearing. For the reasons stated below, the Court GRANTS the Motion to Dismiss.

JURISDICTION

This Court has jurisdiction over the Motion to Dismiss pursuant to 28 U.S.C. § 1334(b). Plaintiff's dischargeability claims are deemed a core proceeding under 28 U.S.C. § 157(b)(2)(I). Venue is proper under 28 U.S.C. §§ 1408 and 1409. The statutory predicate for relief is Federal Rule of Civil Procedure ("Rule(s)") 12(b)(6), made applicable to this proceeding through Fed. R. Bankr. P. 7012 and Local Rule 7012. This matter is referred to this Court pursuant to the District Court's Order of Reference.

BACKGROUND

Debtor GFS Industries, LLC ("Debtor" or "GFS") provides cleaning and environmental services to commercial tenants. As a result of the COVID pandemic, GFS anticipated that the increased demand for sanitation and cleaning services would enable its business to grow. GFS attempted to expand its business to meet the forecasted demand. With the burden of increased administrative costs, GFS resorted to seeking funding through Merchant Cash Advances ("MCA"). Because MCAs require factoring of future account receivables at a discount, GFS was unable to service its operations without sufficient cash flow. Accordingly, GFS filed bankruptcy under the Subchapter V Chapter 11 provisions of Title 11, § 1181 [2] *et seq*. on April 21, 2022.

The instant adversary proceeding was filed by one of GFS's MCA lenders, Avion Funding, LLC ("Avion"). Avion alleges that GFS made material misrepresentations concerning whether a bankruptcy filing was imminent and failed to disclose the existence of other, more senior, MCA lenders from which GFS obtained funding. As a result of these misrepresentations and ***340** nondisclosures, Avion claims that it has been harmed and seeks relief in the form of a declaration that the debt GFS owes to Avion be deemed nondischargeable.

LEGAL STANDARD

Rule 12(b)(6)

[1] **[2]** To survive a Rule 12(b)(6) motion to dismiss, a complaint must contain sufficient facts to state a claim to relief that is plausible on its face. ***Gonzalez v. Kay***, 577 F.3d 600, 603 (5th Cir. 2009) (quoting ***Ashcroft v. Iqbal***, 556 U.S. 662, 678, 129 S.Ct. 1937, 173 L.Ed.2d 868 (2009)). A claim for relief is plausible on its face "when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." ***Iqbal***, 556 U.S. at 678, 129 S.Ct. 1937. In reviewing whether the complaint sufficiently states a claim on which relief may be granted, the Court must accept all well-pleaded facts as true and view those facts in the light most favorable to the plaintiff. ***Thompson v. City of Waco, Tex.***, 764 F.3d 500, 502–03 (5th Cir. 2014). A court should dismiss a complaint if it appears beyond doubt that the plaintiff can prove no set of facts which would entitle him to relief. ***Bell Atl. Corp. v. Twombly***, 550 U.S. 544, 570, 127 S.Ct. 1955, 167 L.Ed.2d 929 (2007). In sum, a Rule 12(b)(6) motion to dismiss "may be granted either because a legal remedy based on the alleged facts does not exist or because the facts as alleged, even if true, do not satisfy the legal requirements of the pleaded cause of action. ***In re Rosetti,*** No. 07-04063-DML, 2007 WL 2669265 (Bankr. N.D. Tex. September 6, 2007).

Rule 9

[3] Though most causes of action are subject to Rule 8(a)'s pleading standard, Rule 9(b) establishes a heightened pleading standard for cases in which the Plaintiff alleges fraud. Under Rule 9(b), fraud claims must be alleged with particularity concerning the circumstances of the fraud. Fed. R. Civ. P. 9(b). Rule 9(b) requires the plaintiff to "plead the who, what, when, where, and why as to the fraudulent conduct." ***Life Partner Creditors' Tr. v. Crowley (Matter of Life Partners Holdings, Inc.),*** 926 F.3d 103, 117 (5th Cir. 2019).

The Court notes that the Motion to Dismiss makes no mention of and provides no argumentation on Rule 9's heightened pleading standard or whether the Complaint satisfies that standard. Instead, the Motion to Dismiss argues that the Complaint does not measure up to the standards set forth in Rule 8. Rule 9, rather than Rule 8, is the measuring stick in cases in which fraud is alleged. Fed. R. Civ. P. 9 ("In alleging fraud or mistake, a party must state with particularity the circumstances constituting fraud or mistake"). Here, the Court must apply Rule 9 because the Complaint alleges fraudulent behavior in all six counts. Consequently, any determinations as to factual sufficiency are made using the standard set forth in Rule 9.

DISCUSSION

In its Complaint, Avion alleges six causes of action under §§ 523, 727, and 1141 that all arise from the same operative facts. The Motion to Dismiss argues that Avion cannot prevail as a matter of law because none of the statutory predicates for the relief sought apply to GFS as a corporate Subchapter V debtor. Conversely, Avion urges that the plain language of the statutes makes these adversary claims cognizable.

In 2019, Congress passed the Small Business Debtor Reorganization Act from which Subchapter V of Chapter 11 was born. Commentators and courts have determined that the legislation's purpose is ***341** to provide recourse to small business owners and individual debtors without the attendant costs and restraints imposed in traditional Chapter 11 cases. Notably, Subchapter V cases do not require the payment of US Trustee fees, filing of a disclosure statement, or application of the absolute priority rule. These changes have largely proven beneficial to those debtors who are able to take advantage of them.

Given the novelty of Subchapter V, courts continue facing important issues regarding its interpretation and implementation. As such, case law concerning the provisions of Subchapter V is lacking. Thus, the Court observes an important threshold issue present in this case: whether a corporate debtor can be granted a discharge in a Subchapter V case. [3] While the answer may seem obvious and unworthy of discussion, the newness of Subchapter V bares a close analysis of its provisions and their application. Indeed, dischargeability actions are moot if the debtor is not eligible for discharge or has voluntarily waived its discharge. In summary form, the validity of Avion's causes of action rely on the subtle—yet critical—assumption that GFS is entitled to a discharge at all. The Court will address the threshold discharge issue before analyzing each cause of action in turn.

I. ***Does a Corporate Subchapter V Debtor Receive a Discharge of its Debts?***

There are two statutes that control the discharge of debts for a corporate Subchapter V debtor: §§ 1141(d) and 1192. The answer to which statute controls a specific debtor's discharge is based on the character of that debtor's confirmed plan. If the plan is consensual, § 1141(d) governs. If, as here, the plan is nonconsensual and thus is confirmed under § 1191(b), then § 1192 controls the fate of the Subchapter V debtor's discharge. After reviewing the language in § 1192, the Court observes that the plain language of the statute contemplates granting corporate Subchapter V debtors a discharge of its debts.

Section 1192 states, "[i]f the plan of the debtor is confirmed under section 1191(b) of this title...the court shall grant the debtor a discharge of all debts provided in section 1141(d)(1)(A) of this title, and all other debts allowed under section 503 of this title and provided for in the plan." The operative statute uses the term "debtor" to describe those who receive discharges under § 1192. The term "debtor" is defined in § 101(13) as a "person or municipality concerning which a case under this title is commenced." The term "person" is also defined in § 101 at subsection (41) as including "individual, partnership, and corporation." Based on this language, it is evident that the term "debtor" in § 1192 encompasses corporations, not just individuals.

[4] Notably, § 1192 does not contain a carve-out provision for non-individual debtors like the similarly drafted § 727(a)(1), which explicitly excludes non-individual debtors from discharge under Chapter 7. It provides, "(a) the court shall grant the debtor a discharge, unless— (1) the debtor is not an individual." 11 U.S.C. § 727(a)(1). Because § 1192 does not contain any provision that would preclude non-individual debtors from obtaining a discharge, the Court holds that the plain language of ***342** § 1192 grants a corporate Subchapter V debtor a discharge of debts provided the debtor meets the statutory requirements. [4] Having established that corporate debtors can receive a discharge in Subchapter V, the Court will now analyze whether Avion can properly file this adversary to seek denial of discharge of its debt.

II. ***Claims Under § 523(a)***

[5] Avion brings two causes of action against GFS under § 523(a)(2) based on fraudulent behavior and misrepresentations it alleges GFS made when obtaining financing from Avion. The statutory predicates for these claims are § 523(a)(2)(A) and (a)(2)(B), respectively. To the extent the parties argue about the factual sufficiency of the claims pled, the Court concludes that there is sufficient factual content to survive a motion to dismiss. Consequently, the Court will focus its analysis on the legal sufficiency of the claims under § 523.

GFS posits that Avion's claims under § 523 must be dismissed as a matter of law because § 523(a) applies only to individual debtors, not corporate debtors. Avion, on the other hand, argues that § 1192's use of the generic term "debtor" means that for Subchapter V purposes, § 523(a) applies to both individual and corporate debtors. The issue, therefore, is whether corporate Subchapter V debtors may be held liable for § 523 claims. The Court observes that this is a case of first impression in this Circuit. For the reasons stated below, the Court determines that the interplay between §§ 1192(2) and 523(a) compels the conclusion that in the Subchapter V context, only individuals, not corporations, can be subject to § 523(a) dischargeability actions.

a. The Applicability of § 523(a) to Corporate Subchapter V Debtors

As with any statutory interpretation exercise, the starting point for the analysis is the statute itself. Here, the pertinent statutes requiring interpretation are §§ 1192 and 523(a). § 1192 states, "the court shall grant the debtor a discharge of all debts provided in section 1141(d)(1)(A)." The statute goes on to except from discharge those debts that are "of the kind specified in section 523(a) of this title." 11 U.S.C. § 1192(2). On its face, § 1192(2) seeks to incorporate the list of debts that are deemed nondischargeable found in § 523(a), without regard for the character of the debtor. In the Court's judgment, however, the preamble to § 523(a) is critical to the analysis. Importantly, § 523(a) contains limiting language, stating that "[a] discharge under section 727, 1141, 1192, 1228(a), 1228(b), or 1328(b) of this title does not discharge an *individual* debtor from any debt..." (emphasis added). Based on this language, the Court makes three observations concerning the interplay between §§ 1192 and 523.

First, § 1192(2)'s reference to § 523(a) only incorporates the list of nondischargeable debts, without expanding it. In other words, the language of § 1192(2) does not intend to except from discharge any debts that § 523(a) does not already except. Because § 523(a) unequivocally applies only to individuals, the language of § 1192(2) does not empower § 523(a) to cast a wider net than the text of § 523(a) permits. Had Congress included a phrase in § 1192(2) ***343** explicitly stating that the list found in § 523(a) applies to all debtors proceeding in Subchapter V, then the interpretation would be straightforward. Congress's choice not to insert this language is instructive.

Moreover, if Congress intended the list of debts to be applicable to corporate debtors, it knew how, because it did so in § 1141(d). Section 1141(d)(6) states: "the confirmation of a plan does not discharge *a debtor that is a corporation* from any debt (A) of the kind specified in paragraph 2(A) or 2(B) of section 523(a) that is owed to a governmental unit..."(emphasis added).[5] Similarly, § 1141(d)(2) states: "A discharge under this chapter does not discharge a debtor *who is an individual* from any debt excepted from discharge under section 523 of this title." (emphasis added). This language is evidence that Congress knew, when it drafted § 1192(2), how to distinguish dischargeability based on the type of debtor. Congress did not make this distinction in § 1192(2). Thus, in order to determine to which debtors § 1192(2) refers, one must look to the language of § 523(a), which unequivocally applies only to individuals.

Second, the inclusion of § 1192 in § 523(a) would be rendered meaningless under any other interpretation. When Subchapter V was passed, Congress also amended § 523(a) to add the newly enacted § 1192 to the list of discharge provisions incorporated in the scope of § 523(a)'s discharge exceptions. § 523(a) now reads, "[a] discharge under section...*1192*...does not discharge an individual debtor..." (emphasis added). Section 1192's addition is vital to the analysis because it evinces Congress's intent. Section 1192(2) as written makes § 523 discharge exceptions applicable to "debtors" without regard to whether the debtor is an individual or a corporation. Critically though, had Congress intended § 523(a) exceptions to apply to entities as well, it would be unnecessary to add § 1192 to a statute that plainly applies to individual debtors only. The fact that Congress added § 1192 into § 523 demonstrates that Congress intended § 1192(2) to limit the § 523 exceptions in Subchapter V to individuals only.

[6] This conclusion is mandated by the canon of statutory construction against surplusage. When interpreting statutes, courts should "lean in favor of a construction which will render every word operative, rather than one which may make some idle and nugatory." Antonin Scalia & Bryan A. Garner, Reading Law: The Interpretation of Legal Texts 69, 174 (2012) (citing Thomas M. Cooley, *A Treatise on the Constitutional Limitations Which Rest upon the Legislative Power of the States of the American Union* 58 (1868)). Here, interpreting § 523 as excepting from discharge debts of corporate debtors in Subchapter V would be to ignore the import of § 1192 into § 523(a). The Court believes the correct interpretation is one which gives meaning to the amendment to § 523. This position compels the Court to conclude that discharge exceptions found in § 523 apply to an § 1192 discharge, but only as to individual debtors.

[7] **[8]** Third, corporate debtors proceeding under Chapter 11 historically have been immune to dischargeability actions under § 523(a). It is well-settled law in this circuit that the § 523 exceptions to discharge apply only to individuals, not to ***344** corporations. *See* ***Garrie v. James L. Gray, Inc.,*** 912 F.2d 808, 812 (5th Cir. 1990) ("the 'willful and malicious injury' exception to discharge, like all of the exceptions to discharge found in section 523(a), applies only to individual, not corporate debtors") (citing ***Yamaha Motor Corp., U.S.A. v. Shadco, Inc.,*** 762 F.2d 668, 670 (8th Cir. 1985)). As this Court itself has explained, it is clear from the language of the Chapter 11 discharge statutes "that corporate debtors in Chapter 11 are not subject to a complaint to determine dischargeability of debt under § 523(a)." ***New Venture Partnership v. JRB Consolidated, Inc. (In re JRB Consolidated, Inc.)***, 188 B.R. 373, 374 (Bankr. W.D. Tex. 1995). For Congress to suddenly depart from this well-established principle when it enacted Subchapter V defies reason.[6] It is much more likely, and confirmed by the language used in Subchapter V, that Congress intended to expand, not discontinue, the principle that Chapter 11 corporate debtors are not subject to § 523(a) complaints to determine dischargeability. Because Subchapter V is merely a subchapter to the broader Chapter 11, this is the required result.

More compelling, the provisions governing Chapter 11 discharge imply that § 523(a) should not apply to corporate debtors. Section 1141(d)(2) states, "[a] discharge under this chapter does not discharge a debtor *who is an individual* from any debt excepted from discharge under section 523 of this title." (emphasis added). Had Congress intended that corporate debtors also be held to the provisions of § 523(a), then clarifying that only individuals under Chapter 11 are liable for § 523 exceptions to dischargeability makes little sense.

[9] In sum, the statutory language along with the broader Chapter 11 statutory scheme mandate this Court's holding that corporate debtors proceeding under Subchapter V cannot be made defendants in § 523 dischargeability actions. Avion's claims under § 523, therefore, must be dismissed for a lack of legal foundation.

b. This Court's Previous Decision Regarding § 523 Discharge Exceptions in Chapter 12

In concluding that Subchapter V corporate debtors cannot be made defendants in § 523 dischargeability actions, the Court is mindful of its previous opinion deciding a similar issue regarding § 523(a)'s relationship with Chapter 12 discharges. Some courts and commentators have cited this Court's decision in ***In re JRB Consolidated, Inc.***, 188 B.R. 373, arguing that the Court's reasoning allowing a § 523(a) dischargeability action against a corporation in Chapter 12 should be extended with regard to Subchapter V because the language of § 1228(a) (controlling discharge in Chapter 12 cases) and § 1192(2) is substantially similar. ***In re Cleary Packaging, LLC,*** 36 F.4th 509, 516 (4th Cir. 2022); 5 Norton Bankr. L. & Prac. § 107:19 (3d ed. 2021); William L. Norton, III and James B. Bailey, ***345** *The Pros and Cons of the Small Business Reorganization Act of 2019*, 36 EMORY BANKR. DEV. J. 383, 386, n. 25 (2020). For the following reasons, the Court believes that its decision in the instant case disallowing dischargeability actions under § 523 as to corporations in Subchapter V can be harmonized with its previous decision in ***In re JRB Consolidated, Inc.***

In ***In re JRB Consolidated, Inc.***, a creditor filed a complaint to determine dischargeability under §§ 523(a)(2) and 523(a)(6) against the debtor, which was a corporation proceeding under Chapter 12. 188 B.R. at

373. The debtor filed a motion to dismiss the complaint on the grounds that § 523(a) did not apply to corporate Chapter 12 debtors, due to § 523(a)'s explicit application to individuals only. *Id.* The Court denied the motion to dismiss, holding that, for the purposes of Chapter 12, the exceptions to discharge found in § 523(a) apply to corporate debtors, not just individual debtors. *Id.* Judge Kelly arrived at this conclusion by examining the interplay of §§ 1228 and 523(a).

The Court began its analysis by comparing discharges in Chapter 11 to discharges in Chapter 12. *Id.* at 374. The Court noted that Chapter 11 provides, "a discharge under this chapter does not discharge a debtor who is an individual from any debt excepted from discharge under section 523 of this title." 11 U.S.C. § 1141(d)(2). In contrast, Chapter 12's incorporation of § 523 is broader, making the § 523(a) exceptions to discharge applicable to "the debtor" without distinction between corporate debtors and individual debtors: "the court shall grant the debtor a discharge of all debts...except any debt— (2) of the kind specified in section 523(a) of this title." 11 U.S.C. § 1228(a)(2). This distinction convinced Judge Kelly that no inconsistency existed between § 1228(a)'s broader application and the limited application of § 523(a) because "individual debtors are still subject to the § 523(a) exceptions" under Chapter 12. *Id.* Thus, Judge Kelly held that § 1228(a) "does not incorporate the limiting definition found in the introductory paragraph of § 523(a)." *Id.*

The Court recognizes the similarities between the language of §§ 1228(a)(2) and 1192(2). Despite the similar language, the Court does not find its decision in this case as inconsistent with the ruling in ***In re JRB Consolidated***. Critical to Judge Kelly's decision was the difference between the operation of Chapter 11 corporate discharges and Chapter 12 corporate discharges. Judge Kelly pointed out that the provisions of Chapter 11 are narrower, only excepting from discharge 1) a liquidating corporate debtor that would otherwise be denied a discharge under § 727(a) (§ 1141(d)(3)); and 2) individual Chapter 11 debtors who have debts of the kind enumerated in § 523(a) (§ 1141(d)(2)). Given the limited exceptions to discharge in Chapter 11, Judge Kelly observed that "it seems clear from that language that corporate debtors in Chapter 11 are not subject to a complaint to determine dischargeability of debt under § 523(a)." *Id.* at 374. Because Subchapter V is not its own chapter of bankruptcy, but rather is a subchapter of Chapter 11, Judge Kelly's analysis regarding Chapter 11 discharges remains applicable to the case here.

Furthermore, Judge Kelly recognized the uniqueness of Chapter 12, stating that the broad language of § 1228(a), "would appear to be consistent with the intent of Congress to provide special treatment for certain kinds of debtors otherwise eligible to file for Chapter 12." *Id.* In short, because Chapter 12 is only available to a small and specific subset of debtors, Chapter 12 cases have unique considerations that are not present in a Chapter 11 case. Therefore, the Court is not mandated to ***346** extend the holding that Chapter 12 corporate debtors are subject to § 523 dischargeability actions into Subchapter V notwithstanding the similar language between §§ 1228(a) and 1192(2).

c. Decisions of Other Bankruptcy Courts

To date, four bankruptcy courts have decided this precise issue. All four bankruptcy courts have held that the § 523(a) exceptions to discharge are applicable only to individuals, not corporations in Subchapter V. ***Jennings v. Lapeer Aviation, Inc. (In re LaPeer Aviation, Inc.),*** Adv. No. 22-03002, 2022 WL 1110072 (Bankr. E.D. Mich. Apr. 13, 2022); ***Catt v. Rtech Fabrications, LLC (In re Rtech Fabrications LLC),*** 635 B.R. 559 (Bankr. D. Idaho 2021); ***Cantwell-Cleary Co., Inc., v. Cleary Packaging (In re Cleary Packaging, LLC),*** 630 B.R. 466 (Bankr. D. Md. 2021), *rev'd* 36 F.4th 509 (4th Cir. 2022); ***Gaske v. Satellite Rest., Inc. Crabcake Factory USA (In re Satellite Rest., Inc. Crabcake Factory USA),*** 626 B.R. 871 (Bankr. D. Md. 2021). All four decisions granted motions to dismiss under Rule 12(b)(6) for failure to state a claim upon which relief can be granted. The Court agrees with the rationales of the courts as explained below.

The bankruptcy courts deciding this issue have been unanimous in pointing out that the limiting language of § 523(a) is dispositive of the issue. As the court in ***In re Lapeer Aviation, Inc.*** observed, "the first sentence of § 523(a) clearly limits the denial of discharge to 'an individual debtor.' " 2022 WL 1110072 at *2. The court goes on to cite numerous pre-Subchapter V cases from across the country to support this proposition. *See* ***id.*** (citing ***In re MF Glob Holdings, Ltd.,*** No-11-15059(MG) 2012 WL 734175 at *3 (Bankr. S.D.N.Y. Mar. 6, 2012)); ***Savoy Records Inc. v. Trafalgar Assocs. (In re Trafalgar Assocs.)*** 53 B.R. 693, 696 (Bankr. S.D.N.Y. 1985); ***Williams v. Sears Holding Co.,*** No. 06-PWG-455-M, 2008 WL 11424255 at *5 (N.D. Ala. Mar. 28 2008); ***Garrie,*** 912 F.2d at 812. As such, the ***Lapeer Aviation*** court found it prudent to expand the reasoning that the preamble to § 523(a), and its limitation to individuals, applies in Subchapter V cases. As discussed above, this Court also finds this limitation applicable to Subchapter V.

Next, the bankruptcy courts have all invoked the canon of statutory interpretation which requires that every word in the statute should be given meaning. The bankruptcy courts explain that "the reference to Section 1192 added to Section 523(a) by [Subchapter V] must be given meaning, and the only reasonable meaning is that Congress intended to continue to limit the application of the Section 523(a) exceptions in a Subchapter V case to individuals." ***In re Satellite Rest., Inc.,*** 626 B.R. at 876. The Court finds this reasoning sound and incorporates it herein.

The bankruptcy courts have also analyzed the history of the corporate discharge in Chapter 11. The courts have pointed out that the corporations were subject to discharge exceptions as far back as 1898. ***In re Rtech Fabrications, LLC,*** 635 B.R. at 565 (citing ***In re Cleary Packaging, LLC,*** 630 B.R. at 474). Congress pivoted from that scheme when it introduced the Bankruptcy Code in 1978, by intentionally removing causes of action that enabled creditors to seek a determination of dischargeability against a corporate debtor in Chapter 11. ***In re Cleary Packaging, LLC,*** 630 B.R. at 474. The only exception to discharge for corporations in the current version of the Bankruptcy Code is found in § 1141(d)(6). This exception was controversial enough that it took eight years to be enacted. ***Id.*** Given this ***347** history, according to the ***Cleary Packaging*** bankruptcy court, "the suggestion that Congress incorporated 19 new exceptions to discharge for small corporations in a bill that was introduced in April 2019, and signed into law by the President in August 2019, seems not only improbable, but also contradicts years of bankruptcy law and policy." ***Id.*** at 475. The Court finds this reasoning persuasive.

Finally, the ***Cleary Packaging*** court identified the fact that § 523(a)—and § 1192 more broadly—only comes into play, with respect to a corporate debtor, if the confirmed plan was a nonconsensual one. ***Id.*** It makes little sense for Congress to except from discharge debts of the kind specified in § 523 as to Debtor A whose plan is nonconsensual but not as to Debtor B whose plan is consensual. This struck the court as a result that "is arbitrary and undermines the equality principles of creditor treatment under the Code." ***Id.*** at 476. This Court agrees.

d. The Fourth Circuit's Opinion in *In re Cleary Packaging, LLC*

The Fourth Circuit, in reversing the bankruptcy court, considered the statutes at issue and determined that Congress intended to make § 523(a) exceptions to discharge applicable to all debtors proceeding under Subchapter V. To support this conclusion, the Fourth Circuit makes six primary arguments based on an analysis of the text, an examination of the purpose Subchapter V, as well as a discussion concerning fairness and equity.

At the outset, the Fourth Circuit proclaimed that "[t]he section's use of the word 'debt' is, we believe, decisive, as it does not lend itself to encompass the 'kind' of *debtors* discussed in the language of § 523(a)." ***In re Cleary Packaging, LLC,*** 36 F.4th at 515 (emphasis in original). Further, the court reasoned that "§ 1192(2)'s cross-reference to § 523(a) does not refer to any *kind of debtor* addressed by § 523(a) but rather to a *kind of debt* listed in § 523(a)." ***Id.*** This Court does not necessarily disagree with the idea that the word debt does not require considering the kind of debtor. Indeed, had § 523(a) not been amended to include § 1192 in its limiting language, the Fourth Circuit's interpretation could be correct. Congress did, however, amend

§ 523(a) to include § 1192 into the limiting language, which in the Court's view, changes the result.

In addressing this point, the Fourth Circuit countered that "to the extent that one might find tension between the language of § 523(a) addressing individual debtors and language of § 1192(2) addressing both individual and corporate debtors —that the more specific provision should govern over the more general." *Id.* (citing ***S.W. Ga. Farm Credit, Aca v. Breezy Ridge Farms, Inc. (In re Breezy Ridge Farms, Inc.),*** No. 09-1011, 2009 WL 1514671, at *2 (Bankr. M.D. Ga. May 29, 2009)). Because § 1192(2) applies only to Subchapter V, whereas § 523(a) applies to all chapters of the Bankruptcy Code, the Fourth Circuit concluded that § 1192(2)'s inclusion of all debtors should control. In this Court's judgment, the Fourth Circuit misapplied this principle. The "general/specific" canon only applies "when conflicting provisions simply cannot be reconciled—when the attribution of no permissible meaning can eliminate the conflict." Scalia & Garner, *supra,* at 183. To reiterate, the Court believes its interpretation maintains harmony between §§ 523(a) and 1192(2). This is mostly because of § 1192(2)'s appearance in the text of § 523(a). Thus, this Court disagrees with the Fourth Circuit's application of the canon.

Next, the Fourth Circuit found support for its decision in the scope of discharge found in other chapters of the Bankruptcy ***348** Code. For example, Chapter 13 and Chapter 7 discharges are only available to individuals. Chapter 11 discharges are available to both individuals and corporations, but Congress was explicit in "excluding a different array of debts from discharge" for each type of debtor. ***In re Cleary Packaging, LLC,*** 36 F.4th at 516. The Fourth Circuit concludes that, because "Congress conscientiously defined and distinguished the kinds of debtors covered by each provision" then its decision to have the discharge provision in Subchapter V apply to both individuals and non-individuals is evidence that Congress intended individuals and non-individuals' discharge under Subchapter V to be treated the same. ***Id.***

While plausible, the history of Chapter 11 corporate discharge supports the opposite conclusion. As discussed above, corporations have not been subject to § 523(a) exceptions to discharge since the inception of the Bankruptcy Code, in part to soothe problems with implementing a corporate exception to discharge that arose under the previous scheme. ***In re Rtech Fabrications, LLC,*** 635 B.R. at 565 (citing ***In re Cleary Packaging, LLC,*** 630 B.R. at 474). Given this history, Judge Paul Bonapfel remarks that "it is difficult to conclude that, in enacting a statute universally proclaimed to have the purpose of facilitating reorganization of small businesses, by among other things, eliminating the absolute priority rule in a cramdown situation, Congress in 2019 intended to reintroduce all the problems with exceptions to the discharge of a corporation that it eliminated over 50 years earlier." Bonapfel, *supra,* at 237. This Court finds Judge Bonapfel's reasoning persuasive and adopts it here.

The Fourth Circuit then observed that § 523(a)'s limitation to individuals is difficult to reconcile with § 1141(d)(6)'s reference to § 523(a) and its instructions that it applies only to corporate debtors. ***In re Cleary Packaging, LLC,*** 36 F.4th at 516. The Fourth Circuit points out that § 1141 is also present in § 523(a)'s limiting preamble. ***Id.*** In other words, the Fourth Circuit takes the position that if the phrase "of a kind" in § 1192(2) incorporates 523(a)'s limiting language, then the same phrase in § 1141(d)(6) must also limit § 523(a)'s incorporation in § 1141(d)(6) to individuals. According to the Fourth Circuit, this interpretation would render § 1141(d)(6)'s application to only corporations meaningless. ***Id.***

The context in which §§ 1141(d)(6) and 1192(2) operate resolves this tension, to the extent it exists. Section 1141(d)(6) references specific subparagraphs of § 523(a)(2), and only provides an exception to discharge for debts from certain entities. 11 U.S.C. § 1141(d)(6) (excepting from discharge debts under § 523(a)(2), but only as to debts to governmental entities). Section 1192(2), in contrast, applies § 523(a) more broadly. There are no limitations placed on how § 523(a) would apply to a potential corporate defendant. The Court, therefore, agrees with Judge Bonapfel that the context of the statutes "make[s] it appropriate to interpret the same words differently." Bonapfel, *supra,* at 219.

The Fourth Circuit further supported its position by analogizing Chapter 12's language in § 1228(a) to the language of § 1192(2) by citing two cases which analyze the language in § 1228(a) and hold that the § 523(a) exceptions to discharge it contains are applicable to both corporate and individual debtors. *See* ***In re Cleary Packaging, LLC,*** 36 F.4th at 516 (citing ***In re JRB Consolidated, Inc.,*** 188 B.R. 373; ***In re Breezy Ridge Farms, Inc.,*** 2009 WL 1514671). Because the language of § 1228(a) and § 1192(2) are "virtually identical", then the Fourth Circuit reasons that the two provisions should be interpreted ***349** the same way. ***Id.*** One of the cases the Fourth Circuit relies on is this Court's prior ruling in ***In re JRB Consolidated, Inc.*** 188 B.R. 373. As analyzed above, this Court does not believe that the same result is mandated despite the similar language in Chapter 12, primarily because "§ 1141(d) distinguishes between individual and corporate discharges." Bonapfel, *supra*, at 224. As one of the bankruptcy courts remarked, "[t]he lack of such distinction within Chapter 12 considered in conjunction with the narrowly circumscribed type of entity that may be a Chapter 12 debtor renders analogy between the two discharge provisions unpersuasive." ***In re Cleary Packaging, LLC,*** 630 B.R. at 472, n. 9 (quoting ***United States ex rel. Minge v. Hawker Beechcraft, Inc. (In re Hawker Beechcraft, Inc.),*** 515 B.R. 416, 430 (S.D.N.Y. 2014)). This Court likewise finds any comparison between Subchapter V and Chapter 12 unavailing.

The Fourth Circuit next argued that its interpretation is grounded in the purposes of Subchapter V as contrasted by Chapter 11 procedures more broadly. The Fourth Circuit observed that Chapter 11 explicitly makes distinctions between discharge provisions applicable to individual debtors and discharge provisions applicable to corporate debtors. The discharge provision of Subchapter V, however, "provides benefits to small business debtors, regardless of whether they are individuals or corporations." ***In re Cleary Packaging, LLC,*** 36 F.4th at 517. Therefore, the Circuit concluded, "an important purpose for Subchapter V would be frustrated" if the bankruptcy court's interpretation were given effect. ***Id.***

This Court finds this argument puzzling. Exactly what purpose would be frustrated by keeping with the decades-long policy of exempting entities from discharge exceptions under § 523(a) is unclear. In fact, this Court believes that it is the Fourth Circuit's opinion that would frustrate the entire Chapter 11 statutory scheme. Because making § 523(a) applicable to corporations is such a deviation from the common understanding of the Bankruptcy Code, Subchapter V's inclusion in Chapter 11 becomes less fitting. Had Congress intended that Subchapter V operate differently in this way, it could have created a new chapter of bankruptcy for small businesses. Nonetheless, Congress chose to include Subchapter V into the broader Chapter 11 scheme. This Court views this choice as instructive. Moreover, the practical effect of making § 523(a) applicable to corporations in Subchapter V cases, but not in traditional Chapter 11 cases would disincentivize corporations from availing themselves of the benefits of Subchapter V. The idea that Congress would aim to create a simpler option for a corporation to pursue bankruptcy while simultaneously implementing impediments to that debtor achieving a discharge of its debts defies reason.

Finally, the Fourth Circuit defended its view by invoking fairness and equity principles. The court recognized that, with the elimination of the absolute priority rule, creditors' rights have been altered in Subchapter V. According to the Fourth Circuit, this means that Congress must have intended § 523(a) to apply to all debtors as a way of counteracting this change in treatment. The Fourth Circuit summarized its position this way: "[g]iven the elimination of the absolute priority rule, Congress understandably applied limitations on the discharge of debts to provide an additional layer of fairness and equity to creditors to balance against the altered order of priority that favors the debtor." ***Id.***

This Court observes that in general unsecured creditors in a Subchapter V corporate case are benefitted, not harmed, by ***350** shielding the debtor from having any debts deemed nondischargeable. For example, if a debtor carries a nondischargeable debt, the debtor would be wise to seriously consider converting to a Chapter 7 liquidation. Unsecured creditors generally receive less under a liquidation than under a feasible plan because liquidation "results in competition for available funds between unsecured creditors with dischargeable debts and those with nondischargeable debts." Bonapfel, *supra,* at 234. The bad news for those creditors whose debts are dischargeable is that "every dollar paid on the nondischargeable debt in excess of a pro rata share of disposable income is a dollar that is not paid to unsecured creditors generally." *Id*. In the end, the courts may be met with mounds of dischargeability actions from creditors all seeking to have their debts deemed nondischargeable. This strikes the Court as a loss for everyone involved. Consequently, the Court is unconvinced by the Fourth Circuit's fairness argument.

For the foregoing reasons, the Court disagrees with the Fourth Circuit's decision in ***In re Cleary Packaging, LLC,*** and joins its sister bankruptcy courts in holding that corporate Subchapter V debtors should not be subject to § 523 dischargeability actions. Accordingly, Avion's claims against GFS under § 523(a)(2) are dismissed with prejudice under Rule 12(b)(6).

III. ***Claims Under § 727(a)***

[10] Avion also brings three claims under § 727(a) seeking a determination that GFS be denied a discharge of any debts. Specifically, Avion alleges causes of action under § 727(a)(3), (4), and (5) respectively. GFS, in its Motion to Dismiss, argues that these claims should be dismissed as a matter of law because § 727 applies only to Chapter 7 proceedings. In response, Avion argues that § 1141(d)(3)(C) incorporates § 727 into Chapter 11 proceedings, and thus GFS is subject to its discharge exclusions. Interestingly, the Motion to Dismiss does not contest the plausibility of the § 727 claims as pled, instead focusing solely on the inapplicability of § 727 and seeking dismissal of those claims as a matter of law. Consequently, the Court determines that the § 727 claims are sufficiently pled and will tailor its analysis to the applicability of § 727 to Chapter 11.

[11] Section 727 of the Bankruptcy Code governs discharge in Chapter 7 cases. Specifically, subsection (a) of § 727 governs the exceptions to discharge. Most often, § 727 is invoked when a creditor, in a Chapter 7 proceeding, seeks a determination that the debtor should not be entitled to a discharge of any of its debts. Avion is correct in asserting that § 1141(d)(3)(C) incorporates the conduct that would deny a debtor's discharge under § 727 into Chapter 11 cases. Section 1141(d)(3)(C) states: "(3) the confirmation of a plan does not discharge a debtor if—...(C) the debtor would be denied a discharge under section 727(a) of this title if the case were a case under Chapter 7 of this title." The plain language of this provision imports § 727 liability into Chapter 11 cases. To the Court's way of thinking, § 1141(d)(3)(C) asks a court to treat the Subchapter V case as if it were a Chapter 7 case and measure the debtor's conduct against the list of nondischargeable actions in § 727(a).

What Avion ignores, however, is that § 1181(c) makes § 1141 inapplicable to this particular case because the confirmed plan is nonconsensual. Section 1181(c) states: "[i]f a plan is confirmed under section 1191(b) of this title, section 1141(d) of this title shall not apply, except as provided in section 1192 of this title." Here, the Court confirmed GFS's plan of reorganization under § 1191(b) because it was a nonconsensual ***351** plan. Consequently, § 1181(c) operates to make any subsections of § 1141(d) inapplicable, including § 1141(d)(3)(C), the vehicle used by Avion to import § 727 liability. There is no provision in § 1192 that would reinstate § 1141(d)'s applicability to the case.

Even if § 1141(d) was in play here, § 1141(d)(3)(C) is only one element of the broader provisions of § 1141(d)(3). Notably, the other two elements are not met here. Section 1141(d)(3) as a whole states,

> [t]he confirmation of a plan does not discharge a debtor if (A) the plan provides for the liquidation of all or substantially all of the property of the estate; (B) the debtor does not engage in business after consummation of the plan; and (C) the debtor would be denied a discharge under section 727(a) of this title if the case were a case under Chapter 7 of this title.

11 U.S.C. § 1141(d)(3)(C). The word "and" is critical because it operates to create an all or nothing proposition.

Here, GFS's Subchapter V plan does not contemplate liquidating property of the estate, and the business will continue to operate past the confirmation of the plan (as a means to fund the plan). These two circumstances leave § 1141(d)(3)(A) and (B) unsatisfied and thus render (C) inoperative. Because Avion relies on § 1141(d)(3) to import § 727 liability to GFS, all subsections of § 1141(d)(3) must be present for § 727 to apply here. Since at least subsections (A) and (B) are inapplicable, it follows that § 727 is also inapplicable.

[12] Furthermore, even if § 727(a) did apply to this case, it does not apply to entities by virtue of its language. Section 727(a)(1) explicitly excepts non-individual debtors from discharge under Chapter 7. ("The court shall grant the debtor a discharge, unless—the debtor is not an individual"). The other eleven subsections of § 727 describe conduct that would make a debtor ineligible for a discharge. If the other subsections were intended to include non-individual debtors, there would be no need to specifically exclude non-individual debtors at the outset of § 727. The Court again declines to offer an interpretation that renders part of the statute superfluous. Scalia & Garner, *supra,* at 174. Accordingly, the Court determines that § 727's limits on dischargeability do not apply to GFS insofar as GFS is not an individual debtor. Therefore, all causes of action under § 727 shall be dismissed under Rule 12(b)(6) for failure to state a claim upon which relief can be granted.

IV. ***Claim Under § 1141(d)(3)***

Similarly, the Court dismisses Avion's claim under § 1141(d)(3) for failure to state a claim upon which relief can be granted. Although the Court believes that Avion's complaint is factually sufficient to support a claim, it fails as a matter of law for two reasons. First, § 1141(d)(3) does nothing more than incorporate § 727 dischargeability claims into liquidating Chapter 11 cases. As such, there is no independent dischargeability claim under this statute. As just discussed, § 727 does not apply to GFS and thus Avion's reliance on § 1141(d)(3) for a dischargeability claim does not state a claim upon which relief can be granted.

Second, as discussed with regard to the § 727 claims, the provisions of Subchapter V render § 1141(d) inapplicable to this case. Again, because the confirmed plan here is nonconsensual, § 1181(c) becomes operative, thus eliminating § 1141(d) from use in this case. Therefore, Avion's dischargeability claim under § 1141(d)(3) is legally insufficient to proceed and must be dismissed under Rule 12(b)(6).

CONCLUSION

For the foregoing reasons, the Court holds that corporate debtors electing to ***352** proceed under Subchapter V of Chapter 11 are not subject to complaints to determine dischargeability pursuant to § 523(a). Additionally, §§ 727 and 1141(d) are not applicable in this case and do not provide a basis for a dischargeability action against GFS here.

Accordingly, IT IS ORDERED that Defendant's First Amended Rule 12(b)(6) Motion to Dismiss Plaintiff's Complaint (ECF No. 6) is GRANTED.

IT IS FURTHER ORDERED that Plaintiff's Original Complaint for Determination of Dischargeability of Debt Pursuant to 11 U.S.C. § 523(a)(2) & (4) (ECF No. 1) is DISMISSED WITH PREJUDICE to refiling.

All Citations

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Footnotes

1 "ECF" denotes electronic filing docket number.

2 Unless otherwise indicated, all section references are to Title 11 U.S.C.—— *et. seq.*

3 The Court recognizes that another interesting and unsettled issue underlies the issues presented: whether transactions classified as "Merchant Cash Advances" like the one here are considered sales or loans. In its briefing, Avion describes the transaction as a sale of receivables, while simultaneously seeking to have its "debt" deemed nondischargeable. With MCAs becoming increasingly common, the Court may be presented with this issue at some point in the future but will not answer the question in this decision.

4 This conclusion is further supported by the existence of this adversary. If Avion did not believe that GFS could receive a discharge, there would be no reason for Avion to file a dischargeability action. Although this issue was not briefed, it bares stating as the provisions of Subchapter V continue to be scrutinized throughout the court system. The Court believes clarification regarding the issue is important and fundamental to the analysis here.

5 The Court notes that because § 1141(d)(6) explicitly applies to corporations, GFS could face potential liability under this statute. § 1141(d)(6), however, only excepts debts under § 523(a)(2) to governmental entities. Here, GFS's debt to Avion is not governmental in nature and thus § 1141(d)(6) would not apply to the debt owned by Avion.

6 While the Court generally is hesitant to rely on legislative history, Judge Paul Bonapfel points out that neither the Report of the Judiciary Committee of the House of Representatives nor testimony given to the Committee regarding § 1192 acknowledged any expansion of the existing Chapter 11 corporate discharge exceptions. Hon. Paul W. Bonapfel, Guide to the Small Business Reorganization Act of 2019, (2022), https://www.ganb.uscourts.gov/sites/default/files/sbra_guide_pwb.pdf at 204-205. Bonapfel points out that had Congress intended to make a seismic change to existing Chapter 11 law, one would expect the House Judiciary Committee Report to have pointed out this change. *Id.* at 205. The fact that it did not is further evidence that Congress did not intend § 523's discharge exceptions to apply to Subchapter V corporate debtors.

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